



U.S. P&C Law Departments Rate the Metrics They Use to Manage Costs and Performance

LexisNexis® Property & Casualty ALAE Cost Containment Survey



INTRODUCTION

Our July, 2015 survey of more than 90 U.S.-based property and casualty insurance company claims and law departments revealed interesting insights into the cost containment strategies top carriers are employing or plan to employ in order to better manage costs.

The July LexisNexis P&C Cost Containment Survey revealed that management of litigation costs, primarily early case assessment and defense, along with vendor and bill review costs, were critical priorities in the organization. Paying the right amount, to the right firm, for the right defense was a key driver of P&C operational effectiveness initiatives and investment decisions. And although a wide variety of cost-control initiatives are in use, there remain immediate opportunities for improvement with more wide-scale adoption of initiatives rated highly effective, such as volume discounts, flat fee arrangements, staffing control plans, electronic billing and even early case assessment.

NEW SURVEY DIGS DEEPER

After analyzing and reporting on those findings, we decided to probe deeper in order to learn more about the specific metrics U.S. P&C claims and/or law departments track to manage costs and to monitor the performance of staff and outside counsel.



Specifically, we wanted to learn which metrics people are tracking, how they rate the effectiveness of various metrics and which metrics they consider the most important. We also thought it would be helpful to know about Allocated Loss Adjustment Expense (ALAE) forecasts and associated cost-control initiatives that are currently in place or planned for deployment.

To find out, we conducted a second online survey of U.S.-based property and casualty insurance companies between September 22 and October 7, 2015. The survey focused on internal professionals handling litigation for the carriers, whether in the Claims or the Law Department. A total of 94 respondents, whose titles included VP of Claims, Attorney, Associate/General Counsel, Staff Counsel, Head of Litigation and others, participated in the survey. The outside counsel spend of the companies surveyed ranged from less than \$10 million to more than \$500 million.

