

Claims Provisions

1.0 Purpose

- 1.1 This provision establishes the terms and conditions under which the reinsurer is liable for claims incurred under the reinsurance agreement.
- 1.2 The provision recognizes the ceding company's authority, and specifies any restrictions on that authority, in handling its claims under the reinsurance agreement.
- 1.3 The provision also covers the procedures the ceding company must follow in order to obtain claim recovery from the reinsurer.
- 1.4 Additionally, this provision may establish a basis for which any extra contractual damages that may be rendered against the ceding company are to be shared between the ceding company and the reinsurer for claims incurred on policies subject to the agreement.
- 1.5 The provision also addresses how the two parties are to share expenses of claim settlement, changes in the amount of insurance benefit due to misstatement of age and/or sex and other various matters.

2.0 Scope

- 2.1 This provision typically is intended to address issues surrounding a request for policy benefits payable by reason of the death or disability of the insured. Policy benefits available by way or exercise of any nonforfeiture provisions of a reinsured policy are normally covered under a different provision.

3.0 General Elements

3.1 Liability

Purpose: This section recognizes the reinsurer's liability under the agreement.

Scope: This provision defines the time period that the reinsurer's liability is effective and may define limits.

General Language - Liability – the liability for insurance benefits reinsured under the reinsurance agreement is normally restricted to the liability of the ceding company for such benefits as limited by the terms and conditions of the particular contract under which the ceding company is liable. The liability usually commences with that of the ceding company (new business). It may reference the effective date of the agreement (inforce business).

4.1 Variations

4.1.1 Per the ACLI Treaty Sourcebook, this language can vary depending upon type of reinsurance such as automatic versus facultative.

Automatic

“For automotive reinsurance, the Reinsurer's liability will commence at the same time as the Ceding Company's liability.”

Facultative

“For facultative reinsurance, the Reinsurer's liability will commence at the same time as the Ceding Company's liability provided that the Reinsurer has made a facultative offer and that offer was accepted during the lifetime of the insured, in accordance with the terms of this Agreement.”

4.1.2 It may limit the liability with language that says it will not extend past that of the ceding company and automatically terminates with the termination of the reinsurance or the death claim is paid or the recapture of a reinsured policy.

4.1.3 The provision may state conditions for the liability to become effective such as the reinsurer's receipt of an initial premium if such is due upon execution. (is this for the treaty or for an individual policy? conditional receipt)

4.1.4 The liability section can be a separate clause from the Claims provision.

4.1.5 The liability of the reinsurer is effective once execution of the agreement is complete.

5.1 Common Problems

- 5.1.1 Consistency between the definitions of “liability” used to address that under the treaty versus under a reinsured policy.

3.2 Notification

Purpose: This is usually the initial step that the ceding company must follow in the process of claims reimbursement.

Scope: This provision sets the parameters for how notice of a claim is given.

- 3.2.1 The ceding company is typically required to give the reinsurer prompt notice of any claim for benefits on a policy reinsured under the agreement. Copies of proofs or other documents bearing on such claims, along with a statement showing the amount of the claim, are normally required to be supplied to the reinsurer in support of the claim for benefits reinsured.
- 3.2.2 The ceding company is typically obligated to notify the reinsurer promptly of its intent to contest, compromise or litigate a claim involving reinsurance.
- 3.2.3 The ceding company is also normally required to provide the reinsurer prompt notice of any legal proceedings initiated against it in response to its denial of a claim on a reinsured policy.

4.2 Variations

- 4.2.1 For a contestable case and/or upon request of the reinsurer, the complete underwriting file might be supplied to the reinsurer in support of a claim for benefits.
- 4.2.2 Ceding company may send an initial notification. It is not yet a request for payment.
- 4.2.3 Same amount of information may be distributed with the notice regardless of the claim amount. Proof of payment, samples of death certificate.
- 4.2.4 Make a distinction between contested claims and death claim notice.
- 4.2.5 Contestable claims may distribute the complete underwriting file. And could also be sent for case of denial.
- 4.2.6 Contestable notice could be based upon an amount
- 4.2.7 Notice of contestable claims might be all contained within its own sub clause to the Claims clause

5.2 Common Problems

3.3 Good Faith

Purpose: This provision reinforces the representation of the ceding company and the reinsurer to their responsibilities to the policyholders in handling claims.

