

# Managing

# CATASTROPHIC LIABILITY

**IN AUGUST, A NATIONWIDE GROCER** recalled all of its store-brand macaroni and cheese due to potential listeria contamination. A week before that,

a company that produces ground red pepper issued a nationwide recall due to possible salmonella contamination. In fact, in 2009

alone, the FDA has already issued nearly 800 recalls.

“Anything implantable or ingestible is subject to catastrophic claims,” says Andrew Barberis, Executive Vice President of P&C severity claims at Chartis U.S. “In fact, if you are anywhere in that chain of distribution, you are potentially on the hook.”

But the world of catastrophic incidents isn’t confined to the food and drug industries. Plant explosions and fires, for example, can cause millions of dollars in property and casualty damage. According to the U.S. Fire Administration, in 2007, 116,500 fires were reported at non-residential structures such as stores, offices, utility and storage structures, resulting in 105 deaths, 1,350 injuries and more than \$3 billion in damage. Unanticipated injury from defective or harmful products account for billions more in losses every year.

These risks highlight the need for catastrophic liability insurance. A company must have protection when large-scale losses or incidents occur or risk sinking into bankruptcy as it defends the claims that arise. Unfortunately, no single insurance carrier will take on the heavy burden of insuring a company for such costs, which can reach as high as a billion dollars. However, companies can layer catastrophic liability insurance to obtain maximum coverage.

“The simple concept is that no one insurance company wants to commit too much of its capital to any one risk,” says Neal Glazer, a partner at D’Amato & Lynch, LLP. “Instead, you find a lead insurer that will issue an initial layer of insurance, and then other insurers will layer on top of that, depending on their appetite for risk.”

## Claims Management

But before their carriers get too involved, the insured companies must assess the claim internally. When a catastrophic claim arises, it is often the job of in-house counsel to do this; in some cases this responsibility falls on the company’s risk manager. Although no two claims are ever exactly alike and each calls for its own unique analysis, there are guidelines in-house counsel can follow when assessing a claim.

“Although every claim is different, there are certain fundamentals, such as knowing the facts, the damages, and the law,” Barberis says.

Different types of claims pose unique challenges. For example, claims arising from a plant explosion are often confined to the specific incident, making the number of claims and damage assessments fairly straightforward. However, in claims involving faulty or contaminated consumer products, including food, assessing the claims can be much more difficult.

“With food-borne pathogens or pharmaceutical cases, you may start with 15 to 20 claims, and then three years later, you could end up with hundreds,” says Earl W. Gunn, a partner at Weinberg Wheeler Hudgins Gunn & Dial. “It’s very important that you plan for that possibility because a poor strategy can make the number of cases skyrocket.”

A major part of this successful strategy is purchasing adequate catastrophic liability coverage.

## Necessary Coverage

Because catastrophic incidents are infrequent, many companies neglect to purchase adequate coverage. This is especially true during difficult economic times, when company budgets are being stretched or outright slashed.

“Many times companies look at their loss history and see that they do not have many claims or do not have large claims,” Gunn says. “That can change overnight.”

This is even more troubling when looking at catastrophic cost statistics, which show that while the occurrence of claims is holding steady, the cost of such claims is increasing dramatically. In addition, as plaintiffs’ lawyers have become more savvy in pressing such claims, the number of claimants will likely continue to rise.

“There are certain types of cases that the plaintiffs’ bar will recognize immediately as profitable,” Gunn says. “They then develop an advertising campaign, which results in many more claimants than you would otherwise have.”

In addition, many companies neglect to obtain catastrophic liability coverage because they believe it is not applicable to their business. However, explosions and fires can occur at any company with a physical space, thus necessitating some level of catastrophic liability insurance. Also, some industries, such as over-the-counter medications, may believe they are immune to such claims because they are not highly regulated like their prescription counterparts. But as the recent recall of contact lens solution has shown, this simply isn't the case.

"This company thought that because it didn't have FDA-approved products it didn't need the same amount of insurance that a prescription pharmaceutical company might," Glazer says. "It barely skated through with enough insurance given the number and seriousness of the claims."

#### Carrier Selection

After the decision to purchase catastrophic liability coverage, the next most important question is how to structure this coverage. Companies gain certain benefits by carrying multiple layers of liability insurance capacity from the same insurance group.

First, the involvement of a single group brings consistency to both claim evaluation and strategy, resulting in efficiencies in the claims handling process.

"This enables the insured to avoid new carriers coming and going as a claim moves into excess layers and the need to 'reinvent the wheel' in calculating a claim's worth and renegotiating claim strategy time and again," Glazer says.

With multiple carriers, the insured risks getting hamstrung by differing claims handling philosophies, which can greatly bog down the resolution of a catastrophic claim. Gunn cites an example of a healthcare product manufacturer with multiple companies underwriting its coverage:

"Each insurer wanted to pursue a different strategy for their claims, even though these claims involved the same product and the same plaintiffs' lawyers," Gunn says. "In fact, the current lead carrier didn't want to use the mediator that had been involved in resolving approximately 40 of the cases already. Instead, they wanted to bring onboard a new mediator who was unfamiliar with the claims, which would have been a waste of time and money."

Barberis notes that when a Chartis insurer has the lead and excess layers in an insurance tower, it enables his company to take a top-down view, formulating a sound and consistent strategy to take ownership of the entire litigation, resulting in expedited resolutions.

Finally, it is important that in-house counsel have a strong working relationship with whichever insurer takes the lead in providing catastrophic liability coverage. As part of the claims process, in-house counsel must regularly communicate with their carriers to brief them on the development of litigation, including the present and projected extent of loss.

"It is good to communicate with your insurers so that as loss moves up the tower, the insurer next in line isn't surprised by what's coming," Glazer says.

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