

# Claims Management Practice – Some Issues for 2008

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## Overview

1. Determining Income
2. Mitigation
3. Regular Care & Attention
4. Some FICS decisions

# Determining Income

## Common scenarios – self employed insured

- insured returns to work on reduced hours, but business maintains previous level of profitability?
- Insured's income & expenses are variable
- insured owns, or has interest in, a number of business entities?
- Insured's business has made a loss pre disability?
- 'managerial' or 'trade' occupation

## What methodology is appropriate?

## Case Study 1

### Application

- Real Estate Agent
- One main agency with related franchises
- Duties – clerical, driving, interviews, auctions, demonstrating
- 50-60hrs pw
- 37% ownership
- Gross Income = \$283,333
- Benefit \$17,000

***[Profit share \$667k; Total Annual Earnings \$975k inc super;]***

### Claim

- Cancer
- RTW after 15 days
- Pre disability salary \$325,000
- Can do about 20% duties
- Discretionary payment by company – ‘not in nature of reward for work’
- The payments equate to ‘paid salary’

***[Pre disability Profit share \$823k; total annual salary \$1.2m or approx \$98k pm]***

## Case Study 1

### Policy wording

- **Earnings** = 'Where the life insured is self-employed i.e directly or indirectly owns part or all of the business or practice – **the income of the business or practice generated by the personal efforts of the life insured** after the deduction of their share of business or practice expenses in generating that income.....earnings do not include investment income and are calculated before tax.'
- **Earnings before disability** = 'The life insured's average monthly earnings for any continuous one year period in the three years before they were totally disabled'
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- **Earnings after disability** = 'The life insured's monthly earnings when they are partially disabled or under rehabilitation.'

# Case Study 1

## Insurer's approach

- Requested information for all related franchises
- argued that profits of the group were to be included in calculation of PDI
- Basis of approach that as a director, the insured was in control of, and responsible for, the overall management and direction of the business
- Loss of income = 16.8%
- M/benefit = \$2,900

## Insured's approach

- Accept 20% of payments made are attributable to 'personal exertion'
- 'personal exertion' reflected in actual time spent at business and value of input which was minimal
- The actual salary paid accurately reflected the 'personal exertion'
- Profit was 'investment income' and specifically excluded by policy
- Discretionary payment to be repaid
- Loss of income = 80%
- M/benefit = \$13,688

***Issues? Outcome?***

## Case Study 2

- Indemnity policy
- Insured an entrepreneur – involvement in numerous companies
- Claim for total disability
- Key issue was calculation of pre disability income
- In relevant period insured received a total of \$256k from 3 companies
- One entity, of which the insured had been a shareholder & director, lost \$24.5m

## Case Study 2

**Pre Disability income defined as:**

*“...Monthly Income you received during the 12 months ...before...disability’*

**Monthly Income defined as:**

*“...the monthly income generated by the business or practice directly due to your personal exertion or activities .....less your monthly share of necessarily incurred business expenses”.*

## Case Study 2

### Insurer's Position

- Insured was heavily involved in failed business even if not officially a director
- The \$24.5m loss can be taken into account as it was a related business
- 'income' is effectively gross earnings less expenses
- The loss wipes out earnings and the result is that there is no pre disability income
- Benefit not payable

### Insured's Position

- Only 'income' from personal exertion was salary paid to him
- Denies being a 'shadow' director of failed business and states he was retrenched from the business
- Even if insured was a director, given entity's size insured's personal exertion was out of proportion to the business turnover

*Issues? Outcome?*

## **FICS Determination 13142**

### **FICS determination 13142**

- Insured a pharmacist in partnership with husband
- TD claim made and paid, dispute as to quantum of PD benefits
- Policy upgrade also applied

### **Member**

- PD benefits should be calculated from tax returns – reflect income insured actually received
- Tax returns showed insured's income had risen during period of disability – therefore no benefits payable

### **Insured**

- Had worked sporadically and with no responsibility
- Economic value of work had reduced significantly, even though insured was apportioned same profit from partnership for tax purposes

## FICS Determination 13142

### Original policy wording

“Average weekly earnings” defined in the policy to mean:

*“income earned by the life insured from **personal exertion** in (her) usual business...less business expenses necessarily incurred in earning that income (but before personal deductions and income tax”*

### Upgrade policy wording

“Income” defined in the policy upgrade to mean:

*“if the ...insured owns part, or all, of a business or practice, income is money generated by the business due to the person insured’s **own activity**...”*

## FICS determination 13142

### Panel Determined:

- Panel found original policy wording to be more favourable as income was confined to income earned *by the life insured* due to *personal exertion* as opposed to money generated *by the business* due to insured's *own activity* and was broader
- Income must be attributable to the insured's 'personal exertion'
- Neither party applied policy to the facts
- Tax returns not determinative of 'income'
- Guiding principles:
  - *apply calculations to relevant periods*
  - *analyse proportion of working time between wife and husband*
  - *analyse actual income earned from personal exertion*
  - *analyse hours worked & quality of function*
  - *income relied on at application irrelevant*

# Potential Methods to Determine Income

## 1. Proportion of hours work compared to pre-disability

Flaws:

- How do you determine appropriate hourly rate?
- Award rate not likely to be appropriate if insured has managerial/supervisory responsibilities.
- Rate for a manager/owner should not be same as other employees as this would not take into account managerial experience, business acumen etc required to run the business.
- Difficult to quantify for a self-employed insured – a fixed rate would only take into account the number of hours worked, without regard to the quality & nature of work performed.
- What is link with 'personal exertion' or 'own activity'?

