Controlling Expenses—Best Practices for Containing Claim Costs

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A Senior Vice President at a casualty insurance company recently expressed alarm at the increasing costs of defending cases in litigation. The reasons were varied but included upward claim severity trends and increasingly aggressive plaintiff attorneys. Discussions with other claim professionals have likewise indicated ongoing concern for managing defense costs. Whatever the cause of rising litigation spending, claims departments are looking for ways to contain costs while maintaining high quality representation.

Claim costs are a concern in all lines of business, but may be more acute for some. In the Medical Professional Liability line, for example, cases often involve significant injury and complicated medical issues requiring multiple expert evaluations. With the professional reputations of their insureds on the line, companies can spend large sums in legal and expert fees working up their cases, followed by more at trial should a defense posture be taken. “Nuisance value” settlements are uncommon.

While defending claims is an inevitable cost of doing business, carriers should continually evaluate their management of expenses and ensure their dollars are being used efficiently. We offer some thoughts on where savings can be found.

The Role of Risk Management in Reducing Costs

Before discussing expense control after the claim has arisen, it would be prudent to first consider the important role of risk management in preventing claims in the first place. To that end, claims and risk management departments should share information and coordinate their efforts. Problematic claim trends addressed...
through effective risk management efforts at the front end will result in fewer claims and lower loss and expense costs on the back end.

At the heart of risk management is increasing awareness among insureds. Sharing stories from claims—case-based learning—can have a significant impact on insureds as they learn of circumstances that led to frequent or severe outcomes. Closed claims where the identities of the parties and case facts are sufficiently altered to preserve anonymity are a potentially rich source of material.

Getting this message to insureds can be done via webcasts, webinars, newsletters or live presentations. Some companies also utilize attorneys from their defense panel to present cases and highlight vulnerabilities, with the Risk Manager present to punctuate certain areas and offer solutions.

Managing Expense Costs
Once the claim has been made, and in many cases gone into litigation, what can be done to ensure expenses are kept reasonable? A better question may be, “Are there protocols in place, understood by the defense firm and monitored by the carrier, to promote efficient and focused defense counsel efforts?” Although it is the insured, and not the carrier whom the attorney represents, there should be a clear understanding by all parties as to required activities by defense counsel, reporting expectations, and required levels of communication.

Many companies use litigation budgets, in-house counsel, and litigation management guidelines. Some use annual retainers, look for the least expensive firms, or simply delete questionable charges. Others routinely roundtable select cases with defense counsel to confirm necessary further activity. Ultimately, it is up to the claims department to determine what they believe to be the most effective methods for cost control while maintaining required levels of legal representation.

We discuss the more commonly used approaches by companies to manage expense costs, as well as some additional items to consider. We have seen insurers adopt a few or many of these approaches, often with their own variations. Perhaps some of the ideas can be useful to your claim operations:

> Leverage Roundtable Discussions
> Use an Expert Database
> Decide to Settle or Defend?
> Consider an Alternative Dispute Resolution

Litigation Management Guidelines
A good best practice for a claim department is establishing and periodically reviewing written Litigation Management Guidelines that defense panel attorneys are required to follow. These usually include reporting requirements to the carrier and requesting carrier permission for certain activities such as retaining experts. It may also include limitations on time spent in certain legal tasks as well as intra-office communications that can be excessive.

This approach is effective when the guidelines have been discussed and clearly understood by carrier and counsel, with a commitment by the claims staff to monitor compliance. Still, some have argued that such guidelines may unintentionally result in a form of abandonment to counsel as the guidelines (and assumptions of compliance) are substituted for more case-specific direction. Carriers that provide defense counsel with case-specific direction, when appropriate, as an adjunct to the guidelines may be able to benefit from both approaches.

Alternative Fee Structures/Defense Counsel Budgets
Some companies have focused on reducing litigation costs by negotiating alternative billing arrangements with their panel firms. However, flat fee arrangements can result in firms being incentivized to doing the least amount of work possible. Some are now electing to use flat fees for specific tasks or budgeting for stages of the case, in essence, using sub-budgets with bonuses related to timing of case resolution.

Overall, defense counsel budgets can be helpful in holding attorneys accountable for their charges. This is effective when reviewed consistently with counsel on each case. Carriers should be mindful of the potential for bad faith against the company and professional liability against the defense attorney in the event that the insured believes the quality of their defense is negatively impacted by cost-cutting considerations.

Defense Counsel Rates and Staffing
Insurance defense rates are usually less than the “rack rate” that firms charge for other corporate work. Still, higher rates may be reasonable and necessary on select cases. This needs to be evaluated on a case-by-case basis with the right firm matched to handle the right task.
Staffing is also an important factor that impacts defense costs. The involvement of an unreasonably high number of attorneys or multiple senior partners can result in wasted time and redundant efforts driving up defense costs. Attorney staffing of a file should be discussed with the firm with clear guidelines. Efficiency should be the key in all areas. Exhaustive research on common issues well known to the firm is inefficient and wasteful, as is “drafting by committee.”

In-House Defense Counsel
Utilizing in-house defense counsel can be an effective control of defense costs if the amount of case work can justify the overhead to keep attorneys on staff. This approach is effective when in-house counsel is as equally capable as outside counsel.

