



ADJUSTING TODAY

Adjusters International Disaster Recovery Consulting

FROM THE EDITOR

First comes the property loss ... then the news that the insurance policy doesn't fully cover the damages. The policyholder is under a second dark cloud before the first one even begins to clear.

That second cloud can have a silver lining, however, if the right expertise and strategies are applied to the adjustment of the loss. In this issue of Adjusting Today, attorney and public adjuster Ethan Gross shares his insight into what those strategies are, taking the reader through a step-by-step series of tactics for optimizing a claim settlement when, outwardly, the coverage seems inadequate to make such an outcome possible.

He presents these strategies as a well-organized, easy-to-follow "Ten Commandments" for handling the underinsured loss. They are not a substitute for having the proper coverage to begin with, but they can provide a silver lining on losses where that was not the case. It's important reading and a valuable reference tool!

*Sheila E. Salvatore
Editor*



How to Make the Most of an Underinsured Loss

By Ethan Gross, J.D.

After suffering a devastating property loss, perhaps the most frustrating news for policyholders is learning that they do not have enough insurance to cover their losses. Once the loss has occurred, of course, it is too late to increase the amount of insurance; but if informed and well prepared, agents, adjusters, CPAs and attorneys can assist policyholders in maximizing their insurance recovery and minimizing the impact of being underinsured.

This article will identify and provide an overview of the 10 most important avenues that can be explored by any insured faced with



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an underinsured property loss. These “Ten Commandments of Handling the Underinsured Loss” are as follows:

1. Consult with your agent or broker.
2. Obtain a complete certified copy of the insurance policy.
3. Be creative in interpreting the policy for hidden/additional coverage.
4. Investigate the potential for third-party recovery in the case of negligence (subrogation).
5. Work with the insurance company adjuster (don't hesitate to ask for help).
6. Request advance payments.
7. Critically analyze the necessity of all restoration activities.
8. Negotiate with all vendors.
9. Investigate tax relief and/or government benefits.
10. Investigate legal options.

Before addressing how best to handle an underinsured loss, we would be remiss if the first step was not to advise readers of the importance of making every effort to insure to value prior to a loss. This advice is fundamental, but it is surprising how many insureds fail to properly insure their risks. Often the error is the result of a simple thing, such as failing to inform the agent or broker of

renovations, additions or significant acquisitions. Other times, it is the result of not spending the necessary time with an agent or broker going over the details of the risk.

Insuring to value can be very complicated. It has been, and will continue to be, the topic of many articles and books. As such, we will not get into the details of insuring to value in this article. However, it is recommended that insureds meet with their agent or broker annually to review their policy. They must take the time to fully describe their business operations and property to the agent or broker, as these advisers cannot properly counsel how to insure a risk until they fully understand the risk themselves. It is also helpful to discuss coverage with a professional public insurance adjuster, whose expertise is focused on the complications and details of the claim settlement process. The public adjuster's experience in reviewing and calculating values post-loss provides them with unique pre-loss insights into often-overlooked areas of coverage. It allows the insured to more effectively value real property, personal property and potential loss of income. Public adjusters can look at an insurance policy from the perspective of how it may be applied post loss and, as a disinterested third party, advise of the possible need for certain additional coverages, such as code upgrade coverage.

That being said, let's look at what to do after the loss:

1. Consult with Your Agent or Broker

Immediately following the loss, it is important to discuss the policy with the agent or broker. It is possible that the loss is not, in fact, underinsured. A quick review of a current insurance declarations page will help identify any potential problems. Additionally, many of the more complex policies — especially manuscript policies — list various coverages under multiple headings rather than the traditional “Building,” “Business Personal Property”

and “Loss of Income” titles. Often there are additional coverages listed within a policy rather than on the declarations page.

The agent or broker will also be able to determine if the policy is a blanket policy. In this case, the amounts the insured may think were sublimits for a particular property are merely values for underwriting purposes, and it is the combined blanket amount that represents the actual policy limit. The agent or broker can also determine if there were any recent changes or amendments to the policy that are not reflected in the insured’s copy of the policy. The agent or broker may also discover that the original application or a subsequent change the insured submitted was improperly processed by the insurance company’s underwriting department. If this is discovered, the agent or broker can contact the underwriting department to make sure the corrected policy is retroactively placed into effect and that the insurance company adjuster knows these changes are applicable to the current claim.

In addition to the above, the agent or broker may be able to provide valuable assistance in a number of ways unique to the particular case.