Scope: This clause is specific to how the parties handle their claims paying practices specific to the protection of the policyholder.

General Language - Good Faith - The provision normally provides for both parties to act in good faith in consideration of a claim for benefits on policies reinsured.

4.3 Variations

4.3.1 A contract is considered to be a contract of "utmost good faith" when the parties to the contract rely heavily on the honesty and integrity of each other.

This language is different from the representations clause in that it addresses how the ceding company and the reinsurer will work together in terms of the treaty such that the policyholder continues to be protected under his policy.

The duty assumes that both parties are sophisticated and knowledgeable in the insurance industry. As a result, they should be aware of what is relevant and necessary for the other party to know. The reinsured must follow the duty by disclosing all material facts to the reinsurer that relate to or affect the original policy and its calculated risk. The reinsured must essentially put the reinsurer in the same position as it would be in when deciding about the risks and the possibility of coverage on the original policy.

In addition, the duty requires that the reinsured act with honesty in negotiating any settlement with the original policyholder. If the settlement is not handled by following the appropriate business procedures, the reinsurer may not be bound by its terms and then does not have to pay under the policy coverage.

Lastly, the duty of utmost good faith requires the reinsured to provide adequate notice of any claim or potential claim to the reinsurer. For notice to be adequate, it should be given as soon as the reinsured becomes aware of a potential claim. To be aware, the reinsured must investigate with diligence to discover these possible claims. Notice is required to make the reinsured aware of the possible need for available funds in case a claim is filed. Notice also allows the reinsured to participate, if desired, in the defense of the underlying claim. Practically, reinsurers may also use the notice of potential claims to

determine renewal of, or change in, premiums under the reinsurance contract. The duty of utmost good faith that is part of reinsurance policies requires the reinsured and reinsurer to deal honestly with each.”

5.3 Common Problems

- 5.3.1 Is there any ambiguity with the interpretation of this language to that of the notion of “follow the fortunes” or extra-contractual damages, or contesting the payment.
- 5.3.2 Be sure to be consistent with any language that is expressed elsewhere in the treaty such as normally, a treaty would include a representations clause in which the ceding company and the reinsurer express intention to comply with the provisions in the treaty.
- 5.3.3 If the settlement is not handled by following the appropriate business procedures, the reinsurer may not be bound by its terms and then does not have to pay under the policy coverage.
- 5.3.4 Should this language be included specific to the claims process?
- 5.3.5 How does it relate to an “act in good faith” clause specific to the rest of the treaty requirements?
- 5.3.6 The reinsurance agreement may require the ceding company to act in good faith in settling any claim or suit. Often the determination of what constitutes good faith is ambiguous which can lead to disagreement between the two parties when attempting to resolve a large and/or difficult claim. The parties might well be advised to consider the question of what constitutes acting in good faith and what constitutes acting without good faith for claim settlement purposes while they are in the process of negotiating the reinsurance agreement.

3.4 Settlement of Death Claims – Ceding Company Limitations

Purpose: This section discusses the involvement of the reinsurer at the time of settlement of the death claim.

Scope: This section defines various claim periods (contestable, non-contestable) and suggests possible variations to consider when defining the role of the reinsurer at the time of claim payment to the beneficiary.

General Language - Limitations on the authority of the ceding company to settle claims – in indemnity reinsurance, the ceding company remains obligated to its policyholder and therefore has the responsibility to settle claims with the claimant. However, as the ceding company cedes a portion of each risk under the terms of the reinsurance agreement, the authority the ceding company maintains for the settlement of claims under the reinsurance agreement may be limited in various ways. Such variations are covered in item 4.2.