Staffing an in-house program with inexperienced attorneys can result in ineffective representation of the insured (negating any cost savings), or at best focusing on more routine, less complex cases.

Tracking Costs and Performance
Some insurers track expense trends by dividing the number of cases closed in a given year by the total expense costs for those files. While this will capture expense costs over the life of the files, companies may find this method preferable to tracking the average cost per file during the year in which those costs were accrued. Other companies track average cost by firm and attorney, as well as ultimate case outcome and number of months to resolution. Of course, jurisdiction and type of cases involved will significantly impact defense costs. Still, this approach may reveal trends that the carrier may use as discussion points with their firms.

Roundtable Discussions
Meeting with defense counsel on select high exposure files to affirm case direction and promote expedient resolution can be time and money well spent. The in-depth discussions may also provide the carrier with a deeper understanding of exposure, leading to more accurate loss and expense reserving. There may be additional benefits, such as an understanding and agreement by all parties regarding necessary further work-up, an opportunity to discuss expense costs if this is a concern, and an overall opportunity to confirm claim strategy.

Expert Database
Some companies have established a database for both plaintiff and defense experts, which may include notes regarding their professional background, whether they testify solely for defense or plaintiffs, their effectiveness as witnesses, and their fees. This may assist the carrier in selecting appropriate defense experts for a given case, as well as potentially having insight into the effectiveness or formidability of plaintiff experts, both of which can impact defense costs.

Settle or Defend?
The inverse relationship between defense and indemnity costs suggests that the more vigorous the defense (and resulting higher defense costs), the less is spent on indemnity. On one side of the spectrum, some companies take a very defense-oriented stance, focusing settlement on those cases with clear or near clear liability. Other companies may prefer a more “business approach” to claim resolution by encouraging earlier settlement if feasible. This inverse relationship appears to hold true up to a point, beyond which overly aggressive claims defense can lead to the occasional surprise plaintiff verdict that negates the favorable resolution achieved on other files. Conversely, companies need to be wary of becoming targets for plaintiff attorneys by too frequently taking a “cost of defense” approach.

Companies that can quickly identify cases suitable for settlement and negotiate resolution—whether those cases are in litigation or pre-litigation—can greatly contribute to defense costs savings. Key to this is working closely with the plaintiff or plaintiff’s counsel, timely obtaining necessary records and expert reviews, and expediently evaluating damages.

Ultimately, carriers should encourage defense counsel’s activities to reach the desired case resolution. If the decision, based on proactive early investigation is for settlement, then extensive additional discovery may be unnecessary.

Alternative Dispute Resolution
One means of reducing expense costs is the use of ADR such as binding arbitration, which not only is less costly than trial, but can be concluded relatively quickly. Unlike cases that rely on
court calendars and available dates, scheduling can be done with more flexibility to include evenings and weekends. Negatives for binding arbitration include the finality of the decision, and the potential question of objectivity of the “neutral” arbitrator who may be biased towards those who would select his or her services in the future.

Outside Services
For those insurers that would like to explore outside assistance, there are a number of companies that offer such services to help benchmark and control legal costs. These companies use a variety of methods including data analytics to help their clients with legal budgeting, law firm comparisons, best practices and outcome patterns.

A Few More Considerations
A number of professional liability companies require a confidential narrative report from their insured at the outset of a claim. In this narrative, privy only to the company and defense counsel, the insured can comment on the details of the claim and point out strengths and weaknesses (as they see them) of the case. A thorough narrative allows the company and defense counsel to get up to speed quickly on both the big picture and the nuances of a claim. It also assists in evaluating liability, causation, damages, and overall case defensibility. Likewise, it may also assist in determining whether efforts would be better spent directed toward settlement.

Some carriers also routinely interview the insured, either face-to-face or on the phone, before or during litigation. Conducting an in-depth interview, particularly after reviewing the insured’s narrative summary and other relevant documents, serves several helpful purposes including:

> Enabling the insureds to review and affirm the events of the claim (which they may have to do repeatedly at their deposition and at trial)

> Addressing potential inconsistencies in the records or narrative

> Allowing the claim handler to independently evaluate the insured and share his or her assessment of case defensibility with defense counsel should the case go into litigation or trial

At its best, this overall approach would significantly reduce defense costs—in some cases allowing the claim professional to handle the case through resolution. At the very least, the carrier has early insight into the case and subsequent defense counsel activity can be more focused. Further, having early insight into a claim can assist the company with reserve accuracy.

Conclusion
Proactive claim handling by the company—including early case evaluation and negotiation with plaintiff counsel—can reduce the number of files that go into litigation and thereby reduce defense costs. In those instances where cases do not settle prior to litigation, early and thorough evaluation can result in more focused and efficient use of attorney activities, again mitigating defense costs.

We hope that the ideas presented in this summary stimulate thought on the subject. No doubt, there are additional approaches employed by others.

The relationship between the carrier and defense counsel requires professionalism, trust and open communication. Ensuring a clear understanding and agreement of expected duties by everyone involved can result not only in a healthy long-term partnership but also in more efficient use of defense dollars.

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Endnotes

2 “Companies look for new ways to control litigation costs,” Inside Counsel, Adele Nicholas, 8/30/13.


5 “Arbitration Pros and Cons,” NOLO Law for All, Barbara Kate Repa.

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