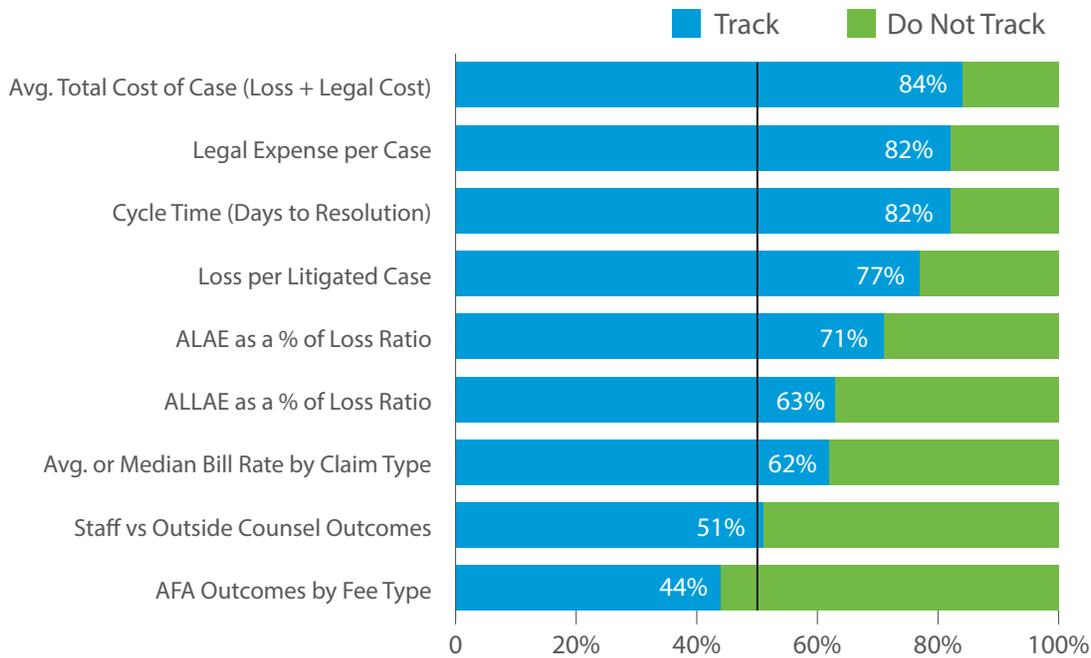
FORMALIZED METRICS AND REPORTING PROGRAMS THE NORM

We opened the survey by asking participants if their department focused on metrics to drive decision-making. Seventy-two percent responded, “Yes,” indicating that the majority of respondents view the ability to track, report on and leverage metrics as an important tool for facilitating litigation management and cost-control, and that they are leveraging that data to aid decision making. In the [LexisNexis Law Department Maturity Model](#), this puts nearly three-fourths of the respondents on the far right side of the model as being data-driven, meaning they consider data about their operations a key tool in their push toward effective litigation management and cost-control.

THE METRICS USED TO EVALUATE AND TRACK PERFORMANCE

What metrics are driving or being used by the P&C litigation management programs? We asked survey participants to indicate which of nine key metrics they track. We presented nine variables, including not just those used by law departments across all markets, but also including some specific to the property casualty industry, such as Loss Ratios, ALAE and ALLAE (Associated Legal Loss Adjustment Ratio). At least half of the respondents reported that they track eight out of the nine metrics we listed. (See *Figure A*) In descending order of usage, the top five metrics tracked are **Average Total Cost of Case** (84 percent), **Legal Expense per Case** (82 percent), **Cycle Time** (82 percent), **Loss per Litigated Case** (77 percent) and **ALAE as a % of Loss Ratio** (71 percent).

