

THE RHA REVIEW

ROUTE TO:

Vol. 12, No. 2, First Quarter 2006

A publication of Robert Hughes Associates, Inc., an international litigation support, actuarial, risk management and insurance consulting company.

Post-Katrina

By Amy v. Puelz, Ph.D. and Bob Puelz, Ph.D.

After a natural disaster such as Katrina, many individuals and businesses finally call upon the language of their insurance policies to speak to the issue of whether damage suffered is covered and, if so, how much will the insurer pay? If the insurer does pay, the question of how insurance rates and contracts will be affected by catastrophic claim payouts is of concern. Historically, negative public perceptions of "insurance" and "claims adjusters" have been reinforced by consumers once they learn that their policies don't pay or their claims will be contested by their insurers. The possibility of being priced out of coverage, or of having no available coverage in future years if large payouts do occur, adds to negative perceptions.

Consumers seem to forget that the very purchase of insurance yields a benefit even if a claim is never filed. While it is true that a benefit of insurance may be its anxiety-reducing feature prior to a loss, it is only a textbook benefit for many consumers who may have to buy insurance originally because of a third-party mandate, whether it is their lender or the law. Anecdotally, post-claim is when the benefits of insurance are measured by most; thus claim denial can be a particularly emotional event for those who are uninformed or uneducated about their insurance contracts. One outcome of the information gap is that litigation often follows among asymmetrically informed parties, leaving the issue of fairness to the court.¹

What is the current state of fairness, and how might it apply to potential

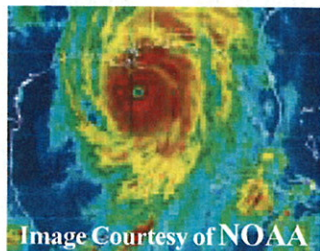


Image Courtesy of NOAA

claimants who were in the path of Katrina? The vast gray area of how a claim is appropriately handled is of interest not only to those affected by the hurricane tragedy but to all since if one has no insurance for the assets destroyed by Katrina, the only recourse

is governmental or charitable reimbursement. How might that gray area be defined? To begin, we note that the gray area has a fluid boundary depending on insurance contractual language vis-à-vis the actual event. If a peril is defined simply as a "hurricane," then an insurer might rightfully argue that a hurricane is not insured under a contract when "hurricane" is not listed as a covered peril or is specifically excluded. However, if a claimant reasonably believed that a hurricane was a covered peril within the complicated insurance contract, should the insurer be required to cover losses due to a hurricane?

The distinction between flood and wind is important in the Katrina context and is not a trivial concern to most claimants. Policyholder claimants who read their property insurance contracts will likely find that wind damage is covered but flood damage is specifically excluded. For the latter coverage to explicitly exist, a supplemental contract, issued in conjunction with the National Flood Insurance Program (NFIP), should have been purchased. Whether coverage implicitly exists is the issue left to the courts. While the insurance industry is careful to assert that the relevant insurance contract does not cover and never has covered floods, particular claim scenarios are often more complicated.² Thus, as noted recently by Adam Scales, insurance contracts are complex. The courts often bring a reasonable-expectations doctrine to coverage interpretation, and once these elements are brought to bear on specific facts, policyholders usually receive the benefit of the doubt.³ Scales also points

(Post-Katrina, continued inside)

Litigation Support: Maximizing Value from your Consultant

By Burl Daniel, CPCU, CIC, CRM

Insurance attorneys are busy people! No two litigation cases are the same! No secrets here. As insurance litigation consultants, we find this particularly true of both the defense and plaintiff trial lawyers who retain us. Attorneys face weekly court filings, deposition schedules, and/or courthouse deadlines. Below are a few ideas which might help attorneys involved in insurance litigation obtain better value from the fees paid for their witnesses' expertise and services.

Expert reports:

It is not unusual to receive calls from attorneys needing expert report/opinion letters within 3 to 7 days. I personally have been asked to review 500 to 600 pages of documents; do peripheral research; join conference calls with the attorney, the client, and other parties involved; and produce my expert report post haste. While we can and do provide such short-fuse reports, we simply cannot do our best work trying to complete what may be a 40-hour project in 12 to 15 hours.

Reasonable lead time allows us to ask better questions, better analyze the data, seek additional information, and provide the attorneys with our best report possible ... not so different from when attorneys prepare a case for mediation or trial. Attorneys know how proper preparation improves their overall case presentation to the mediator, arbitrator, jury, or judge. We understand that attorneys live and die by turnaround time. We are simply suggesting that with moderate lead time, we can reduce cost and improve your odds at the courthouse.

(Maximizing Value, continued inside)

IN THIS ISSUE:

- **Post-Katrina**
- **Maximizing Value**
- **From Near and Far**
- **New Team Member**

(Post-Katrina, continued from cover)

out that courts tend to find for the claimants when a covered cause contributes damage, even though an uncovered cause has also contributed.

