

Property Casualty 360

Opinion: The Real Cost of Certificates of Insurance

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One of the most daunting—and often reviled—tasks facing agencies today involves the processing of certificates of insurance. This is an activity that typically generates no revenue for the agency but creates significant operational costs and dramatically heightens the agency's E&O exposure.

One consultant estimates the cost to issue a plain-vanilla ACORD 25 document at \$7; and if some customization is required, it could be as much as \$15-18. This figure could go even higher when responding to requests that insist upon the completion of some sort of "compliance checklist" that consists of dozens of broad, vague, generalized questions about policy coverages.

For example, an agent was given a multipage questionnaire he was required to complete, along with an "affidavit" warranting that coverage was in place and conformed to the construction contract (of which he had read two of 88 pages) that was to be notarized and witnessed by a disinterested third party and sent to the certificate holder via certified mail. This document required that over 400 entries be completed.

These affidavits and checklists often want the agent to proclaim that the insurance policy(ies) are in compliance with indemnity agreements the insured has entered into—when the reality is that they almost never do.

One producer and a customer-service representative (CSR) spent two and a half hours on one certificate that had to be redone four times. The last time was because a field on the form was not applicable, and the CSR had entered "NA"—but the certificate holder would only accept an entry of "N.A." So they had to reissue the certificate and add the two periods after the "N" and "A." The contractor was due \$300,000 on a job, and the GC refused to pay until the certificate met expectations to the letter (or, better, punctuation mark).

Another agent estimates that 3 percent of the firm's commercial-lines revenue went to pay for certificate operations last year. That's a big chunk of agency profit being invested in an activity being provided to third parties virtually free of charge. The agent estimates the cost of issuing certificates is double the cost just three years ago due to the increase in, and complexity of, requests.

Unlike insurers that can increase premiums when expenses rise, agents have no way of passing along these costs unless they can (and are willing to) charge a fee for this service. If they charge a fee, they open a potential E&O exposure in that a fee might be construed as consideration, creating a contract out of the certificate that might be actionable against the agent. And the reality is that fees are not legally an option in many, if not most, states.

For many agencies, certificates have become a costly black hole that takes valuable time away from servicing customers while creating unnecessary expense for the agency. Essentially, the agency is providing a free service to a party (the certificate holder) with which it has no business relationship. Some certificate holders appear to view insurance agencies like government agencies that offer public services to which they're entitled.

In addition to operational costs, certificates create significant E&O costs. From not being a blip on the radar screen of E&O carriers just a few years ago, today as much as 15 percent of all commercial-lines E&O claims can be attributed to certificates of insurance and/or additional-insured issues. Consider three recent E&O claims:

- The insured requested an additional-insured endorsement as required by the construction contract, but the agent failed to obtain it. The claim was settled for \$180,000. (At least three independent studies indicate that 40-50 percent of all certificates that indicate additional insured status are incorrect.)
- In another claim, an agent used a blanket additional-insured endorsement. However, it required that AI status requests arise from written contracts. There was no written contract, so the blanket AI endorsement was not triggered. The cost to settle? \$445,000.
- In the third and last example, an account was nonrenewed, and the agent could not find another market. The insured found an E&S carrier, but the carrier couldn't or wouldn't issue certificates of insurance. As a favor to his former client, the agent used the firm's agency-management system to issue 4,000 certificates. As it turned out, the coverage was not actually in force. Following several accidents, including a fatality, an E&O lawsuit was filed. Settlement cost: \$10,290,000.

At the moment, there is a trial court case proceeding involving a flood loss where the certificate of insurance allegedly indicated more flood-insurance coverage than was actually provided. The amount at stake is \$150 million.

The costs associated with certificates of insurance are not trivial, whether you're considering operational expenses or potential E&O claims. To learn more about risk managing your certificates-of-insurance exposure, visit the Big "I" Virtual University's free Certificate Resource Center at www.iiaba.net/VU.

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