

Subrogating Aggregate Deductible Recoveries

July 17, 2019

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What is a SAD Recovery?

Defining the SAD Situation

- Aggregate (Eroding) Deductible Defined

Policy Scenarios

Insured Examples

1. Property Management Companies
2. Real Estate Investment Funds
3. Family Corporations

Aggregate Deductible in Practice

OVERVIEW

- Policy period dependent
- Per location, per loss deductible
- No carrier indemnity liability until the aggregate deductible is eroded
- Adjustment and cause & origin investigation still required regardless of aggregate status, especially on larger claims

SAD Question #1 – What do I do if indemnity is within the Aggregate Deductible?

SAD Answer #1– Proceed through standard subrogation process

First, a Quick Intro to Subrogation

Subrogation is the process by which an insurance carrier that has paid a policy holder for a covered loss seeks to recover those payments from the third party that was ultimately responsible for causing the loss in the first place.

Subrogation exists in many different lines of insurance: property, auto, workers compensation, just to name a few.

The insurance carrier “stands in the shoes” of the insured



But why subrogate?

- Aren't insurance carriers in the business of paying for property damage when a loss occurs in exchange for premiums? Isn't that the whole point of insurance?
- Well, yes. But if a third party caused the damage, they shouldn't get a free pass just because a property owner was wise enough to obtain an insurance policy obligating its carrier to pay the owner when a covered loss occurs.

- An insurance company might have a contractual obligation to make policy payments for a loss that occurs, but that doesn't relieve the responsible third party from being held to account for the damage their acts or omissions caused.
- And that distinction is the key to understanding why subrogation occurs in the first place.

Examples of Subrogation

Joe and Susie Homeowner own a home in Chicago, which is insured by ABC Insurance Co.

Joe and Susie recently hired Mike the Electrician to install new lights in their kitchen. They hired Mike because they aren't electricians and don't know how to install lights. Fortunately, that's Mike's area of expertise.

Mike comes to their home and installs the lights as promised. He leaves and everyone is happy. A week later, while Joe and Susie are having dinner in their kitchen, those nice new lights begin to produce smoke and then a fire quickly grows and spread, causing major damage to their home.

Fortunately, Joe and Susie got out of the home safely and then submit a claim to ABC, who eventually pays Joe and Susie the amounts due to them under the policy so they can repair the fire damage to their home.

Aggregate Deductible Example – **STARK v. GROOT**

BACKGROUND SCENARIO

- Insured: Stark Industries
- Policy Period: January 1, 2018 to January 1, 2019
- Loss Location: Avengers Tower, 200 Park Ave, New York, NY
- Aggregate Deductible: \$2,000,000
- Location Deductible: \$100,000
- Date of Loss: February 14, 2018
- Type: Structural damage following an arc reactor explosion. Recent work by electrical subcontractor, Groot & Associates, LLC.
- Reserves: \$600,000

VIDEO FOOTAGE MOMENTS PRIOR TO ACCIDENT



Subrogation Potential Exists

Investigation Overview

- Electrical Engineer's Opinion: Groot & Associates was contracted to install electrical components at the arc reactor and failed to properly seal the button before commissioning – clearly didn't know what they were doing!
 - Fire Investigator confirms cause and origin was electrical near the button
 - Available claims against Groot & Associates:
 1. Negligence
 2. Breach of Contract

Aggregate Impact

Recall:

- Aggregate Deductible: \$2,000,000
- Location Deductible: \$100,000
- Date of Loss: February 14, 2018
- Reserves: \$600,000

New Facts:

- Policy Loss runs as of the DOL show global aggregate erosion at only \$250,000
- Adjuster and carrier conclude that there will be no indemnity payments and no exposure

DO NOT CLOSE THIS FILE!