Figure A
Metrics Tracked to Help Manage Costs/Performance

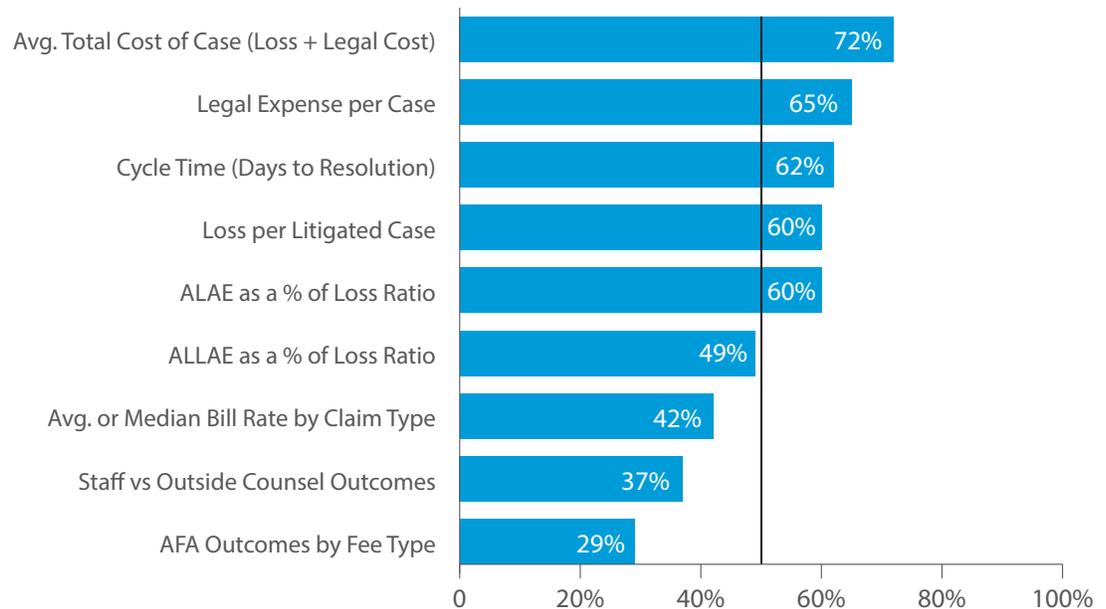


While 71 percent of respondents report that they track **ALAE as a % of Loss Ratio**, three out of five departments also track **ALLAE (Allocated Legal Loss Adjustment Expense) as a % of Loss Ratio**. This may indicate an increased focus on the legal portion of cost-control. ALAE reporting is required in the industry in order to understand combined ratios and free up reserves for investing. If there is a surprise here, it may be that it is not 100 percent. It is also possible that ALAE tracking occurs at a different level in the organization. ALLAE is a more specific number, looking at the cost of legal defense alone, and then tracking that against loss ratios. With the ubiquity of eBilling systems, it is now easy to isolate legal defense costs.

More than 60 percent of the claims departments surveyed report that they also track **Average or Median Bill Rate by Claim Type**. This metric cuts across both hourly rate discounts and staffing practices to provide an average rate. It is good to see the refinement of this metric around claim type versus tracking by firm alone. Similarly, some companies may push firms to use weighted billing averages. Weighted average bill rates, and median bill rates that track hourly rates only, are only part of the picture in that they show control over rates, but may not reflect a difference in total cost of defense. Again, the widespread use of eBilling makes this an easy metric to grab.

Half of the respondents report tracking **Staff vs. Outside Counsel Outcomes**. This is a key finding, as staff counsel is in widespread use at some carriers and is routinely considered to be more cost effective for 3rd party defense. There is a disparity between the general industry stance of the value of staff counsel and the number of carriers reporting that they track it. This may be a place where there is room for more data-driven management. Only **AFA Outcomes by Fee Type** was reportedly tracked by fewer than 50 percent of the survey respondents (44 percent). According to prior research, including the March 2015 CLM Litigation Management Study, AFA use is relatively steady, with little growth right now.

Figure B
Metric Effectiveness



RATING THE EFFECTIVENESS OF METRICS

We asked the survey participants to rate the effectiveness of the same nine metrics. Ratings for metrics characterized as either very effective or effective ranged from 29 percent to 72 percent, with no single metric dominating in terms of perceived effectiveness. (See Figure B) Five of the nine metrics used were rated either very effective or effective by more than half of those using them. The top five metrics in terms of rated effectiveness were **Average Total Cost of Case** (72 percent), **Legal Expense per Case** (65 percent), **Cycle Time** (62 percent), **ALAE as a % of Loss Ratio** (60 percent) and **Loss per Litigated Case** (60 percent).



Four metrics were rated as very effective or effective by fewer than half of the respondents. Although very near to the mid-point, **ALLAE** was rated either very effective or effective by 49 percent of those using the measure. **Average or Median Bill Rate by Claim Type** was rated very effective or effective by 42 percent of the survey respondents. Future studies may reveal whether one of these metrics is on the way up in its effectiveness rating while the other is on the way down, and if this snapshot is capturing that moment in time when they meet in the middle.

The two metrics rated either very effective or effective by the smallest percentage of respondents, **Staff Counsel vs. Outside Counsel Outcomes** (37 percent) and **AFA Outcomes by Fee Type** (29 percent) are the same two metrics that respondents reported using the least.

It is difficult to say if these metrics are not being used because they are not considered effective or if the use of these metrics is too new to this segment and the jury is still out on their effectiveness. The recent 2015 CLM Litigation Management Study reported that 39 percent of executives with staff counsel operations believe they do a better job of measuring outside counsel effectiveness than staff counsel, while approximately six percent felt they do a better job of measuring staff counsel. This indicates that the industry has a ways to go to truly assess staff counsel versus outside counsel outcomes. It is not necessarily easy to track staff counsel versus law firm outcomes as the data may reside in different systems, and management must declare it a strategic imperative with associated processes to enforce data collection and reporting.