2. Obtain a Copy of the Insurance Policy

It is a good idea in every claim to send a letter to the insurance company adjuster requesting a certified copy of the entire policy, including all forms and endorsements. It is impossible to perform a proper policy review unless you have a copy of every provision. Additionally, insureds frequently receive notices from their insurance carrier regarding changes to their policies. In most states, any changes to a policy that limit or reduce coverage are not effective unless notice of the change is sent to the insured prior to the loss. Conversely, changes that broaden or increase coverage may be effective regardless of whether the insured received prior notice. Therefore, if after receiving the policy there are some recent changes that limit coverage, check to make sure the insured received notice of these changes prior to the loss.

To be sure that you have a complete copy of the policy, it is best to cross check the forms listed on the declarations page of the policy with the forms in the policy. Generally there is a section on the declarations page titled, “Forms and Endorsements” or some similar language, followed by several letter/number combinations such as CP 00 10. These “form numbers” identify all forms



and endorsements that make up the policy, and they are also printed on the corresponding form or endorsement. Make sure to match up all the endorsements listed on the declarations page with all of the actual forms and endorsements. That way you can be sure you have the entire policy and can conduct a comprehensive analysis.

This is also the time to look for other insurance. For example, personal property may also be covered under employees' homeowners policies, or a landlord may have insurance on the building and the tenant on business personal property. In the latter example, if one policy is underinsured, the insureds can look to the other policy for coverage or move certain items from "building" to "business personal property," since, as will be discussed shortly, some items are coverable under both categories.

One example of where another policy may offer some relief in a residential loss is if the insured

owns a vacation property. Most homeowner policies include coverage for personal property anywhere in the world. However, the amount available for personal property not at the residence premises is usually limited to 10 percent of the policy limit. Thus, if the primary residence is destroyed and the personal property loss exceeds limits, the insured may be able to make a claim under the policy issued on the vacation home. While the amount available may be limited to 10 percent of the personal property limits of coverage, it will help minimize the underinsured loss.

Examples under commercial policies typically involve leased equipment that also may be insured by the lessor. As such, a claim can be made by the lessor under their own policy. This will free up the insured's money for their own property. Additionally, with most commercial policies, the extension of coverage section will provide coverage for newly acquired property.



This coverage usually provides a limited amount of coverage on new buildings and personal property for 30 days (sometimes longer depending on the policy). There are several scenarios that could trigger this coverage. One example is where the insured has products that have been sold but not delivered to another business. The damaged or destroyed items will likely be covered as “newly acquired property” under the purchaser’s policy. This prevents the insured from using their limited business property money to pay for property of others.

3. Review the Policy for Hidden Coverage

This is the simplest and the most likely place to increase the recovery and minimize losses. However, it is also a commonly overlooked step. For those unfamiliar with reading insurance policies, it would seem that the amount of insurance available is the amount listed on the declarations page. This is not the case. Insurance policies contain a variety of language that provides additional coverage that will actually increase the policy limits or pay certain additional amounts regardless of policy limits. When reading insurance policies you may discover that coverage might first be provided then taken away, and sometimes given back. A good example is code upgrade coverage, also known as ordinance and law coverage. Many policies specifically exclude code upgrades in the exclusions section of the policy. Then they add it back, with a specific limit, as an additional or extended coverage. If a building claim exceeds policy limits and it is determined that some of the repairs are required by codes, you may be able to tap into this additional coverage.

Look for an inflation guard endorsement that provides automatic increases in coverage (and, of course, premiums) every year. Often this endorsement increases the coverage on a prorated basis. Thus, the limit of insurance increases slightly over time. Inflation-guard endorsements may be found in commercial as well as homeowners insurance.

It is a good idea in every claim to send a letter to the insurance company adjuster requesting a certified copy of the entire policy, including all forms and endorsements.

Another critical coverage to look for is guaranteed replacement cost coverage. This is only found in homeowner policies and sometimes goes by different names (e.g., “replacement cost plus”). In short, this coverage provides for the full cost to replace a structure without regard to stated policy limits. Of course, there are some restrictions and limitations (see the policy for details). Initially, this coverage was unlimited. Now, however, most policies will only pay up to an additional 20 to 25 percent over stated policy limits. Some guaranteed replacement cost policies also increase the contents limits on a prorated basis in conjunction with the amount the building policy increases.

