
ERRORS & OMISSIONS

RISK MANAGEMENT ALERT

Can statistics give the wrong impression?

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It is possible that when your customers are determining what or how much coverage to buy, they want to get a better understanding of how often that coverage will be needed. Let's consider flood coverage, for example. The customer asks about the likelihood that their house will get flooded over the next few years. As their agent, you advise them that their house is located in a "1 in 100" flood zone, which means that over the course of the next 100 years, their house will be flooded once. "1 in a 100" sounds like fairly good odds, and makes a strong case to *not buy* flood coverage. As a result, the customer decides that flood coverage is not something they need.

This exact situation occurred in Minot, North Dakota, in 2010. A customer discussed their personal lines coverage with their insurance agent and, during the discussion of flood coverage, the customer was advised that they were in a "1-in-a-100-year flood area." The agent was being truthful as the last time the Souris River in North Dakota reached the highest level was in 1881, over 125 years earlier! Unfortunately, that "1 in a 100 years" occurred just one later in 2011. The levees were topped and over 4,000 homes were destroyed or damaged. So, it was actually "1 in a 129 years," except the following year was that year. An E&O claim was brought against the agency. This situation is not unique.

Another rare event took place in Charleston, South Carolina, in October 2015. It involved something that had a statistical chance of occurring of .1%, or "1 in 1,000 years." While most would conclude that an event with this type of statistical probability is highly unlikely, it did happen. A "once-in-1,000-years" rainfall occurred, resulting in widespread amounts of 15-20 inches and localized amounts of over 25 inches, mainly in the Charleston tri-county area. This led to significant property damage.

A key takeaway from these two events is that when discussing coverage with customers, whether an event is a "1 in a 100 years" or "1 in a 1,000 years," there may be a tendency for the agent or producer to not address the coverage since the chance of the coverage applying is so remote. This should not happen. Even if the chance of the event such as a flood, earthquake, etc. occurring is remote, agents and producers should still inform the customer of the availability of the coverage. Providing the customer with a proposal is the best approach as it forces the customer to make a decision about whether or not they want the coverage. If the agency does not mention the coverage, could it be viewed that they are essentially making the decision for the customer? The last thing you want is for the customer to come back after an uninsured loss and argue "If I knew the coverage was that inexpensive, I would have bought it."

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A key E&O loss prevention issue involves customer accountability. This should be a goal of every agency.

Have you ever had a customer ask for your advice about whether to buy certain coverage? This will often sound like “What would you do?” or “What do you recommend?” Agencies need to know how to answer these types of questions. Imagine if the agent in the above scenario commented that “If I were you, I wouldn’t buy it.” How is the customer going to feel after they have a claim that isn’t covered? It’s quite possible that they could bring an E&O claim against your agency alleging they relied upon your “poor” advice. It is probably best to say something such as “What I would do is immaterial. This is your home and you need to decide what coverage you purchase.”

Bottom line, interjecting statistics into the conversation with the customer should be undertaken with extreme caution. While statistics provide historical perspective, there is no way to know whether those statistics will continue the same pattern moving forward. Maybe in the example above, it would have been best for the agent to tell the customer, “that area has not been flooded in over 100 years, but next year could be that year.”

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