Aggregate Impact

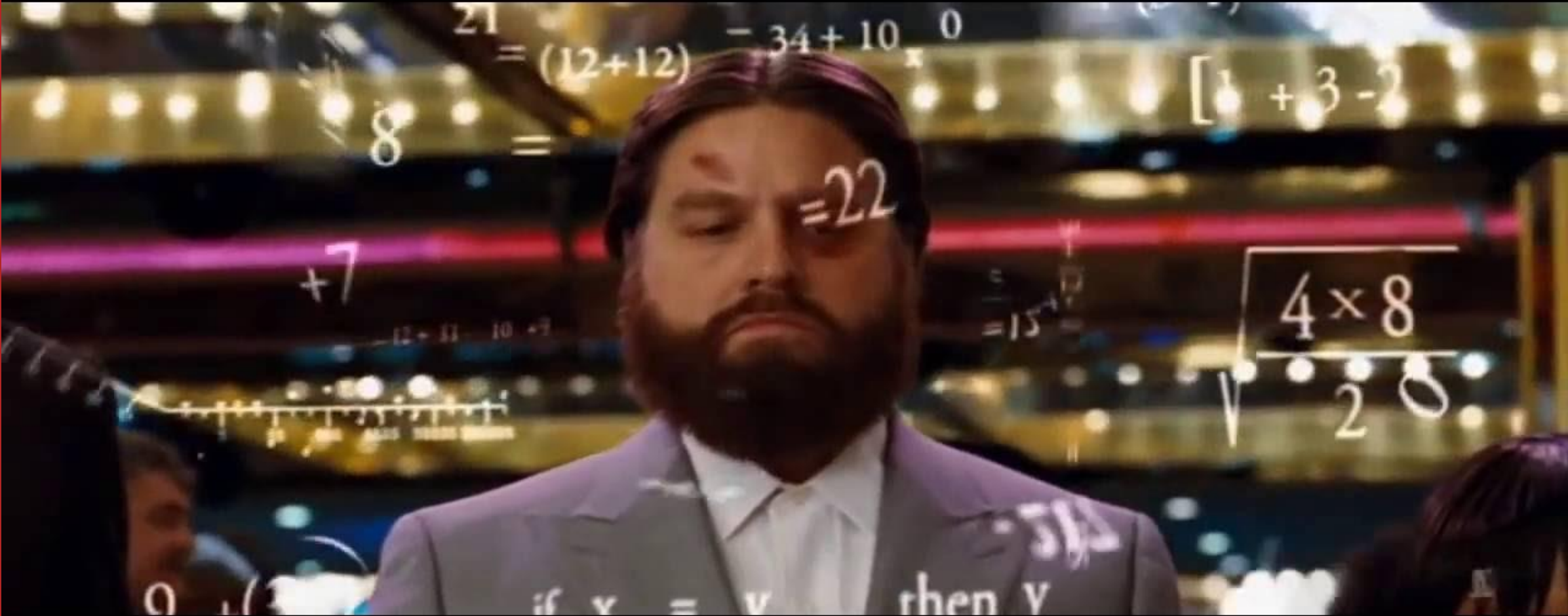
SAD Question 2: Why shouldn't I close a file that falls within the aggregate deductible and shows no exposure as of the date of loss?

SAD Answer 2: Subrogation takes a long time. By the time the payment would occur or indemnity closes, the aggregate deductible is likely fully eroded from subsequent claims.

Subrogation Takes Time

- Subrogation takes a long time
 - Inspection(s)
 - 1-2 months from DOL
 - Adjustment
 - 4-6 months from DOL
 - Indemnity Payment
 - 7-9 months from DOL
 - Loss Runs at time of Indemnity Payment
 - Aggregate deductible eroded before negotiation begins!
 - Premature closure prejudices otherwise viable subrogation claims

Retroactive Subrogation Recovery Still Applies



How it Works

- Tools towards Recovery
 1. Complete Investigation
 2. Proceed with Adjustment
 3. Joint Recovery Agreement with Insured
 4. Recovery Budget
 5. Demand
 6. Negotiation
 7. Recovery Payment Distribution (AD dependent)

STARK v. GROOT –

Cost of Premature File Closure

Timeline 1 – Around Date of Loss, February, 2018

- Aggregate Deductible: \$2,000,000
- Location Deductible: \$100,000
- Date of Loss: February 14, 2018
- Reserves: \$600,000
- Aggregate Erosion: \$250,000

Timeline 2 – 8 Months Later, October, 2018

- Post-Adjustment Indemnity Exposure: \$600,000
- Aggregate Erosion: \$3,600,000
- Carrier Policy Payments: \$1,600,000
- Premature file closure cost: Up to \$600,000

Premature closure prevented up to **\$500,000** in recovery funds from going back to the carriers with the insured getting back up to **\$100,000!**

Aggregate Not Fully Eroded

SAD Question 3: What if at the adjustment is closed and indemnity exposure is confirmed, the aggregate has not yet eroded?

**Assumption: Groot & Associates' liability insurer immediately agrees to liability and pays the full adjustment as soon as it is finalized.

SAD Answer 3: The Joint Pursuit Agreement controls and any recovered funds would replenish the aggregate or be split between exposure payments and the aggregate, costs of pursuit to be paid back out of the recovery.

Nobody Ever Rejects the Recovery Check

- Real World Examples
 - Roofing Fires
 - Vehicular crashes
 - Product defects
 - Cigarette Smoking

QUESTIONS