4.4 Variations

4.4.1 Noncontestable vs. contestable claims – Variation in the limitations on the authority of the ceding company to settle claims may extend from virtually unrestricted authority on noncontestable claims, or anywhere in between. Restrictions of authority may involve the ceding company having to obtain one or more of the following from the reinsurer before it is allowed to settle a claim for benefits under a reinsured policy:

- opinion
- concurrence
- advice/consultation
- recommendation
- approval
- direction

Note, the degree of the ceding company's obligation to the reinsurer before settlement is permitted has a direct bearing on the wording that will be acceptable to both parties in the area of extra-contractual damages – the greater the degree of control by the reinsurer, the more the wording might reflect reinsurer participation in such damages.

4.4.2 If a reinsurer specifies that the ceding company obtain some form of reply from the reinsurer before settlement of a claim, a time restriction

might be imposed on the reinsurer for delivery of the reply. Should the reinsurer not respond within the allowed timeframe, the reinsurance agreement might indicate the ceding company is then allowed to assume the reinsurer has no objection to the ceding company's contest or settlement of the reinsured claim.

- 4.4.3 Amount of coverage – Variation in the authority of the ceding company to settle claims might also depend on the amount of benefits at issue, either in absolute dollar terms (i.e., cases exceeding \$x of total benefit) or in the relative portions of benefits retained and reinsured (i.e., if the amount of retained benefit is less than the amount reinsured). The reinsurer might be particularly concerned about a case where the ceding company has no retention. Variation in such authority might also depend upon whether the case has been ceded on an automatic or facultative basis originally.
- 4.4.4 During the contestable period, the ceding company should promptly notify the reinsurer of its intention to investigate, contest, compromise or litigate a claim. The company should provide the reinsurer all relevant information and documents, as they become available, pertaining to the contested claim and should promptly report any developments during the reinsurers review.
- 4.4.5 While the policy is in the contestable period, the ceding company should perform an investigation into the legitimacy of the claim. Depending upon the location of the death, various methods of confirmation can occur (phone calls, personal visits, photographs, etc.)
- 4.4.6 If the reinsurer opts out of any contest or litigation for the claim, they have the obligation to pay their portion of the reinsured amount. Payment of this benefit amount will also preclude them from sharing in any expenses incurred due to the contest or litigation, from the point the reinsurer notifies the ceding company of its desire to withdraw from the contest or litigation. Opting out of the contest or litigation also disallows the reinsurer from sharing in any reduced liability that might be determined through the contest or litigation.
- 4.4.7 If the reinsurer agrees to be a party to the contest or litigation of the claim, they will also share in any reduction or increase in liability determined through the contest or litigation.
- 4.4.8 If a dollar limit of benefit is used to define the involvement of the reinsurer, a need to define whether the limit covers the full benefit of the policy or the reinsurer's share should also be considered.
- 4.4.9 Regardless of any limits defined in the treaty for contestable claims, the reinsurer should be able to request and receive whatever paperwork they deem necessary to justify payment of the claim.

5.4 Common Problems

5.4.1 How much paperwork should be sent for contestable claims?

Duplication of massive files from underwriting or the issue process may not be necessary.

Does anything special need to be considered regarding denied claims during the contestable period that were not approved by the reinsurer for denial? Specifically, if it's chosen not to include the reinsurer in the review of contestable claims, or there is a limit to their involvement and the ceding company subsequently denies the claim, should the reinsurer be notified of the denial at that time? If so, how much information should be shared with the reinsurer regarding the denial?

3.5 Expenses

Purpose: The purpose of this section is to give some guidelines regarding the amount of expenses that can be reimbursed by the reinsurer

Scope: This provision defines the various types of claim expenses that can be reimbursed from the reinsurer, with various guidelines to the limit of the expenses allowed.