From an AFA perspective, the recently released [LexisNexis 2015 Mid-Year Enterprise Legal Management Trends Report](#) indicates that overall industry AFA utilization remains relatively stable with 8.6 percent of corporate billings and seven percent of all matters under some sort of alternative fee arrangement. Legal work for the Insurance sector comes in above average with nearly 17 percent of matters and eight percent of billings under AFAs. Given the volume of commodity type work common in the Insurance sector it is surprising to not see AFA outcomes by fee types being utilized more. AFAs have played a larger role in the relationship between carriers and law firms than they have in the broader corporate law market, and may be coming back now that it is easier to get good data about results and cost. This is a place where eBilling systems are not necessarily helpful as many do not handle alternative fee engagements well, and instead use kludges and workarounds to jam them into the system. The risk for claims legal departments is twofold; a decrease in efficiency from having to use multiple processes and a loss of good data to report on costs and outcomes. Some carriers may be waiting for a system that grants them the same efficiency as their eBilling system, but allows them to track and report on AFA engagements and outcomes as well.

IN THEIR OWN WORDS: THE MOST IMPORTANT METRIC

Next, we asked respondents which of the nine metrics they considered to be the most important, and why. These answers demonstrate the holistic, yet data-driven approach in place at carriers today focusing on time and money. In descending order of rated importance, the top four metrics are: 1. **ALAE/ALLAE**; 2. **Cycle Time**; 3. **Average Total Cost of Case**; and 4. **Legal Expense Per Case**.

The verbatim responses revealed that carriers most value allocated loss adjustment expense and allocated legal loss adjustment expense as key indicators of performance and relevant to their decision-making about claim litigation. This is not surprising given that nearly three quarters track ALAE.

Among our survey group there is also widespread recognition that the second-highest-rated metric, **Cycle Time**, the duration of a case, is a very valuable metric for P&C claims departments. Does it make a difference to the business? While we may answer the question across segments of the insurance industry by looking at aggregate data, the survey respondents' verbatim responses tell us it is a critically effective metric for their own business:

"The number of days to resolution tracks multiple things such as efficiency of counsel, efficiency of claims handling, identifying cases for early resolution, evaluating timing of getting reserve to full value"

"Communicating with the customer is extremely important and delivering on the promise promptly and accurately customer service, retention and reduces litigation"

"By bringing claims to a rapid close, we can avoid legal expenses as well as claims costs per claim"

"The most important aspect is resolution for a client quickly"

"Cycle time shows difference between early settlements and verdicts"

Since every business has its unique components, tracking the amount of time it takes to close a matter forms the baseline upon which all initiatives can be measured. Cycle time is necessary for assessing success and measuring people, firms and expense performance. Knowing its own cycle times gives a claims department the ability to participate in the conversation about the value of speedy resolutions and get past the philosophical and into the practical – which helps it make an impact on its business.



The third most important metric according to our survey respondents is **Average Total Cost of Case**. The verbatim responses provide insights into why this metric is valued highly:

"...gives you a very good indication of the ability to leverage the legal system when the injuries are the same and the attorney handles the file correctly and the claims representative negotiates properly"

"I think the average total cost of case, provided there is a breakdown between cost and loss, and a review at certain points in the litigation where resolution was possible to determine if spending the additional costs is bearing fruit"

"Average cost per case - takes into play the whole picture"

"Total cost of case is most important -- a claim resolved early after thorough investigation usually is the best solution"

