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Thinking About Switching Insurance Companies?

Five Questions to Ask Before You Do

By Cort T. Malone


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In the current economic climate, it is wise for policyholders to take stock of their insurance portfolios and consider whether a change in insurance companies would be beneficial. While re-examining existing insurance is a step in the right direction, risk managers cannot make an informed decision without considering several key issues, including *limits, additional layers, claims handling history, mandatory policy clauses, pre-existing conditions, and pitfalls of a new application process.*

Limits: Do You Have the Right Amount of Coverage?

The first step for a risk manager planning to collect information about the offerings of various insurance companies is to gather and review all relevant internal information about potential liabilities to determine whether current insurance limits provide sufficient coverage. This can be accomplished through a combined review of past litigation expenses and any new business operations or risks that have arisen since the last insurance purchase or renewal. Companies often find that recent developments or projects have increased potential liability while insurance limits remained the same—leaving a coverage gap that could prove ruinous. By testing the insurance market, you may find that you can obtain greater limits for the same (or even lower) premiums. In contrast, some insurance companies require a "cap" on the limits available for certain types of insurance—which leads directly to the next issue.

Additional Layers: Should You Consider Excess or Umbrella Coverage?

A policyholder may decide against increasing its primary layer limits and instead purchase excess or umbrella coverage above the limits of the primary insurance policy. Excess/umbrella coverage provides greater limits for potentially catastrophic exposures—often at a relatively low premium—because the coverage does not kick in until exposure reaches a high level. When deciding between increasing primary limits versus obtaining excess/umbrella coverage, carefully review the specific policy terms because primary and excess/umbrella insurance often have significant differences, such as whether defense costs are covered.

> ***"Insurance is worthless if it doesn't pay claims, and some [insurance] companies seek to avoid or lessen their obligations through certain policy terms."***

Claims Handling History: Have Your Experiences Been Positive or Negative?

Switching insurance companies and programs is not merely a by-the-numbers decision because each insurance company has its own way of dealing with claims. Indeed, a policyholder should regard its past claims handling experiences with its current insurance company as a key factor in deciding whether to switch. Were previously submitted claims paid promptly or otherwise treated fairly? Insurance is worthless if it doesn't pay claims, and some companies seek to avoid or lessen their obligations through certain policy terms.

Mandatory Policy Clauses: Are They Limiting Your Options?

One example of an undesirable policy term is a mandatory arbitration provision, which could

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allow your current insurance company to force you to arbitrate claims for which coverage seems to be clearly provided under the policies at issue. Under such arbitration clauses, companies faced with any potentially large exposures that should be covered under their policies may be faced with only one recourse if their insurance companies deny coverage—an arbitration proceeding. Other policies may not contain an arbitration requirement, but specify that the law of a particular jurisdiction must apply should litigation occur. Typically, the jurisdiction chosen by the insurance company will be one in which the law is unfavorable to policyholders. When deciding whether to change insurance companies, consider arbitration and/or mandatory jurisdiction clauses a strike against any insurance company that insists upon them.

"Pre-existing" or "Known" Conditions: Do You Know Your Risks?

The term "pre-existing condition," widely associated with health insurance, may be applicable to a manufacturer or other corporate entity that has certain types of potential liabilities such as pollution risks or suits brouiagtght by shareholders. There is a common insurance policy exclusion for "pre-existing conditions" known to a "responsible insured" but not disclosed or identified in new policy applications. This type of exclusion can make it very difficult to secure coverage for certain risks.

If you lack a complete inventory of your company's "known" potential liabilities, your company may fall victim to these exclusions. It is therefore crucial to undertake a yearly evaluation to ensure awareness of any and all potential risks, including new liabilities, and to report the findings to your insurance company. Because insurance companies require that policyholders detail all of their potential risks, including any known, pre-existing conditions, the only way to be protected from coverage denials is to stay one step ahead by being cognizant of your own liabilities, informing your insurance companies about them, and keeping detailed records of those communications.

Avoiding the Pitfalls of a New Application Process

The "pre-existing conditions" exclusion highlights an additional risk inherent in switching insurance companies. A change in insurance companies always requires filling out entirely new application materials, which entails a risk of forgetting to include critical information. Though you might think that an error as simple as leaving off one particular item, such as a location on a schedule of proposed insured properties, should only prevent coverage for that location, it is entirely possible that an insurance company will seek to rescind an entire policy based on one innocent mistake in the application. One way to prevent this from happening with respect to scheduled locations is to request that your new policy include a clause broadening coverage to include inadvertently omitted sites. Anything less may leave a company potentially uncovered for any location that it innocently failed to mention in a new policy application.