General Language - Expenses – In the event a claim for benefits is contested, compromised or litigated, the reinsurer is normally required to share the payment of specific claim expenses involved, unless it declines to participate in the denial of the claim (see item 3.11).

Typically the reinsurer participates only in unusual expenses incurred in the assertion of defenses to the policy and then only in the proportion that the reinsured benefit amount bears to the total benefit amount under the policy. Normally, routine investigation and/or administration expenses, including salaries of home office personnel and interpleader expenses are not covered.

4.5 Variations

4.5.1 Provided a third party performs investigations, routine investigation expenses are typically covered under the treaty. The definition of expenses that are covered can be summed up as “all expenses from third parties that are incurred in the contest, compromise or litigation of a death claim”. This can include legal expenses as well as investigation expenses.

4.5.2 A reference to the amount of the expenses as “reasonable” should be made.

4.5.3 If any punitive, exemplary, extra-contractual or similar damages, fines or penalties, statutory or otherwise are assessed against the ceding company as a result of acts, omissions, or course of conduct committed by the ceding company, the reinsurer may not be a party to these expenses unless they were actively involved in the decisions of the ceding company.

5.5 Common Problems

5.5.1 What is the definition of “unusual” expenses?

5.5.2 How much validation of the third party expenses should the reinsurer be allowed?

3.6 Amount

Purpose: The purpose of this section is to define the amount of the benefit to be paid by the reinsurer to the ceding company upon the death of the insured.

Scope: This section will discuss normal amounts of benefits to be paid as well as other scenarios that can cause different amounts to be paid.

General Language - Amount – The reinsurance agreement might limit the total amount the ceding company recovers from all reinsurers on a claim to an amount that does not exceed the amount the ceding company pays the beneficiary for the claim. This would include any prepayment due to accelerated benefits. If such amount is exceeded, the agreement will provide for return of such excess to the reinsurers in proportion to their participation in the risk.

3.6.1 Changes in amount – Reinsurance agreements normally indicate that if the amount of insurance benefit provided the beneficiary is increased or reduced due to a misstatement of age or sex of the insured that is established after death, the reinsurer will share such increase or reduction in proportion to the relationship of the reinsurance liability of the total liability on the policy proper to the discovery. Typically the agreement will provide that adjustments of premiums for prior coverage in such cases are made without any adjustment of interest.

3.6.2 Contested claims – If the ceding company's contest, compromise or litigation results in a reduction in its liability, unless the reinsurer has bailed out of the claim the reinsurer normally will share in the reduction in the proportion that the reinsurer's net liability bears to the sum of the net liability of all reinsurers on the insured's date of death.

3.6.3 Misrepresentation or suicide – If a misrepresentation on an application or death by suicide results in the return of policy premiums by the ceding company rather than payment of policy benefits, the reinsurer will normally refund to the ceding company all of the reinsurance premiums paid for that policy. If a death of an insured by suicide results in payment or reduced policy benefits, the reinsurer will pay its share of the reduced policy benefits.

4.6 Variations

4.6.1 Payment is made in one lump sum regardless of the mode of payment made to the beneficiary.

4.6.2 Any interest paid to the beneficiary can also be charged to the reinsurer. This is charged in the same proportion as the relationship for the net amount at risk.

- 4.6.3 For waiver of premium claims, the company will continue to pay premiums for reinsurance except premiums for disability reinsurance. The reinsurer will pay its proportionate share of the gross premium waived by the company on the reinsured policy, including its share of the premiums for benefits that remain in effect during disability.
- 4.6.4 For claims on accelerated benefit riders reinsured under the agreement, the benefit amount payable by the reinsurer will be calculated by multiplying the total accelerated death benefit payout by the ratio of the reinsured net amount at risk to the face amount of the reinsured policy.
- 4.6.5 Any legal expenses or investigation expenses incurred during the settlement of the claim can also be requested at the time of the payment of the base claim (See Section 3.5 for discussion on expenses)