The impact of Katrina on coverage rates and contract language is of concern to the broad spectrum of insurance consumers. Although insurers cannot adjust present rates to make up for Katrina losses, they may have the economic need to adjust rates based on the new loss severity and probability information. Thus it is likely that consumers in hurricane-prone areas will find new coverage rates higher than pre-Katrina rates. How insurers interpret this new loss information and how they allocate its impact may result in state regulators and/or legislators stepping in and arguing against rate adjustments. The balancing process between the insurer's economic viability of selling insurance in a particular area and the political pressures to keep coverage affordable for consumers will likely play out in the courts. We only need to look at the recent problems with homeowners' insurance in Texas to know the importance of weighing the benefits of market solvency versus the costs of increasing insurance prices.

Additionally, courts will most likely play the primary role in determining an insurer's coverage liability for excluded flood damage when normally included wind damage plays a role in the economic loss.⁴ The gray area will be defined case by case and state by state, and these results will set a precedent for future storms. We anticipate that if the insurers' liability regarding flood damage is significantly increased as a result of legal action resulting from Katrina, the effect will be broad-based without regulatory intervention. Publicly, the industry has acknowledged that if insurers are compelled by the courts to pay for flood damage, "insurance prices around the country will have to rise."⁵

As stakeholders in post-Katrina insurance outcomes assemble, we think there are a few pertinent questions relevant to potential litigation.

1. When the insurance contract was entered into, did the insurer require the policyholder to acknowledge an understanding of the contract and its covered perils?

2. When the insurance contract was entered into, did the policyholder know about the existence of the NFIP? If so, what was the policyholder's understanding of why the NFIP exists?

3. In a press release by the Insurance Information Institute, there is a statement that "the insurance industry will fulfill its commitment to its customers." How is the commitment understood by the consumer? Moreover, did insurance consumers receive representations from their insurers about coverage or commitment?

In addition to these questions, it may be of use to take a more scientific approach to the issue of predicting claim outcomes

"We anticipate that if the insurers' liability regarding flood damage is significantly increased as a result of legal action resulting from Katrina, the effect will be broad-based without regulatory intervention."

before litigation is pursued. Both insurers and legal representatives have a vested interest in the results of such an approach.⁶ From an insurer's perspective, the attributes of settled claims vis-à-vis litigated claims may yield important insights into practical claim-settlement strategies. Whether claimants should value litigation ultimately comes down to the chances that possible benefits exceed the cost of pursuing litigation. Knowledge of those factors that are correlated with successful litigation will be extremely useful.

In sum, current and future litigation in courts post-Katrina will no doubt have a significant impact on all aspects of the insurance market. The scope and future of federally funded programs such as the NFIP, and the legal ramifications of excluded causes of loss in insurance contracts, may reshape the market. Beyond the courts, however, it is apparent

that contractual innovations and partnerships between public and private parties are necessary to create workable solutions for future catastrophic events such as Hurricane Katrina. Equitable knowledge of the risks in a contracting relationship is a reasonable goal to be pursued. **RHA**

Footnotes

¹Mediation opportunities sanctioned by the regulatory authority of Louisiana (http://www.lidi.state.la.us/whats_new/Hurricane%20Mediation%20Program%20brochure.pdf) and Mississippi (<http://www.doi.state.ms.us/katrina/mediationqa.pdf>) do exist.

²As stated by the industry, "Flood losses have never been covered under any homeowners insurance policy." See http://www.disasterinformation.org/disaster2/facts/katrina_faqs/.

³See http://writ.news.findlaw.com/commentary/20050919_scales.html.

⁴Mississippi filed a complaint seeking to void homeowner policy flood exclusions (<http://www.ago.state.ms.us/insurance.pdf>).

⁵See http://www.iii.org/media/hottopics/additional/katrina_faqs/.

⁶"The Effect of Legal Rules on the Value of Economic and Non-Economic Damages and the Decision to File," Mark Browne and Robert Puelz, *Journal of Risk and Uncertainty* (August 1999) 18: 189-213.

Dr. Amy Puelz is an associate consultant with RHA, Inc., specializing in risk assessment and financial modeling. Her Ph.D. areas combine management science and finance, and she has served as a faculty member at Emory University, the University of Memphis and Southern Methodist University.

Bob Puelz is the Dexter Professor of Risk Management and Insurance in the Cox School of Business at Southern Methodist University, and is a member of the Real Estate, Insurance and Business Law faculty. He holds BS and MA degrees from the University of Nebraska and a Ph.D. from the University of Georgia. At Cox since 1992, he has consulted on issues surrounding Lloyd's of London, insurance agency valuation, life insurance contract interpretation, and insurance business standards and practices.

(Maximizing Value, continued from cover)

Preparing for deposition:

We usually can provide you the best value as your "consulting expert" well before depositions begin. We are not attorneys providing legal advice. We do not practice law. We do not represent clients as their legal counsel. However, we can provide a depth of technical knowledge in each consultant's particular area of insurance expertise. We can assist attorneys with technical insurance-deposition questions. We may also be able to suggest coverage or claim areas to avoid or downplay, depending on the insurance issues in question. We can serve as a sounding board for industry-practices issues and insurance-agency practices issues, and we very likely have experience with cases similar to the case at hand.