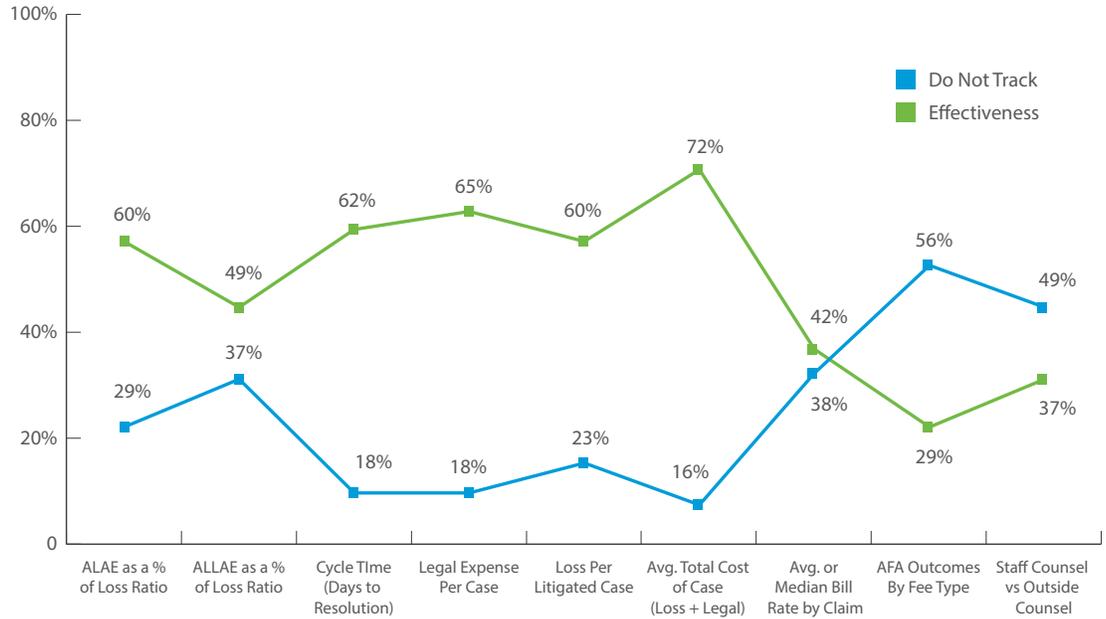
The fourth most important metric is more granular – **Legal Expense per Case**. The verbatim responses indicate that this metric is valued for a variety of reasons related to its generally predictive capabilities:

"Over varying jurisdictions it gives us a better handle on trends, types of claims and overall costs from the onset "

"Legal expenses per case to identify opportunities to impact investigations"

"Legal expense per case to know expenses for claims and as well as legal"