5.6 Common Problems

- 5.6.1 Is there a need to discuss the timeliness of the claim payment? What is reasonable?
- 5.6.2 At what point is reimbursement sought from the reinsurer – once the claim has been approved for payment to the beneficiaries, or after all the beneficiaries have been paid?
- 5.6.3 Difficult to distinguish in ceding company reinsurance reporting when a policy goes on waiver. Ceding company reporting varies. Some use a claim status to indicate a policy is on waiver in administrative reporting and may or may not indicate the amount. Others do not reflect it in the administrative reporting but submit claims documentation. It can be difficult to distinguish if a policy event is indeed a waiver or another policy event such as a policy reduction or risk amount change.
- 5.6.4 Another issue that might be prudent to address during the process of negotiation of the reinsurance agreement is the issue of accelerated benefits. Although the ceding company may not now accelerate benefits on any reinsured policies, it is possible the ceding company might want to change its position at some future point. The two parties are advised to establish a dialogue on this issue before it arises as it may require a modification to agreement language.
- 5.6.5 Recapture and reductions resulting from remaining risk ceded specifics should be included in the appropriate articles.

5.6.6 When accelerated benefits are not covered by the treaty, the Ceding Company will at times reduce or pay a benefit and reduce the face amount on the direct admin system. This reduced amount is then passed through to the reinsurance system resulting in a drop in the face amount reinsured, which it is difficult for the reinsurer to identify. At times it is not discovered until claims time when the ceding company bumps the amount back up to full face amount for reimbursement.

3.7 Lump sum payment

Purpose: This section details the final step in the claims process; settlement of claims benefits to the Ceding Company.

Scope: This provision defines the mode(s) that the reinsurance agreement specifies for final payment.

General Language - Lump sum payment - Usually the payment of death proceeds by the reinsurer will be made in a single sum regardless of the ceding company's mode of settlement options. Refer to item 5/6 for comments concerning accelerated benefits.

4.7 Variations

4.7.1 Although the reinsurer typically settles claims paid by reason of death in a single sum regardless of the mode of settlement the ceding company uses with the beneficiary, payments required due to the disability of the insured are typically paid by the reinsurer on an agreed-upon periodic basis. Reinsurer usually prefers to pay once a year, despite the mode of settlement of the ceding company.

4.7.2 Payments – If the frequency of claims on a block of reinsurance is large, it might be practical to settle claims on a batch basis rather than individually. Such a variation should be defined in the reinsurance agreement.

4.7.3 Interest for payment delays of the reinsurer to the ceding company on lump sum death proceeds might be made at rates other than those payable by the ceding company to the beneficiary. The two parties must negotiate a rate agreeable to the situation.

4.7.4 If netting claims from premiums is allowed, it is sometimes provided the party that seeks to avail itself of this right of offset is not in breach of any provision of the agreement.

4.7.5 Partial Payments – though not typically outlined in the treaty, frequently due to the inability of the Ceding Company to locate all the beneficiaries or the existence of a minor beneficiary a partial payment is made. The pending portion is pending sometimes long periods of time or even many years. The reinsurer prefers to pay the entire benefit to the Ceding Company in one lump sum rather than managing pending files/amounts for lengthy periods of time and paying interest

5.7 Common Problems

3.8 Interest

Scope: This section details the final step in the claims process; settlement of claims benefits to the Ceding Company.

Purpose: This provision sets the parameters for when and what interest is paid by the reinsurer.

Interest – It is normal for the reinsurer to reimburse state-required interest on its proportionate share of the ceding company's claim proceeds except where otherwise specified or negotiated.

3.8.1 The two parties may also agree to additional interest paid by the reinsurer to the ceding company if the reinsurer's claim reimbursement is delayed beyond some defined period. The parties might tie this interest item to a similar interest item for overdue premiums under the reinsurance agreement.