I have read several depositions in which the questions being asked explored insurance coverage having little or no bearing on the case at hand. In nearly all these cases, a 15-30 minute discussion with an expert before these depositions were taken could have helped the attorneys focus their effort. When you have the luxury of any time and can give us an advance snapshot of case facts, basic case documents, and even a short bit of review time, we can usually help you focus

deposition questions ... focused on the most likely applicable coverage parts and focused to avoid areas not likely to help your client's case.

We filter through technical insurance issues, thus freeing attorneys to focus on the legal aspects and the strategy of the case. As consulting experts we can help focus an attorney's deposition preparation in many areas. For example:


- Subtleties of coverage analysis
- Background of insurance agency operations
- Carrier claims procedures/standards
- Comparison of claims-made vs. occurrence forms
- Suggestions about additional insurance coverage areas which may apply.

Who pays the freight?

Plaintiff attorneys often front litigation costs and may be repaid only if their clients prevail. Defense attorneys normally bill hourly fees, court costs, and other legal costs (including expert fees) to the insurance carrier or insured. In either case, but perhaps more importantly, for the attorney working on a contingency fee, it is important to properly assess the likelihood of prevailing before significant cost commitments are made.

Perhaps the worst scenario occurs when one side had either a very difficult case or virtually no chance to prevail from the outset of litigation, or when it thought it was bulletproof. By the time the party discovers that it is not indeed bulletproof a lot of time and money have gone down the drain. While we could never predict with certainty any final decision a mediator, arbitrator, jury, or judge might make, it is likely that our experience could greatly reduce the uncertainty of the situation. One of our consultants has likely seen a case (or cases) similar to the one at hand. A short telephone call early in the game can suggest when/where:

- Additional coverage might be available
- The policyholder simply does not have coverage
- The insurance company's denial was ill-considered
- Your policyholder might have coverage under some other policy
- An agent "did/did not" perform prudent service in analyzing client needs
- Opposing counsel may be confused as to the "insurance coverage" facts

We appreciate being considered and/or retained to join a litigation support team. The simple ideas above should streamline the process and provide the attorneys involved with better value for the fees they pay. 

FROM NEAR AND FAR



According to the Insurance Information Institute, homeowners' insurers have settled almost 70 percent of claims in Mississippi and Louisiana arising out of Hurricane Katrina. The I.I.I. estimates that more than 700,000 claims have been settled in these states. These claims are said to amount to more than \$11 billion.



It is estimated that insurers will handle about 1.75 million claims related to Hurricane Katrina in Alabama, Florida, Louisiana, and Mississippi alone, and more than one million claims arising out of hurricanes Rita, Dennis and Wilma. Rita claims are centered in Texas and Louisiana, while the majority of claims from Dennis and Wilma's damage are in Florida.

Mr. Daniel has a broad range of insurance industry experience. He has been in the insurance business for 32 years, 25 of which have been as an agent. He completed his agency career as senior vice president with Frost Insurance Agency in Fort Worth, Texas. A sampling of Mr. Daniel's clientele includes oil jobbers, manufacturers, the distribution industry, construction, trucking, and insurance companies.

ROBERT HUGHES ASSOCIATES INC.

508 TWILIGHT TRAIL, SUITE 200
RICHARDSON, TEXAS 75080
(972) 980-0088 FAX (972) 233-1548

PRSRT STD
U.S. POSTAGE
PAID
RICHARDSON, TX
PERMIT NO. 1380

ADDRESS SERVICE REQUESTED

New Member of the Team

Christa Meyer Hinckley has become an associate with RHA. Ms. Hinckley has a very strong insurance and risk-management background, with special emphasis in aviation. She was a senior attorney with AMR Corp., parent company of American Airlines, for eight years, followed by seven years as Managing Director – Insurance and Risk Management for AMR. She was most recently Global Runoff Claims Leader for GE Employers Reinsurance Corp.

Ms. Hinckley is currently in private law practice and serving as a consultant. She will provide consulting and expert witness services in many areas, including but not limited to transportation industry insurance and litigation; multiparty, multi-jurisdictional/international litigation; global crisis management; complex global insurance programs and coverage issues and mergers; and acquisitions and international transactions. 

THE RHA REVIEW

Publisher Robert N. Hughes
Editor John R. Oakley
Assistant Editor Alice H. Oakley

The RHA Review is published quarterly by Robert Hughes Associates, Inc. — an independent international litigation support, actuarial, risk management and insurance consulting company based near Dallas, Texas, with offices in Houston, Texas, and London, England. The purpose of this publication is to offer insurance-related information and critical comment pertinent to the clients, friends and fellow professionals of Robert Hughes Associates, Inc. This publication is available free to interested parties. The information contained in this publication is intended to be general in nature; readers should obtain professional counsel before taking any action on the basis of this material.

For more information, contact
John R. Oakley, Editor
508 Twilight Trail, Suite 200
Richardson, TX 75080
Tel. (972) 980-0088.

Copyright © Robert Hughes Associates, Inc.,
2006. All rights reserved.