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UNDERWATER: Cleaning up Fraudulent Water Mitigation Claims

By Brian S. Tenzer, Esq.

Occupying top-of-mind awareness among property insurers, fraudulent water mitigation claims are on the rise nationwide. They are viewed as major concerns in many regions, including South Florida, where insurers fear fraudsters could destroy the homeowner insurance market by driving up rates, forcing the industry beyond the financial reach of most residents.

Some home insurance executives say rates across South Florida are expected to rise by six percent or more this year, largely because of a significant hike in non-catastrophe claims — a majority of them water loss claims that are inflated by unscrupulous water mitigation companies.

This is not to imply that all water mitigation companies are engaging in fraudulent activity. A majority of them act fairly and honestly. However, the old-school approach taken by many insurers toward fighting fraudulent enterprises, coupled with their reliance on government being able and willing to fix the problem, allows unscrupulous companies to charge excessive fees, bill for services that were not rendered, and charge for equipment that was never used.

In fact, many of these companies pay “finder’s fees” to plumbers, contractors — even insurance agents — generating false or inflated claims through an entire network of fraud. Many fraudulent water

mitigation companies create, or are part of, very sophisticated fraud networks. It’s no longer a case of just dealing with occasional problematic “mom and pop” businesses, so the old way of combatting this fraud no longer is an effective solution.

Complicating matters, it’s often difficult to determine fair payment for each water damage claim. There is no scientific model in use to calculate water mitigation costs, as there is for wind storm damage estimates.

Many in the insurance industry view the Assignment of Benefits (AOB) as the primary culprit in the escalation of water mitigation fraud. The provision enables an insured to enter into a contract that directly transfers all rights to the insurance benefits regarding water damage to the water mitigation company, including the filing of a lawsuit against the insurer to collect those benefits.

Over the course of several years, the industry has sought to reduce the problem by restricting the right to assign post-loss benefits. Legislative relief is not a viable option as it is both a lengthy and uncertain process. Beyond that, rarely, if ever, does government regulation stop a bad person from committing insurance fraud.

Additionally, courts have ruled against

any infringement of contracts they consider legal and that have been accepted as legal contracts for more than 100 years. Opponents of legislation argue there is no substantive proof that AOBs cause fraud.

So, what's an insurance company to do?

- First, re-direct the focus. Assignment of Benefits provisions are not the problem — fraudulent companies are and they will continue to exist and submit fraudulent claims with or without any restrictions on the assignment of benefits. Carriers should stop trying to fight fraud by eliminating AOBs and, instead, identify the companies that consistently submit fraudulent claims, then focus on stopping the problem at its source.
- Start by examining which companies have the largest financial impact on the carrier. Bigger doesn't necessarily mean bad, but they should start where the stakes are highest if they hope to keep the bottom line from bleeding money. Then, find those high-impact

companies that have been shown to submit inflated claims on previous occasions, or who conveniently dispose of damaged pipes, preventing inspection of the actual damage, and focus their efforts on those companies.

- Identify suspect water mitigation claims early and develop an efficient internal structure to collect and distribute information. Insurers need to develop standard operating procedures that facilitate early contact with the insureds to authenticate the extent of damages and to verify work performed by water mitigation companies.
- Develop standard questions for recorded statements by adjusters in order to determine the number of days mitigation actually occurred on site, confirm how many employees and machines were used, and how often they were checked.
- Assign specific in-house and field adjusters to investigate these claims so they are sure to follow proper protocols; are better able to identify trends,

associations with plumbers and other contractors; and all relevant information is efficiently shared up and down the chain of command.

Insurance companies and their investigators also must recognize that mitigation companies don't work alone. Identifying the fraudulent mitigation company is like uncovering just the tip of an iceberg. In most cases, active fraud participation extends beyond the mitigation company to a much larger network — everyone from rebuild contractors and plumbers, to public adjusters and even insurance agents. Many unscrupulous mitigation companies pay finder's fees to plumbers and insurance agents for profitable referrals — passing on that expense to the insurer.

For example, a plumber who replaces leaky pipes can easily earn four times or more what he made on the job by telling the customer there could be unseen water damage. If the customer is worried and wants the area checked out, the plumber recommends the mitigation company paying him the finder's fee. That compa-

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-William "Bubba" Ryan, CEO

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ny could then bill the insured's carrier for work that didn't need to be done, or for work that was never even done.

Insurers must understand that to successfully combat fraudulent water mitigation claims they must identify and investigate these relationships, as well as eliminate the entire network.

How do you identify a network of operatives in a water mitigation scam? A performance trend analysis may be the solution. Simply put, it's doing a thorough examination of everyone and everything involved in the mitigation and restoration.

- Review all the documents associated with the claim. Carefully examine all businesses and service people involved — how many times has that person or group of people been involved in a series of claims? Do the same people collaborate on mitigations more often than can be attributed to coincidence? Are their bills higher than most others?
- Look for trends or commonalities that suggest intent. Compile the information gathered from these investigatory

forays to create a playbook for future cases. That way, you'll know what to look for, and what you may need to know even before you enter the discovery phase of a case.

- Use all evidence of trends to convince a judge or a jury that something the water mitigation company characterizes as a mistake, actually is a pattern and practice of the company with the intent to deceive the insurer and collect insurance benefits to which they are not entitled.

And just as you must identify all of the players in a mitigation fraud network before launching an investigation, you must attack them all when litigating the case. There are two good reasons for this.

First, like a multi-headed monster, cutting off one part of a damage mitigation network leaves the rest to continue the fraud, while the one damaged grows back. Second, there might not be enough evidence to file against the mitigation company or the head of the ring. However, by aggressively pursuing everyone involved in

the fraud, you may be able to get that evidence from someone else in the scheme.

It may be possible to find a back door inside the ring's operation that provides access to hidden information and provides the ammunition to take down the leader. It may also be possible to cultivate a valuable confidential informant who can provide inside information on additional scams.

A win-win in the battle against fraud

Also, examine all claims in the aggregate, rather than just the one case under consideration. Seek out examples that show the company in the client's claim, which used restoration business "X" or plumber "Y," used those same vendors in multiple other cases — particularly if one or more of those claims were deemed fraudulent. Finding a pattern of complicity that extends well beyond coincidence may help point the way to fraud.

Be judicious, but take certain cases to court. That accomplishes two things. It forces the mitigation companies to prove a loss is covered, and that their charges are reasonable. It also demonstrates to them, and others, that the company is willing to stand up to fraud and won't make payments on inflated claims. Many times those fraudulent companies will stop targeting your company and focus their efforts elsewhere — such as on carriers that do not scrutinize fraudulent claims as closely.

The time has passed for carriers or the industry to just yell "fraud!" and expect action. They need to demonstrate concrete evidence that fraud has been committed and exactly how much that fraud is costing individual consumers. Only then will it be possible to put a crimp in fraudulent mitigation claims, and only then will lawmakers be willing to take up legislation that helps curb such criminal activity. 🍷

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