Figure C
Opportunity to Reduce Costs

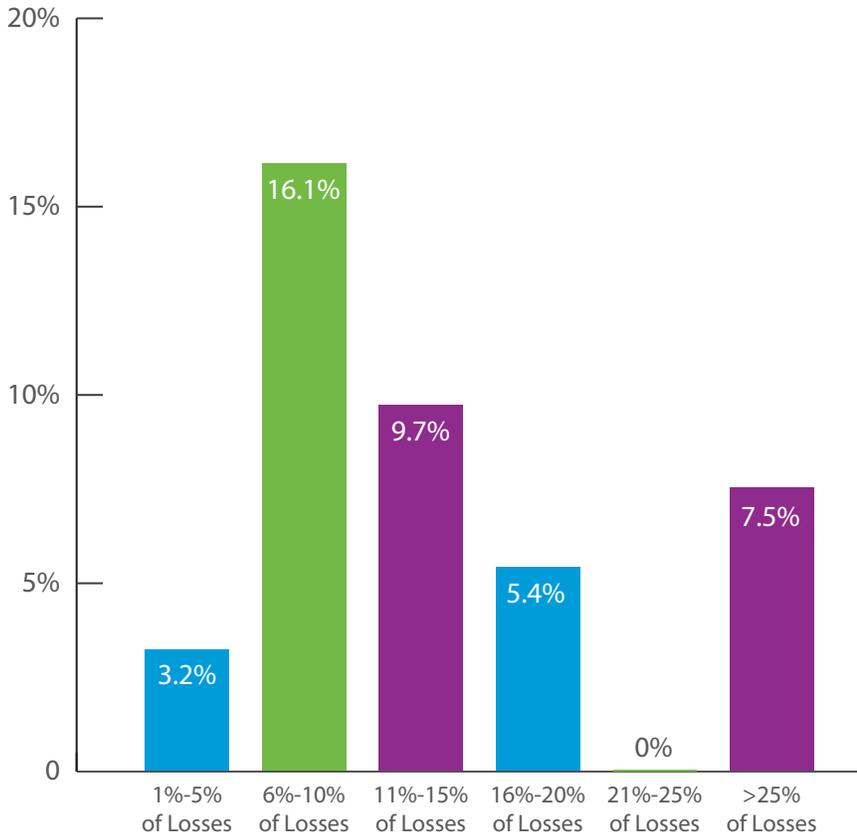


OPPORTUNITY TO IMPROVE PRACTICES

Where are the opportunities for improved practices and management? In light of the greater than 60 percent effectiveness ratings attributed to **Average Total Cost of Case**, **Legal Expense per Case**, **Cycle Time**, **Loss per Litigated Case** and **ALAE as a % of Loss Ratio**, it's reasonable to assume that claims and legal organizations that are not currently tracking these metrics could improve their management of litigation costs by doing so. (See Figure C)

Figure D

ALAE Percent of Losses 2014

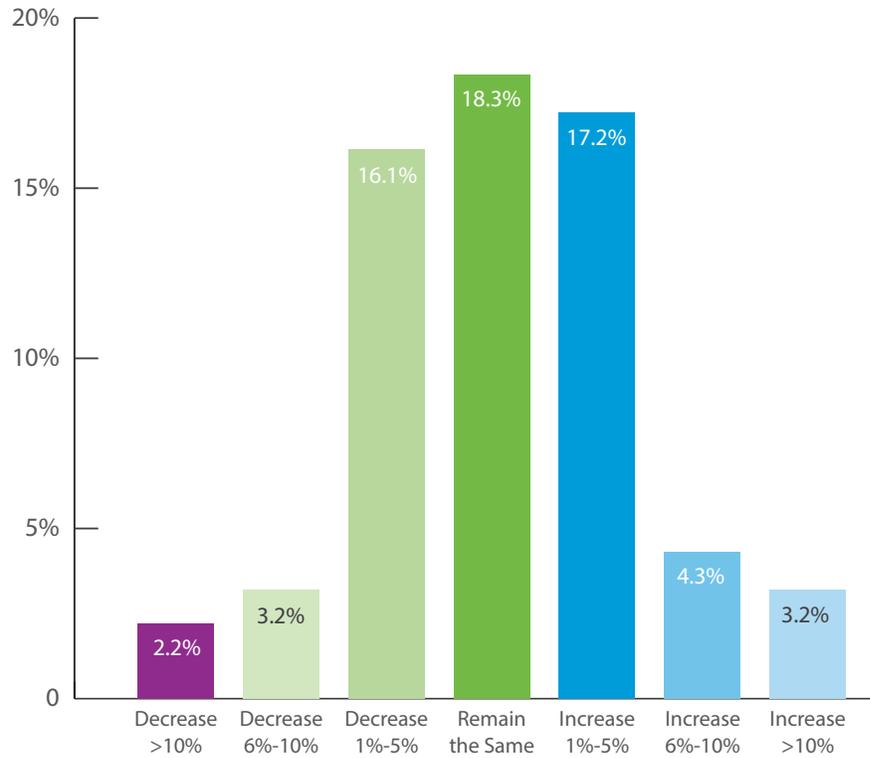


ALAE PERCENT OF LOSSES 2014

We asked the survey participants the following question: “On a company-wide basis for 2014, what percent did your Allocated Loss Adjustment Expense (ALAE) run to your losses?”

While fewer than half of the respondents were willing or able to share their ALAE ratio to losses with us on this survey, the results do hold some interest. (See Figure D) The largest group (16 percent) reported that their ALAE/Loss ratio was between six and 10 percent, with a combined total of just under 26 percent reporting a range of 6-15 percent. An additional 7.5 percent reported the surprising result that their ALAE ran above 25 percent of losses.