Look for “Coverage B Other Structures”

One other commonly overlooked provision in homeowner policies is “Coverage B Other Structures.” Other structures are typically insured at 10 percent of the dwelling limit. People generally associate this coverage with detached garages or sheds. There may be two significant areas of relief with this coverage. First, some policies allow the insured to add the Coverage B limit to the Coverage A limit under certain circumstances. (This is very policy specific.) Second, the Coverage B language is usually loosely written and the

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operative word “structure” is not defined. Thus, any man-made item that is not connected to the house fits in this coverage. This may include such items as driveways and sidewalks, which commonly need replacement as a result of repair efforts. For additional support regarding this argument, as well as other arguments and questions concerning coverage, a great resource is the *FC&S Bulletin*.¹

“Additional Coverage”

After reviewing the declarations page for potential changes to the stated limits, it is important to look through the entire policy. There are a few sections in the policy where you can anticipate finding extra insurance to help cover the loss. Most policies have sections titled, “Additional Coverage” and/or “Extensions of Coverage.” “Additional Coverage” generally refers to coverage items that are added to the policy with a sublimit, but which do not increase the policy limits. “Extended Coverage,” on the other hand, generally refers to coverage for specific items or types of losses with sublimits that are in addition to the policy limit.

Thus, an item claimed under Extended Coverage could be paid up to the specific amount listed, even if policy limits were previously exhausted. Today, many policies use these terms interchangeably, as is done throughout this article. Therefore, it is critical to read these sections carefully to determine if the sublimit is within the policy limit, or if it increases it. Also, many commercial policies have special endorsements unique to the type of business insured, such as a restaurant package. These industry-specific packages typically have several excellent additional coverages in these special endorsements.

Examples of Extensions

Some policies contain only a few extensions of coverage, while others may have as many as 15 or 20. Some typical examples of these extended coverages are debris removal, landscaping, electronic data processing (computers), code upgrade, fine arts, valuable papers, landscaping, and newly acquired property. There are two very common extensions of coverage that insureds often fail to fully utilize.



The most common coverage extension is for debris removal. Virtually every policy allows some additional money for debris removal, once policy limits are exhausted. The amount will either be a stated dollar amount or a percentage of the stated limit of coverage. The two most common errors people make are that they assume debris removal only applies if the building is being demolished, and they calculate the amount solely as a percentage of the building limit.



Regarding the issue of building demolition, the policy language refers to removal of debris. Every insurance repair job has a debris removal component. Under most policies, the entire tear out and disposal of all damaged items falls under “debris removal.” Therefore, in an underinsured claim where repairs are being made, it is important to segregate the tear-out and disposal costs from the general estimate, and to claim those costs under debris removal.

Also, most policies are worded loosely enough that debris removal coverage will provide separate monies for building debris and contents debris. Thus, even though an insured may hit limits under the building debris coverage, they can often segregate the cost to remove and dispose of destroyed contents as well.

Landscaping

Another common extension that is generally overlooked is landscaping coverage. Often, trees and shrubs are damaged as a result of the loss or will be damaged during the course of repairs. Once a landscape bid is obtained, a claim can be made immediately for the loss. Most insurance company adjusters tend to assume that these costs must be incurred before payment is made, relying on replacement cost coverage. Yet the extended coverage for landscaping, unlike debris removal, typically does not include “when incurred” language. And since trees and shrubs appreciate

with time, the actual cash value and replacement cost value should be the same.

Interpreting Policy Language

When reviewing the policy, remember that many words have broad meanings that can expand coverage. Since insurance companies usually write the policies, most courts have held that any ambiguity in an insurance policy is to be interpreted in favor of the insured. Therefore, a little creativity can help when underinsured. If you look at things a little differently, you may be able to create a strong argument to increase your recovery.

One typical scenario is where an insured has exceeded limits on the building, but not the business personal property, or vice versa. There are many items that can easily fit into either category. Fixtures and equipment, for instance, are often specifically addressed under both the building and business personal property coverage. Thus, when the claim is prepared, these items may be claimed wherever they will be most beneficial to the insured. Simply by using the definition in the policy, you can support the placement of these items relative to the claim.

One common scenario involves expediting expenses: If there is an additional cost to expedite

Insurance policies contain a variety of language that provides additional coverage that will actually increase the policy limits or pay certain additional amounts regardless of policy limits.

the repair or replacement of an item, then that part of the cost may be recoverable under the extra expense coverage in the policy instead of the property coverage.

Another example of creativity coming to the rescue in an underinsured claim comes from a real situation. Years ago, there was a small fire at the campaign headquarters of a U.S. Congressman. The office was underinsured, mainly because no one contemplated the cost of replacing build-out items such as carpet, ceiling tiles and paint, when the insurance was purchased.