4.8 Variations

4.8.1 When Misrepresentation or Suicide or Misstatement of Age or Gender, refund net premiums minus interest or make adjustments without interest respectively.

5.8 Common Problems

3.9 Waiver of Premium

Scope: This section details the final step in the claims process; settlement of claims benefits to the Ceding Company.

Purpose: This provision defines the mode(s) that the reinsurer's specify for waiver benefit payment.

General Language - Waiver of premium – Under a waiver of premium benefit, the reinsurer typically requires the ceding company to continue to pay premiums for the life reinsurance coverage, waiver benefit for the duration of the waiver claim period is not paid, and then returns a benefit amount as a reinsurance benefit. Such arrangements might be noted in the reinsurance agreement.

4.9 Variations

4.9.1 Waiver of Premium - The Reinsurer will pay waiver benefit annually regardless of the frequency of payment to the claimant. Cover recapture implications in the Recapture Clause.

5.9 Common Problems

5.9.1 Difficult to distinguish in ceding company reinsurance reporting when a policy goes on waiver. Ceding company reporting varies. Some use a claim status to indicate a policy is on waiver in administrative reporting and may or may not indicate the amount. Others do not reflect it in the administrative reporting but submit claims documentation. It can be difficult to distinguish if a policy event is indeed a waiver or another policy event such as a policy reduction or risk amount change.

5.9.2 Ceding company discontinues paying life reinsurance premiums during a waiver claim period, when only the waiver premiums should be waived during the benefit period.

3.10 Refund of Premium

Scope: This section recognizes that there may be unearned reinsurance premiums as of the date of death may be handled.

Purpose: This section just states how unearned premiums may be handled.

Refund of premium – reinsurers may refund any reinsurance premiums unearned as of the date of death. If such refunds are made under the reinsurance agreement, they are typically made without any adjustment for interest.

4.10 Variations

4.10.1 Refund of Premium - Reinsurers may not be required by the treaty to refund unearned reinsurance premiums. Refunds of unearned premiums may include interest.

5.10 Common Problems

3.11 Opt Out

Scope: This section recognizes the reinsurer's option to avoid participation in a claim denial.

Purpose: This section defines the reinsurer's right to opt out of a claim contest, compromise or litigation, states the procedure for opting out, and specifies the parties' rights in the event of an opt out.

General Language - Opt Out – If the ceding company contests, compromises or litigates a case reinsured under the agreement and the reinsurer does not want to participate in the denial of the claim, the reinsurer may be provided the option to pay its share of the benefit to the ceding company and fix the amount of its settlement at that point. If the agreement provides this option to pay its share of the benefit to the ceding company and fix the amount of its settlement at that point. If the agreement provides this option and the reinsurer chooses to exercise it in a claim situation, the reinsurer would not participate in any adjustments to the settlement (in either direction) as a result of litigation thereafter.

4.11 Variations

5.11 Common Problems

5.11.1 The ceding company should consider whether inclusion of a opt out provision will cause problems if it disputes a claim after its reinsurer has bailed out. If a reinsurer pays its share of a claim but the ceding company continues to defend the claim, the claimant may discover that the reinsurer has bailed out and try to sue that fact against the ceding company.

5.11.2 Issues arise surrounding how much time the reinsurer has to make a decision whether to opt out. Typically, the ceding company has a legal or regulatory obligation to make a timely claim decision. This sometimes does not allow the reinsurer sufficient time to make an informed and reasoned decision as to whether to opt out.

5.11.3 Issues also arise as to how much information the reinsurer is entitled to receive from the ceding company in order to make an informed decision.

5.11.4 In the event that there is not full disclosure by the ceding company at the time the reinsurer is required to make a decision, the reinsurer may have the right to subsequently opt out at a later date upon becoming fully informed.

5.11.5 In cases where the reinsurer opts out of a claim denial, that fact, along with any communication of the opt out decision or the reasons for the decision could be discoverable in litigation.

3.12 Extra-contractual payments –

Scope: This section addresses the issue of responsibility for extra-contractual liabilities.