Figure E
ALAE Forecasted Change



ALAE CHANGE FORECAST

When we asked the survey participants how they expected their Allocated Loss Adjustment Expense (ALAE) to change in the next 12 months, a combined 18.3% percent responded that they believe ALAE will either remain the same, 17.2% believe it will increase one to five percent, and 16.1% believe it will decrease one to five percent. Half the respondents, therefore, expect no, or nearly no, change, while nearly equal numbers expect a 6% or greater increase in ALAE (7.4 percent) as anticipate a 6% or greater decrease in ALAE (5.4 percent)..

IN THEIR OWN WORDS: WHY THEY EXPECT ALAE TO CHANGE

The respondents' verbatim responses to our question about how they expect their ALAE to change reveal two distinct worldviews. Those who project a decrease in ALAE indicated that they believe that having effective cost controls in place (early identification, good relationships, front line management, etc.), would allow them to manage ALAE effectively.

Reasons for Decrease – Effective Cost-Control

"Controlling and managing more of the legal aspect of claims... provide more focused budgets and enforce compliance"

"Early identification of cases which should be resolved. Along with claims handlers actively pushing cases to trial or resolution"

"Establishing relationships w/select law firms in high volume areas; making sure that the anticipated expense will produce the desired outcome"

"Front line management of litigated claims"

"Different business partners are more efficient in handling claims"

Conversely, the verbatim responses of survey participants who expected ALAE to rise indicated a belief that they are largely responding to forces outside of their control (rising rates, case complexity, cycle time, explosive litigation, etc.).

Reasons for Increase – Outside Forces

"Rising rates and additional complexity in the marketplace which increases time for resolution"

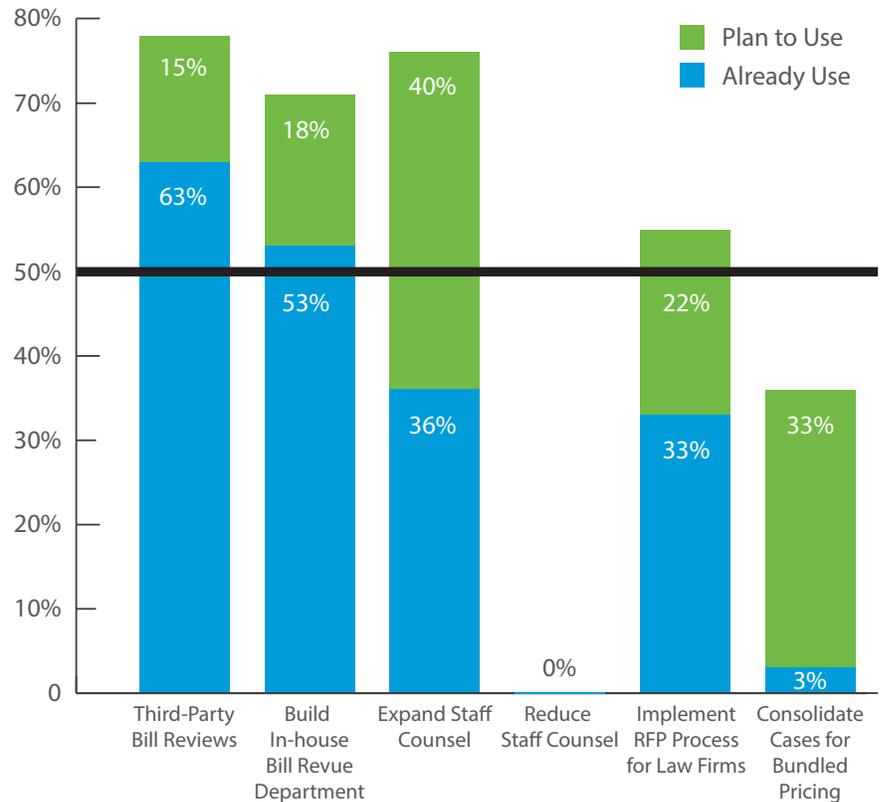
"Cycle time"

