

Partnering for Success

SAPIENS

Reinsurance Claims Leakage

By Martin Greenberg, Reinsurance Product Manager, Sapiens

For more information, please contact us at info.sapiens@sapiens.com.

Claims leakage is a significant issue that affects the bottom line of any insurance company. In order to understand and ultimately analyze the effects of claims leakage, one must first observe the source of the problem – claims handling and settlement. It is self-evident that carriers must firstly assure there is proper handling of claims on the level of direct claims (how the company manages claims settlements, knowing the cost of claims settlement and managing recoveries). In the area of inwards (assumed) reinsurance, managers must ensure accurate documentation of data received from ceded insurance companies and follow-up on claim developments.

For ceded reinsurance claims, it must be emphasized that in all cases of incorrect claims handling, the result is financial loss to a carrier's bottom line. As a result of reinsurance claims leakage, insurance carriers are losing millions in realized revenue.

Let's look at some business-related causes of ceded claims leakage:

- 1) A claim is not allocated to reinsurance contract(s); or the claim is allocated to certain reinsurance contracts, but not to all contracts
- 2) A claim is allocated incorrectly to reinsurance contracts and consequently wrongly recovered
- 3) A claim recovery is allocated to reinsurance contracts, but calculated incorrectly
- 4) Claims accounting and technical billing are poorly handled, resulting in late – or missed – recoveries.

As with any problem, “the fix” starts with understanding why these situations occur.

Claim Leakage Sources

Currently in the insurance industry, many carriers manage their reinsurance activity via manual calculations (spreadsheets). Obviously, manual handling will be prone, to some extent, to human error. A carrier can't fully rely on the calculation of claims provided by its reinsurance department, and the process lacks effective control mechanism.

Obviously, implementing reinsurance management technology is surely a significant improvement. However, it needs to be acknowledged that many reinsurance management systems provide only a partial business solution, and significant functionality is still being handled manually. So even though a carrier may have some automated processes, the lack of proper control can still result in claims leakage.

It's essential to understand just how complex this becomes within the current business environment, as reinsurance programs are becoming more and more sophisticated; a reinsurance program can consist of a mix of proportional and XL treaties, including

facultative protection, with various layers and attachment points, inuring rules and terms and conditions – reinstatements, aggregates, currency calculations, interlocking rules, stability and indexation, etc.