Purpose: This section discusses the numerous issues and considerations regarding whether the reinsurer is liable for extra-contractual payments, and how those payments are apportioned.

General Language - Extra-contractual payments - Negotiation of acceptable reinsurance agreement language for this item can prove to be a challenge. Reinsurers agree to indemnify ceding companies for the economic losses which flow from the issuance of a reinsured policy. This, extra-contractual damages are outside the basic contractual liability of the reinsurer. Any discussion regarding extra-contractual damages are qualifications of this basic position

- 3.12.1 Some reinsurers prefer not to address the issue of extra-contractual payments in the agreement. In order to avoid problems situations later, the parties should discuss the matter and mutually agree whether silence implies that the reinsurer will or will not participate in extra-contractual payments. Other carriers consider silence in the agreement about this issue to be very dangerous and prefer to clearly establish the intent of the parties one way or the other in the written document.
- 3.12.2 There are a number of kinds of extra contractual payments: the ceding company might gratuitously pay amounts which it is not obligated to pay by the terms of the reinsured policy (“ex gratia payments”): the ceding company might be obligated to pay damages because of its intentional or negligent conduct (“punitive or exemplary damages”).
- 3.12.3 Most reinsurers decline to participate in ex gratia payments, while many though not all, are willing to pay their proportionate share of compensatory damages. The most difficult area of negotiation typically centers on the issue of whether the reinsurer will participate in punitive or exemplary damages.
- 3.12.4 Some reinsurers explicitly state they will have no liability for any punitive or exemplary damages assessed against the ceding company as a result of a claim based on alleged or actual bad faith, failure to exercise good faith or tortuous conduct. Expenses incurred in connection with claims for punitive or exemplary damages are also excluded.
- 3.12.5 There are two ways of thinking about how, as an exception to the general rule in 3.12.4, a reinsurer might participate in punitive or exemplary damages. First, a ceding company might request a

reinsurer to provide insurance on the risk that the ceding company might be obligated to pay punitive or exemplary damages. The coverage in this instance is more akin to insurance than to reinsurance (since to be reinsurance the initial loss had to be incurred in connection with a policy benefit), and is more of a casualty benefit than a life benefit (since the insured event is tied to the malfeasance of the ceding company and not to a mortality or morbidity risk). It could be that a separate premium is required for this type of coverage.

- 3.12.6 Second, a company might request the reinsurer to bear responsibility for the consequences of the reinsurer's involvement in the in the actions which give rise to any punitive or exemplary damages assessed against the ceding insurer. Thus, some reinsurers state that while they are not liable for punitive or exemplary damages as stated in 3.12.4., there may be special circumstances involved which could indicate the reinsurer should participate in punitive or exemplary damages and related expenses, and further state that such circumstances are difficult to define in advance, but are generally cases where the reinsurer was an active participant in the act, omission or course of conduct that ultimately resulted in the assessment of the punitive or exemplary damages and expenses. Such division might vary in proportion to the benefit liability of each party of an assessment of each party's role in the particular case.
- 3.12.7 It is important to note that the working of the provision dealing with punitive or exemplary damages should reflect the amount of freedom, or lack thereof, that the ceding company has to settle reinsured claims without being bound by the reinsurer's involvement. It is also important to note that a distinction can be made between extra-contractual damages which flow solely from the decision to deny a claim and such damages that flow from execution of that denial. While ceding companies and reinsurers may limit the amount of freedom that the ceding company has to deny a claim without reinsurer involvement, typically execution of the decision to deny is within the ceding company's freedom. Therefore, if punitive damages are assessed against a ceding company due to its execution of a denial of a claim, even reinsurers that included wording in 3/12/6 will not share in such punitive damages.
- 3.12.8 It is also important to note that if the reinsurer does agree to participate in punitive or exemplary damages as set forth in 3/12/6 above, its participation is probably limited to "claims-related" punitive or exemplary damages. If punitive or exemplary damages are assessed against the ceding company in connection with other aspects of the reinsured policy (for example, with respect to problems surrounding the underwriting, issue or administration of the policy), the reinsurer will not participate in these damages because it was not an active party in any of these acts.