"Amount of litigation being forced by public adjusters"

"Explosive litigation"

"Increased expert fees and legal fees associated with coverage disputes"

Figure F
ALAE Cost-Control Initiatives



ALAE COST-CONTROL INITIATIVES for 2015

In response to a question regarding existing or planned cost-control initiatives aimed at Allocated Loss Adjustment Expense in 2015, sixty-three percent of respondents indicated that they currently use third-party bill reviews, with an additional 15 percent saying that they plan to implement such reviews in the future. In-house bill review departments are in place in 53 percent of the claims departments surveyed. An additional 18 percent responded that they planned to build an in-house bill review department. (See Figure F)

These figures are not surprising given the volume of invoices processed by P&C carriers. Our data indicates that bill review, whether in-house or via a third party, will continue to be integral to cost-control now and into the future.



Of more interest in terms of cost-control initiatives are respondents' plans around Staff counsel. None of the respondents reported that they planned to reduce staff counsel. In contrast, 40 percent said they plan to expand staff counsel, making it the second highest initiative planned to control cost. These responses reinforce a finding from the 2015 CLM Litigation Management Study, which reported that 53 percent of executives with staff counsel operations believed that staff counsel usage would increase industry-wide over the next five years.

This has implications for the points raised above, which is that effective measurement needs to be put in place for carriers to use data to assess the effectiveness of this strategic approach.

As far as other initiatives are concerned, 33 percent said they already have an RFP process in place for law firms and an additional 22 percent plan to implement an RFP process. And while only three percent reported that they currently consolidate cases for bundled pricing, 33 percent indicated their intent to implement case consolidation in the future. Both of these initiatives have impact on the business landscape for law firms supporting the P&C insurance market.

IN THEIR OWN WORDS: HIGHEST PRIORITY COST-CONTROL INITIATIVE

Finally, we wanted to probe deeper into our survey respondents' thoughts on managing litigation costs. We asked them to tell us, in their own words, what they regarded as their highest priority when it came to a cost-control initiative. To facilitate our analysis, we grouped the open-ended responses into four general categories: **Bill Review, Early Claims Resolution, Innovate and Contain Legal Costs/Expenses**. Broadly speaking, the respondents expressed a belief that proper management, supported by actionable analytics, would allow them to better manage costs. A sampling of the grouped verbatim responses follows:

Early Claims Resolution

"Settle claims prior to having claim going to suit"

"Resolve case timely versus litigating on clear liability and paying double"

Innovate

"True RFP process for outside counsel and further analytics comparing cases managed internally vs. externally"

"Requiring legal budgets"

"Legal spend analysis"

"Law firm convergence"

"Consolidate cases for bundled pricing"

"Flat fee charges with certain firms on standard cases or on cases where settlement docs and very little else needs to be done"

Contain Legal Costs/Expenses

"Managing vendor costs, such as court reporters and experts"

"Expert expense control"

KEY TAKEAWAYS

Our survey of the metrics that U.S. P&C insurance company claims/law departments track revealed several key insights:

- 1 Claims legal departments are data-driven organizations, which puts them on the right side of the LexisNexis law department maturity model.
.....
- 2 Litigation management is a top priority for the majority of P&C claims departments.
.....
- 3 Tracking metrics can continue to provide opportunities to reduce costs.
.....
- 4 The majority of respondents don't expect ALAE to change significantly in the next 12 months.
.....
- 5 The level of litigation management control in place is key to ALAE projections.
.....
- 6 As staff counsel grows, the importance of tracking outcomes and measuring effectiveness will increase.

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The CounselLink solution is an Enterprise Legal Management solution suite for matter management, legal spend management, legal hold, analytics and strategic consulting services. LexisNexis CounselLink Solution is positioned in the “Leaders” Quadrant of the Gartner’s Magic Quadrant for Enterprise Legal Management and has earned an industry reputation for helping to improve legal department performance and outcomes.

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