Most commercial leases require the tenant to insure these build-out items. Businesses that rent office space commonly calculate risk based on their hard goods such as computers, desks and copiers.

In the case of the underinsured congressman, virtually all of his insurance recovery went to repairing/replacing “building” items such as the carpet and painting. In the fire, campaign posters and other literature were destroyed. After reviewing the policy, it was discovered that “valuable papers” were not defined. Some examples were included, but not a definition. The

dictionary provided only a very broad definition. So the items were claimed as valuable papers. The insurance company immediately dismissed the argument. However, after the insured explained their position and supported it with the dictionary definition, as well as some case law regarding ambiguities in insurance contracts, the carrier acquiesced. This is a great example of how ambiguous policy language combined with a little creativity can minimize an underinsured loss.

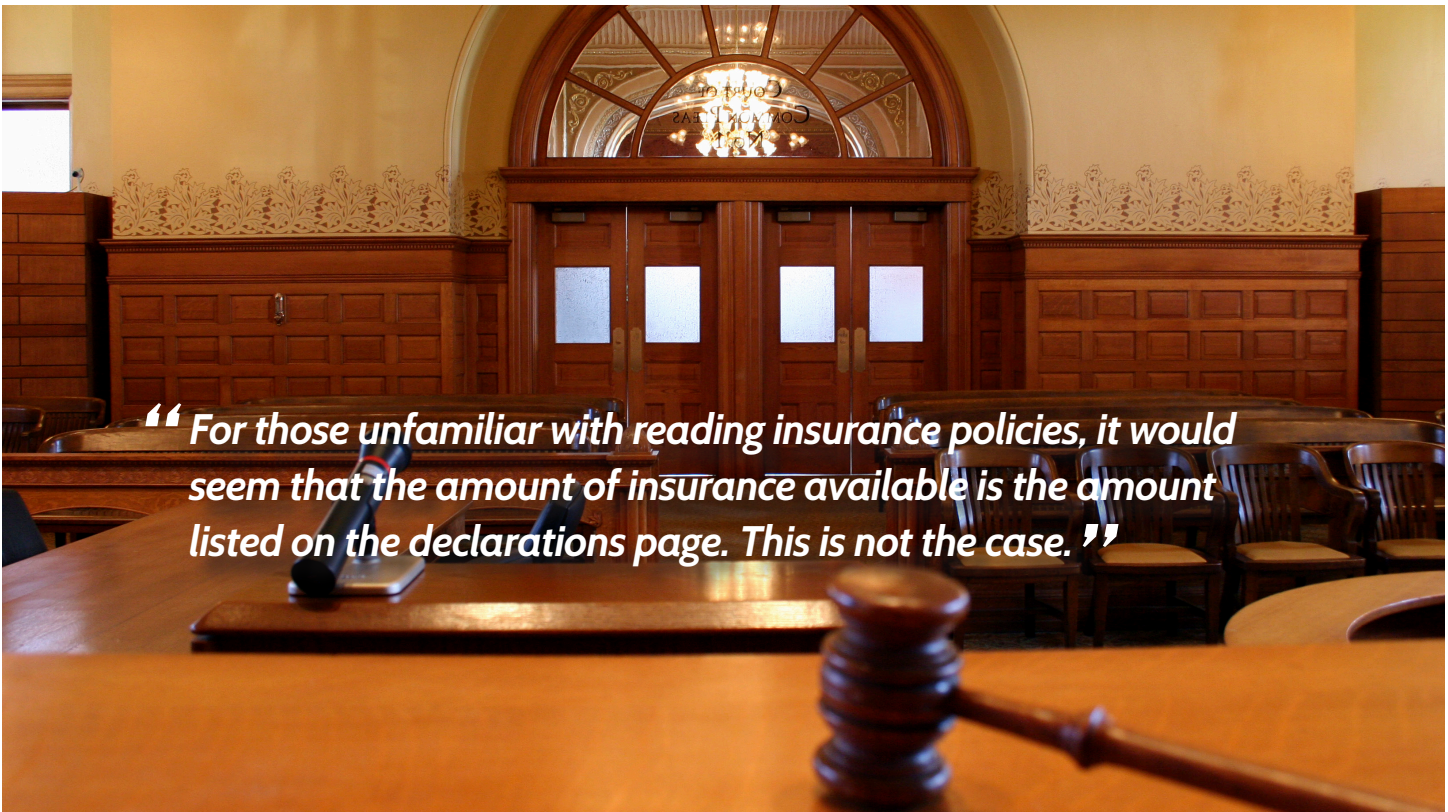
Coinsurance

A third example of where creativity comes into play while calculating a claim is when the insured faces a potential coinsurance penalty. In those circumstances it may be more beneficial to opt to make an actual cash value (ACV) claim rather than a replacement cost claim, as the insured may net more money. This may seem counterintuitive, but if a policyholder is underinsured and they calculate their loss based on replacement cost, they may incur a penalty greater than what they lose by basing their claim on ACV. As a final note, be careful in reviewing and applying the coinsurance provision, as it is sometimes applied incorrectly.

4. Investigate the Potential for Third-Party Recovery

Many losses are caused by the negligence of third parties. This can be the result of anything from faulty wiring by an electrician to a defective lamp that overheats. Some losses may not be the result of a negligent person or a defective product, but they are magnified by them. For example, a defective smoke detector/sprinkler system may not cause a fire, but its failure to work will certainly increase the damages. When the loss is caused or compounded by the negligence of a third party, the insured may be entitled to recover the underinsured portion of the loss in a civil action (tort claim) against the negligent party (tortfeasor).

There are several things that must be considered if the insured is going to pursue a tort claim. First, they should consult with an attorney immediately



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to make sure that they preserve all of their rights and the evidence, and that they provide proper notice to potential third-party defendants. Failure to do so could bar them from recovery. They should also consider hiring their own cause and origin investigator immediately as it is more difficult to determine the cause of the loss as time passes and the evidence becomes stale. If there is a possible tort claim, then the insurance company will most likely pursue a claim against the tortfeasor under their subrogation rights. The insured, their attorney and the investigator should try to work closely with the insurance company's team to share resources and strengthen their case.