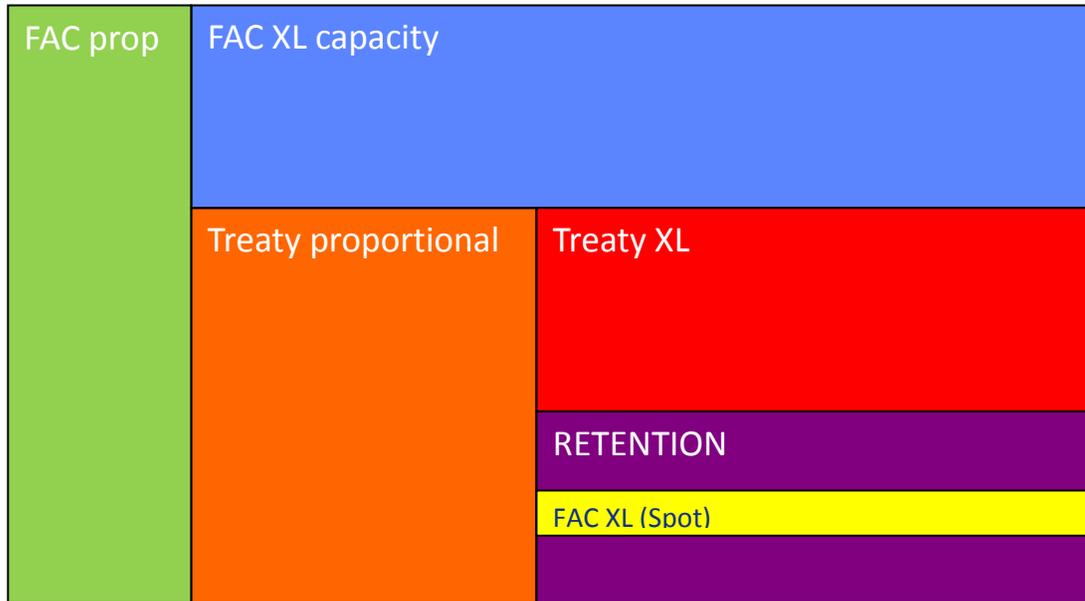


Figure 1: example of complex reinsurance program

Besides appropriate management of the reinsurance program, there is the issue of inaccurate or inadequate information in claims transactions. All transaction information must be detailed clearly within a claim transaction to ensure accuracy; lack of control over the policy & claims information is an additional source for error and ultimate exposure for claims leakage.

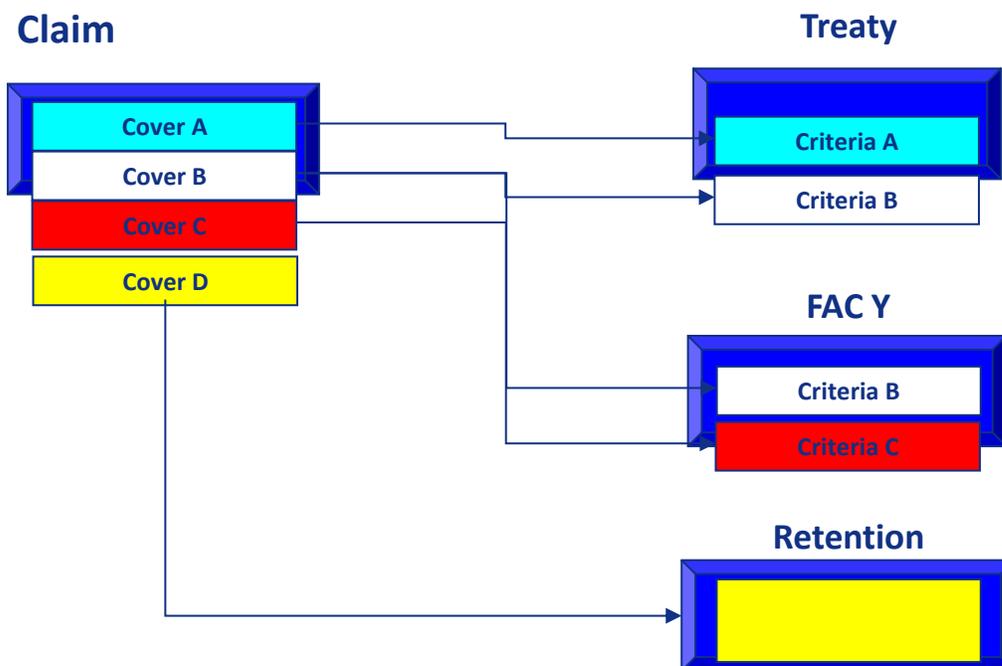


Figure 2: example of complex claim allocation to reinsurance contracts

Billing and collections can also play a fundamental role in reinsurance claims leakage. There can be cases with an inadequate billing process or poor integration with accounting in an organization; improper interfaces between reinsurance and accounting can result in faults and latency in the claims billing process. In addition, the inability to perform claims recoveries follow-up resulting from improper account tracking and aging, as well as difficulty in cash application to claim items, can result in incorrect claims accounting and missed collection.

To summarize, the problem relating to the above issues is that one can never know the true measure and full extent of such losses, especially as there are multiple factors causing claims leakage ranging from contract management, claims information, claims billing and interfacing with accounting. At the end of the day, we know claims leakage exists, however we cannot know about it until after conducting a proper audit.

Improving the reinsurance claims recovery process

We know the symptoms and the elements; so how can we improve the situation? The remedy lies in a composite course of action. A key component is harnessing a comprehensive reinsurance management technology platform that enables overall management of the reinsurance program, including all types of contracts. The system must maintain the data items and business rules required for claims transaction allocation and ultimately provide comprehensive calculations, while taking into consideration terms and conditions, warranties, reinstatements, aggregates, events,

limits of liability, currency management, etc., as well as supporting contract inuring rules. An additional – but very significant – factor in the reinsurance program management is flexibility, enabling swift response to business changes, and ongoing program adjustments.