4.12 Variations

5.12 Common Problems

- 5.12.1 Companies might attempt to anticipate problems associated with inclusion of the provision referred to in 3.12.6 of this checklist. Rather than define those circumstances which will obligate the reinsurer to participate in punitive or exemplary damages, the provision leaves the matter open to future determination. Also, the term "active party" is not defined. As pointed out in 4.2.1 of this checklist, the relationship between the ceding company and the reinsurer may vary quite significantly. Both parties are advised to agree in advance upon the circumstances which will impose the status of "active party" upon the reinsurer.
- 5.12.2 There is not complete acceptance of the distinction contained in 3.12.7 between extra-contractual damages that flow from the decision to deny a claim and those that flow from the execution of that denial. The parties are advised to be aware of a potential for disagreement on this issue.
- 5.12.3 It is unfair to expect the reinsurer to assume a proportionate share of extra-contractual liabilities since the reinsurer is not in a position to control exposure to extra-contractual liability. The reinsurer has no ability to select, train or supervise the sales force or claim administration personnel, has only limited knowledge of the ceding company's claims administration practices, and is not involved in the actual administration or investigation of the claim.
- 5.12.4 Agreeing to liability for extra-contractual payments could violate the charter of the reinsurer, since the reinsure is then put in a position of an errors and omissions /property and casualty insurer.
- 5.12.5 Requiring the reinsurer to pay a proportionate share of extra-contractual payments could have the effect of removing an incentive to properly administer claims, especially in cases where the ceding company has a very small retention.

4.0 (General) Variations

5.0 (General) Common Problems

- 5.1 The parties should address how to coordinate claims activities effectively if there is more than one reinsurer involved. Failure to effectively anticipate this issue can lead to difficult circumstances on individual claim situations.
- 5.2 The checklist addresses issues that arise on claims of single life plans. Special wording may be required to properly handle joint life and/or second-to-die plans. For example, such plans may require unique wording to handle such items as simultaneous death, jump in cash values on the first death or the important issue about notification of the reinsurer upon the first death.
- 5.3 Another issue that might be prudent to address during the process of negotiation of the reinsurance agreement is the issue of accelerated benefits. Although the ceding company may not now accelerate benefits any reinsured policies, it is possible the ceding company might want to change its position at some future point. The two parties are advised to establish a dialogue on this issue before it arises as it may require a modification to agreement language.
 - 5.3.1 Recapture and reductions resulting from remaining risk ceded specifics should be included in the appropriate articles.
 - 5.3.2 When accelerated benefits are not covered by the treaty, the ceding company will at times reduce or pay a benefit and reduce the face amount on the direct admin system. This reduced amount is then passed through to the reinsurance system resulting in a drop in the face amount reinsured, which it is difficult for the reinsurer to identify. At times it is not discovered until claims time when the ceding company bumps the amount back up to full face amount for reimbursement.
- 5.4 For a variety of reasons, the ceding company may not want to investigate a claim as thoroughly as the reinsurer considers appropriate. In the most difficult case, the ceding company might wish to pay a claim that the reinsurer thinks ought to be denied by the ceding company.
- 5.5 A ceding company and the reinsurer may not have reviewed certain issues of claim philosophy at the outset. For example, if the ceding company typically adjusts the death benefit in cases where a smoker has lied to secure coverage at more favorable nonsmoker premium rates and the reinsurer's position is to deny such claims, controversy is likely to develop.
- 5.6 Offset provisions – some companies prefer to include a reference to an offset provision in the article covering claims. Other companies prefer any such reference in a separate article. Still other companies prefer no such reference at all. The parties should negotiate to establish their position and document it in the treaty appropriately.