

**DEFERRED LOSSES IN LIABILITY INSURANCE.**

**Condensation of Valuable Paper, by Charles H. Neely, Appearing in the Recently Published Proceedings of the Insurance Institute of Toronto.**

To properly estimate the ultimate cost of outstanding claims is the most perplexing problem that confronts the casualty insurance underwriter in making up his balance sheet, for it may be said that therein lies the vital question of profit or loss.

In no other branch of insurance underwriting does this element of "contingent" or "outstanding" liability play such an important part, for in the nature of Employers' Liability, or Public Liability Insurance the value of any claim is undetermined until it has been adjudicated by a court of last resort or settled.

In liability insurance, aside from giving the original notice of accident, no limitations of time for making claim may be imposed upon the insured without nullifying in a great degree his protection under the policy. Moreover, the occurrence of an accident to the workman of an insured does not necessarily constitute a loss under the policy; there must have been not only accident but the facts and circumstances attending it must prove negligence on the part of the employer under the provisions of the Common law or legislative enactments of the Province in which the risk lies and therein are found the difficulties of the claims adjuster.

The first obstacle is the human tendency of the employer to minimize his fault and put the blame upon the unfortunate man who is injured. In his preliminary report of the occurrence that view is stated, and stoutly maintained throughout, until perhaps months or years afterward the evidence of the claimant is brought out in court.

The insurance company is further lulled into security by the statement that the injury is trivial, estimating the period of disability at a few days, and that nothing more will be heard of the case, when months or years afterward the injured makes claim for loss of hand or foot or mysterious internal injuries that will disable him for the remainder of his life. Thorough investigation by the company of each accident would prevent such surprises to a large extent, but the expense seems unwarranted and impracticable in so-called "trivial" cases and remote risks.

The value of the claim being based primarily on the extent of the disability, in the nature of things the worst claims are longest deferred, and so universally is this the case that settlements made within the year on any given year's business constitute a small percentage of the total incurred claims of the year, and woe to the underwriter who, finding a large balance of cash left over from his receipts and disbursements, passes lightly over the "outstanding" and distributes the funds in dividends; he may need them at a later date.

The following table has been prepared from an experience covering a large volume of premiums written and it shows what percentage of these premiums was paid out in losses during each year from the time premiums were received.

The table shows that the loss payments made in the years following the year in which the business was written amounted to 41.81 per cent., but there was no means of knowing that this would be the case when the company's books were closed at 31st December of the year the business was written. These results are remarkably similar to the

results shown by a well known actuary of the United States dealing with millions of dollars of premiums.

The table is as follows:

**RATE PER CENT. OF LOSSES TO PREMIUMS WRITTEN.**

Year.	Claims paid Each year.	Outstanding Total At end of each year.	Claims paid p. c.
1	9.28	41.81	9.28
2	22.48	19.33	31.76
3	10.48	8.85	42.24
4	6.24	2.61	48.48
5			51.09

The difficulties of estimating each case with any degree of accuracy are such as to render it impossible, and many plans of averages have been invoked by the different offices.

By some all "claims" are subdivided into three classes, viz.: "appeals," "suits" and "claims" and the average cost in each subdivision as shown by past experience is used as a basis for making the outstanding list. This system has its fault in two particulars. Certain "accidents" that were not considered "claims" at the time of making the list, will subsequently develop into claims, and perhaps suits or appeals; and many cases that were listed as "claims" will become suits or appeals, before settlement.

It therefore seems essential to a sound outstanding list that all known accidents should be dealt with on a uniform basis of average cost over a period of years, and with a view to the greater security of the public interest several of the American States, notably New York and Massachusetts have enacted legislation with the following requirements:

All accidents reported during a period of five years ending at least five years prior to the statement are taken into account—the gross sum paid thereon is shown and the average cost deduced. The number of accidents that resulted in suits, and the total cost of all suits are segregated therefrom, and the average cost per suit is found.

With this basis of averages made up from each company's experience, the law requires that a company shall show in its annual statement the total number of accidents reported to it during the last preceding eighteen months, this number is multiplied by the average cost of accidents as previously determined, and from the result is deducted the sum of all payments made on account of said accidents; the balance is carried to the outstanding account. To this is added the sum of all existing suits multiplied by the average cost of suits previously shown, and the total must be carried as a reserve for outstanding losses.

This comprehensive method of dealing with what may appear to the layman an unimportant element of the balance sheet, has appealed to the most experienced underwriters as the best known system of solving this vexatious problem, but it is not free from fault because of the enormously increasing tendency of claims due to the greater physical hazard of modern machinery, legislative enlargement of the workman's rights and socialistic spirit of jurymen, as well as the unscrupulous conduct of certain members of the legal and medical professions.

A higher appreciation of the subtleties of this contingent liability is essential to the conservative manager who wishes to escape the humiliation of confessing to his board that his reserves of the previous year have proven inadequate, and the present year's profit must be drawn from to supply the deficiency, perhaps to the extent of impairing the dividend if not the surplus.