There are some complicated aspects to pursuing a third-party claim: specifically, the juxtaposition between the insured's right to recover its underinsured loss; and the carrier's subrogation rights, since both parties will be vying for money from the same defendant. Fortunately for the insured, most jurisdictions follow the equitable rule known as the "made-whole doctrine." This

doctrine provides that, in the absence of statutory law or valid contractual obligations to the contrary, an insured must be fully compensated for its losses before the subrogation rights of the insurance carrier arise.

Under the made-whole doctrine it would appear that there should not be any issues with regard to the insured's priority in the recovery. However, recently insurance companies have been attempting to supersede the insured's priority under this doctrine via contractual language. While the standard subrogation language in most policies does not impact the insured's rights, some new policy language and some subrogation documents (subrogation receipts) are being drafted to give the carrier the right to recover first. Furthermore, many courts have upheld such contractual language, allowing the carrier to recover first.

Even when there is no issue with regard to the insured having priority in the recovery, there can

It is important to ask for advances immediately, in as large amounts as possible. Better that the insured have use of the money.



still be issues if both the insured and the carrier are pursuing a third-party claim. Since most cases settle prior to trial, if the offer is enough to satisfy the insured but not both the insured and the carrier, the carrier may reject the settlement offer and thus stymie a favorable settlement for the insured. Additional complications can arise if there is no agreement as to the total amount of the insured's loss, since there will be issues and possibly additional litigation on how to apportion a final award.

There are some actions the insured can take to minimize the conflicts with the carrier in pursuing a third-party claim. First, the insured's attorney should carefully review any subrogation receipts that are presented to the insured to sign. If they contradict the made-whole doctrine, then they should be revised. Also, in some cases, it may be better for the insured to negotiate an agreement to split any settlement or award proceeds on a percentage basis that is fair under the facts of the specific case. That allows the insured and the carrier to work together and usually achieve a more prompt settlement. Also, when the insured is willing to agree early on to a percentage split with the carrier, typically the carrier will be willing to cover the costs (not fees) of litigation. In short, an early agreement with the carrier can be beneficial for both the insured and the carrier.

5. Ask the Insurance Company Adjuster for Help

Despite the sometimes-negative perceptions of insurance company adjusters, it is often simply their tremendous caseload or the negative attitude of an insured that will prevent them from pointing out ways to maximize coverage. Ask them what you can do to maximize coverage, and they may be able to point out coverages of which you were unaware. Also, adjusters have a separate category for loss adjustment expenses. Sometimes they can pay for some of the costs as a loss adjustment expense. Have them explain exactly how much documentation they need to pay limits, so you do not spend an unnecessary amount of time documenting a claim and thus delaying payment.