Conclusion: Think About Everything

When faced with harsh economic realities, insurance companies are likely to reexamine their claims handling processes. The resulting changes could lead policyholders to consider switching insurance companies if there is concern about the new practices of a current insurance company. Before jumping into the insurance market blindly (or based solely on the recommendations of a broker), policyholders must ask themselves a number of questions. A policyholder that understands its own insurance needs, including proper coverage limits, options for

excess or umbrella coverage, past claims handling experiences, and all potential liabilities will be much more likely to come to the correct decision regarding where to procure its future insurance coverage.

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2008 Year in Review

By Mark R. Garbowski


Mark R. Garbowski

An attorney's review of the year in insurance (or any field) would normally be expected to focus on legal developments, including new major court decisions. In 2008, however, the economic developments of the third and fourth quarters of 2008 took center stage.

Economic Contraction and Subsequent Claims

The major risk event in the economy in 2008 relates to the market loss and bank failures due to the sub-prime mortgage collapse and general financial meltdown.

Lawsuits have been instituted against investment banks, investment advisors, banks, mortgage companies and virtually everyone involved in the securitization of mortgages. Many such claims may be covered under standard insurance policies already purchased prior to the financial crisis. Policies already purchased may cover costs of defending the lawsuits and costs of settlements or judgments in the lawsuits.

Depending on the lawsuit, coverage may be found in Directors & Officers (D&O) insurance coverage, professional liability (E&O) insurance coverage, fiduciary liability insurance, or financial institution bonds (FI bonds). Each of these policies cover the corporate policyholder and its managers, officers, and general partners against losses due to unintentional or negligent acts, errors, omissions or fraud.

Insurance Industry Bailout(s)

In September, the Federal Government provided a substantial bailout package to American International Group, Inc. (AIG), the parent company to a vast family of companies whose primary business is selling insurance products. The terms of the deal have and the amount of money involved has changed, and increased, since the original deal. As part of the deal, the government is set to obtain a significant equity stake in the company. Rumors of financial difficulty have surrounded certain other commercial insurance companies. Many policyholders are prudently checking the soundness of all their insurance providers as they renew for the coming year. The AIG situation also brought attention to Credit Default Swaps—a product similar to insurance but subject to considerably less regulation.

Legal Developments

Even with all of the above, most attorneys cannot resist noting some of important legal developments in their field. The following is not comprehensive, but does cover some of the highlights:

As noted previously in this space, New York has had three important developments in insurance law in 2008. The first was the decision in the *Bi-Economy* case that allowed policyholders in New York to recover consequential damages from their insurance company, a right long enjoyed by policyholders in other jurisdictions. The second New York development was the *Elacqua v. Physicians' Insurers* decision ruling that an insurance company's failure to advise a policyholder of a right to independent counsel violated New York's deceptive business acts and practices law, specifically General Business Law § 349. The final New York development was the passage of

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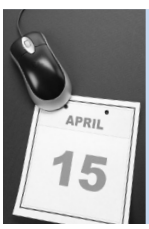

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a bill to relax—in certain circumstances—New York's very strict rules that allow insurance companies to avoid coverage when notice of a claim or occurrence is late, even if the insurance company was not prejudiced by the delay. New York has now joined the majority of states in imposing a prejudice standard for late notice denials when the statute applies.

Other states had significant Supreme Court decisions regarding insurance issues. Two come from Texas:

In January, the Texas Supreme Court similarly rejected the rule that prejudice is irrelevant to late notice and held that "an insured's failure to timely notify its insurer of a claim or suit does not defeat coverage if the insurer was not prejudiced by delay." P*AJ, Inc. v. The Hanover Insurance Company*. The next month, the Texas Supreme Court ruled in *Fairfield Ins. Co. v. Stephens Martin Paving, LP.*, that Texas public policy does not bar insurance coverage for punitive damages under some types of workers' compensation and employer's liability insurance.

Maine's highest court issued an important decision on insurance company efforts to rescind policies based on alleged misrepresentation in the policy application. To succeed in such an effort, the Court ruled, in *Liberty Ins. Underwriters, Inc. v. Estate of Faulkner*, that an insurance company must prove fraud, including the elements of materiality and actual reliance on the misrepresentation by the insurance company. On the other hand, the insurance company can rescind even if the material misrepresentation was made in an earlier policy application for which the current policy was a renewal. Even if the renewal application did not include the misrepresentation, the insurance company can be entitled to rescission.

In Washington, that state's highest court ruled in October that an insurance company is bound by the factual findings of a reasonable settlement of an underlying liability claim when a coverage determination depends upon those same facts. In *Mutual of Enumclaw Insurance Co. v. T&G Construction Inc. and Villas at Harbour Pointe Owners Association*, the Washington Supreme Court determined that a good faith settlement establishes the policyholder's damages even when the insurance company has not acted in bad faith, and noted that several other state courts agreed.

Mark Garbowski is a senior shareholder and member of Anderson Kill's insurance recovery group, with particular experience in professional liability insurance, directors and officers (D&O) insurance, fidelity and crime-loss policies, Internet and hi-tech liability insurance issues.
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