An additional component is proper management and processing of policy and claims transactions, maintaining all necessary information, and performing automated allocation to reinsurance contracts, including all required calculations.

However, maintaining a fully-automated system is not the complete answer; another key measure relates to ensuring suitable controls. Basic accounting “inventory” controls are naturally required for ensuring completeness of transactions and figures; but in addition to the obvious controls, there's also the need for a birds-eye “sanity” view of reinsurance results accuracy; this can be achieved by utilizing management information reporting and business intelligence technology, based on the underlying reinsurance software information repository. Ultimately, managers should receive up-to-date, relevant and concise business information to notice business inconsistencies and irregularities.

Looking further at control issues from a micro, rather than macro, perspective, we should expect a reinsurance management system to offer extended control via entity detailed inquiry capabilities – presenting party, contract and claim information. Other measures should be implemented – exception reporting based on a carrier's specific reinsurance program and random testing of specific business cases. These should reflect all aspects of reinsurance processing – such as allocation to reinsurance contracts, including inuring order (working, aggregate, etc.) and accurate calculations (limits, shares, reinstatements, aggregates, etc.).

Good housekeeping includes applying automated billing and accounting procedures. Carriers must implement automated production of reinsurance technical billing statements, and business results should automatically be transferred the reinsurer/broker current accounts and GL. Convenient cash application processes and controls should be in place, having the ability of highlighting unpaid items and maintaining an audit trail of payment collection. Finally, aging reports are essential for follow-up of late recoveries.

Summary and conclusion

Reinsurance claims leakage can be a significant source of revenue loss in an insurance organization. The major causes are related to manual processing and lack of proper controls. Implementing comprehensive automated business processes and controls via reinsurance software technology are essential for ensuring accuracy and eliminating financial loss.

There are several leading reinsurance software management systems in the market. Carriers would be well advised to seek an appropriate platform that will provide in-depth reinsurance functionality and the required flexibility for proper management of the reinsurance business and accounting.

Partnering for Success

The logo for Sapiens, featuring the word "SAPIENS" in a bold, blue, sans-serif font. A stylized blue swoosh underline is positioned under the letter "A".

This document and any and all content or material contained herein, including text, graphics, images and logos, are either exclusively owned by Sapiens International Corporation N.V and its affiliates ("Sapiens") or are subject to rights of use granted to Sapiens, are protected by national and/or international copyright laws and may be used by the recipient solely for its own internal review. Any other use, including the reproduction, incorporation, modification, distribution, transmission, republication, creation of a derivative work or display of this document and/or the content or material contained herein, is strictly prohibited without the express prior written authorization of Sapiens.

The information, content or material herein is provided "AS IS", is designated confidential and is subject to all restrictions in any law regarding such matters and the relevant confidentiality and non-disclosure clauses or agreements issued prior to and/or after the disclosure. All the information in this document is to be safeguarded and all steps must be taken to prevent it from being disclosed to any person or entity other than the direct entity that received it directly from Sapiens.

USA

395 West Passaic Street
Rochelle Park, NJ 07662
Tel: +1 201 820 3500

Canada

10 Kingsbridge Garden
Mississauga, ON, L5R 3K6
Tel: +1 905 507 9700

United Kingdom

Pierhead St., Cardiff Bay
Cardiff CF10 4DQ
Tel: +44 29 2044 8600/1

France

27, Avenue de l'Opera
75001, Paris
Tel: + 33 1 70 38 53 21

Israel

Azrieli Center
Holon, 588 5800
Tel: + 972 3 790 2000

USA

4000 CentreGreen Way,
Cary, NC 27513
Tel: +1 919 405 1500

Australia

111 Elizabeth Street
Sydney, NSW 2000
Tel: +61 2 8222 3100

United Kingdom

1 George Street,
Uxbridge, UB8 1QQ
Tel: +44 1895 464 000

Belgium

Brusselstraat 59, 2018
Antwerp, Belgium
Tel: +32 3 3040800

Japan

Queen's tower C 11F
2-3-5 Minatomirai, Nishi-ku
Yokohama 220-6211
Tel: + 8145824777