6. Request Advance Payments

This may seem like an obvious need on the part of policyholders who have just experienced a major loss; however, even in clearly underinsured claim situations, insurance company adjusters do not always offer to make payments prior to the claim being submitted. It is important to ask for advances immediately, in as large amounts as possible. Better that the insured have use of the money. Also, the availability of cash will help the insured to acquire better deals with vendors and make decisions more quickly, which will also help to minimize the loss.

7. Critically Analyze the Necessity of Restoration

Immediately after a loss, the most common reaction is to make every effort to commence repairs. Restoration contractors can be a valuable resource in mitigating losses. However, most insurance repair work, whether to buildings or to personal property, is very expensive. There are significant costs involved in such things as expediting repairs, dry out, covering, protecting, moving and storing, etc.

It may be a better business decision, for example, to dispose of otherwise salvageable equipment and replace it. It is also an opportune time to look at the necessity of various pieces of equipment. The restoration contractor's job is simply to come in and attempt to save everything — despite the fact that some items may not be worth saving. Rather than rushing to put everything back just as it was, take the time to analyze where to spend the limited resources available.

For example, policyholders may be able to replace equipment with less expensive items that can still handle the load, or to downsize the operation by making better use of space with more efficient equipment. Since the restoration companies will not know which items are most critical to the insured, they may exhaust all of the insurance money on non-critical repairs and have nothing left for the critical ones.

In an underinsured situation, the policyholder should not sign an all-encompassing work authorization for a restoration contractor until they take the time to determine what specific items they want cleaned and repaired and then hire the contractor for very specific restoration services.

8. Negotiate with Everyone

Generally speaking, vendors to the insurance industry (e.g., building and contents restoration companies, etc.) negotiate prices with the insurance company, not with the insured. If there is

ample insurance, then the insured is not impacted by the cost of these repairs. Yet in an underinsured situation, it is particularly important to understand that insureds can and should negotiate with vendors to stretch their limited funds as far as possible. The insured should notify the vendors that they are underinsured and work will be awarded based on the most competitive bid. If possible, it is best to first obtain a cash settlement, then negotiate for the various services needed.

9. Investigate Tax Relief and Government Benefits

In the event of major disasters, such as flood, wildfire, tornado or hurricane, the government may provide loans or grants to offset some of the losses incurred by those living in the area. The Federal Emergency Management Agency (FEMA) website, www.fema.gov, contains valuable information on potential funding sources.

It is also useful to know that, to the extent the loss is underinsured, the insured may be able to declare a loss and receive some tax relief. This is very complicated and it is a good idea to get professional guidance when pursuing this avenue. The Internal Revenue Service website, www.irs.gov, is an excellent source of general information; however, due to the ever-changing and extremely complicated tax code, the best course of action is to consult with a competent CPA or tax attorney.

10. Investigate Legal Options

This item is listed last because litigation is the most timely and costly method of recovering money. Hopefully, after looking into the first nine options, the underinsured loss will be sufficiently minimized so that this route becomes unnecessary. However, this does not mean that an insured should wait until all other methods and options are exhausted.

Lawsuits have critical time and evidentiary requirements that must be satisfied; otherwise the insured can lose their rights. Lawsuits must be

filed within the applicable statute of limitations and evidence must be preserved in order to maintain actions against negligent third parties or, in some instances, errors and omissions claims in the event the agent or broker was negligent. While the other methods outlined in this article may get policyholders close enough to being whole, the insured should consult with an attorney shortly after the loss to make sure they do not inadvertently lose any of their rights.

Conclusion

While it is best to head off an underinsurance situation through proper analysis of coverage needs ahead of time, after a loss occurs there are still many avenues available to policyholders to maximize their financial recovery and minimize their underinsured losses. Experience and creativity are key to developing the best possible strategy for presenting an underinsured claim. Insureds should not be afraid to call in the expertise needed to get the best possible recovery.



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¹ The *Fire Casualty & Surety Bulletin (FC&S Bulletin)* is a widely respected insurance industry publication. It is published by the National Underwriter Company. This publication includes explanatory sections and a question-and-answer database where the editors respond to coverage questions. The database has a user-friendly search engine, which makes finding information on your topic simple. While the *FC&S Bulletins* do not have the binding effect of published court opinions, they tend to be very persuasive. Additionally, when dealing with questions of additional coverage, the amounts tend to be smaller and, therefore, rarely litigated. Thus, published opinions on questions concerning additional coverages are limited. For more information, visit www.nuco.com.



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