## Potential Methods to Determine Income

2. **Include all income received from ALL ENTITIES insured has a share or interest in – less apportionable expenses**
  - But income received from “all entities” is not likely to be considered as being income from “personal exertion”
  - More likely to fit within “own activity” definition
  - Does not quantify or establish a link to personal exertion or own activity

## Possible Methods to Determine Income

3. **Similar to 2. including income from ALL ENTITIES less apportionable expenses, but with adjustments for items such as:**
  - Investment income
  - Depreciation
  - Donations
  - Expenses such as motor vehicle etc.
- Not as narrow as 1, but more attributable to “personal exertion” than 2.
- More complex than 2, therefore more difficult to calculate with certainty.

# Factors to Consider in Determining Income

## No Golden Rule

- Relevance of underwriting practice?
- Case by case, common sense approach

## The Policy

- Intention?
- definition of income & possible interpretations
- Annual calculation or monthly? Reconciliations??
- Upgrades

## Circumstances of insured

- Employee/self-employed?
- If self-employed, size & structure of business?
- Interest in other entities?

## Some Cases

### **Nosic v Zurich Aust Life Insurance Ltd [1995] QCA 519**

- Income = ‘...amount earned by insured..’
- Partnership income filtered to insured via family trust

### **Associated National Life Insurance Comp. Ltd v Patane [2000] SASC 443**

- Partnership situation again
- Earnings increased post disability

## Duty to Mitigate

### What is the duty to mitigate?

- Duty of the party whose legal rights have been infringed to act reasonably in mitigation of damages

### In context of Life insurance policy, this could mean it is unreasonable to .....

- not to return to work in duties within capacity
- refuse to undergo reasonable treatment
- refuse to participate in rehabilitation

## Duty to Mitigate a Loss

### Potential difficulties

- You will need evidence of failure to mitigate loss
- Legal position re refusing to undergo treatment
- Policy wording may limit opportunities
  - Rehab not compulsory
  - Partial disability benefits based on actual return to work and loss of income
  - proving loss of income due to disability
  - total disability benefit if unable to do 'one duty'
- FICS approach

# Duty to Mitigate

## Potential Approaches

- Argue duty an implied term (note legal rules in this area)
- Duty of good faith?
- Definition of total disablement – following advice of doctor (if applicable)
- Notify insured duty & steps insured reasonably required to undertake rehab
- Obtain medical opinion that rehab appropriate – support from treating doctors
- Obtain evidence of likely recovery & impact on liability if steps had been taken to mitigate

## Regular medical care and attention

What constitutes “regular care and attention”?

**Policy** – *‘...following advice of a medical practitioner’*

Scenario :

- Claim notified 7 years after claim event
- Insured claims PD during this period – working 4 days/week
- HIC & PBS records available
- Clinical notes obtained
- However, regular GP for majority of this period now retired and difficult to locate
- From above information, can determine 14 or 15 consults over 7 years were for claimed condition or prescription repeats for claimed condition

***Does insured meet the criteria?***

## Regular care and attention

### ***Atton v NMLA [2007] NSWSC 310***

- single attendance on a medical practitioner is insufficient to establish regular care & attention
- “regular care” constituted more than one visit to a doctor – connoted repetitive medical assistance
- “regular attention” connoted a series of appointments

### ***Abacus Consultants p/l v NMLA [2003] SADC 135***

- ‘..under continuous direction and professional care of a m/practitioner...’
- back injury; limited treatment until such time as surgery required
- ‘clause is broad enough to accommodate conditions that are clear cut and not amenable to immediate treatment’
- Diagnosis, prognosis and recommendation as to timing of surgery has the effect of being continuous and such advice amounts to ‘direction and p/care’

## A Couple of FICS Decisions

### **Underwriting Evidence, D 17618**

- Initial opinion defer
- Supplementary opinion 'decline'
- Importance of underwriter statement explaining how a 'decline' decision reached

### **Policy Issued 'subject to cancellation', D 17201**

- Application – 'yes' to cancellation of other IP policy
- Revised Terms signed re 2 health issues; no mention of other IP policy
- Policy schedule issued – noted that policy issued subject to cancellation of other policy
- Held – cancellation of other policy was not a condition precedent; insurer had not done enough to make the cancellation of other policy a condition precedent; notice of condition precedent came after policy commenced