

APPRAISAL VALUATION PROBLEMS INHERENT IN ADJUSTING JEWELRY CLAIMS

By John J. Camozzi, Esq.¹ c 1993

It is estimated that the domestic insurance industry pays over \$1 billion annually in jewelry claim settlements.² Two of the most common problems inherent in adjusting jewelry claims are valuing lost items and reconciling inconsistent appraisals. This article will briefly examine each of these problems in the context of gemstone jewelry claims from the perspective of the claims representative, and will offer suggestions for the underwriter that could minimize their effect.

Lost jewelry creates the most difficult adjusting problem. The underwriter will usually require the insured to submit a written appraisal of value before issuing the policy. This appraisal is usually obtained by the insured at the local retail jewelry store where the item was first purchased, and is often nothing more than a modification of the original sales receipt with an inflated value. In most instances, the retail jeweler is not trained by the Gemological Institute of America ("GIA") in the art of identifying and grading gemstones. Frequently, the retail jeweler will have no formal training. In those instances where the original retail jeweler prepares an appraisal apart from the sales receipt, the retail jeweler is bound by the appearance of propriety to legitimize the original purchase price, regardless of the actual value, by providing the customer with an appraisal that values the item at or above the purchase price.

If the insured obtain an appraisal from a jeweler other than the original retail jeweler, the appraisal becomes more credible but continues to display inherent bias. The insured will usually advise the appraising jeweler that the appraisal is for insurance purposes. The appraising jeweler may be motivated by business considerations and, as a gesture of good will toward a potential customer, incorrectly inflate the stone value.

Nevertheless, and regardless of the motivational context of the insured's original appraisal, once an item of jewelry is lost, the insurer is often faced with the problem of adjusting a claim of dubious value based upon an inherently biased appraisal, or an incomplete or unverifiable appraisal of fair market value.³ Occasionally, an adjuster will be asked to rely upon a written appraisal by a jeweler that has not adequately examined the stone. Less frequently, the insured will offer the adjuster an appraisal by a jeweler that has never seen the stone. Finally, it is not uncommon for the adjuster to be given an appraisal that states a value but does not describe the stone with enough specificity to allow a second jeweler to confirm or deny the appraised value. In each of these scenarios, the adjuster is asked to adjust a first party claim without sufficient evidence to reasonably dispute the insured's statement of value.⁴

Reconciling inconsistent appraisals when the item has been damaged but not lost is less problematic but continues to present appraisal valuation issues. Most notably, a damaged stone remains available to the adjuster for an independent appraisal by a Certified Gemologist Appraiser ("CGA"), a CGA equivalent appraiser, or the GIA (collectively "Certified Appraiser"). If the insurer retains an independent Certified Appraiser to examine the stone before settling the claim, the Certified Appraiser can issue a report that verifies damage and establishes a basis for

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claim valuation. The claims representative may then reasonably rely upon the Certified Appraiser's report in evaluating and adjusting the claim irrespective of the insured's appraised value. Nevertheless, few jewelry claims are subject to an independent appraisal during the claims process.

The usual scenario is for the adjuster to ask the insured for an appraisal of the damaged stone. In the most egregious example, the insured and the appraising jeweler will agree that the jeweler's appraisal will overstate either the value of the stone or the extent of damage affecting the value of the stone. More commonly, however, the parties will agree that the jeweler will be given the stone for salvage or will provide the insured with a replacement stone at the higher appraised value. If the insurer relies upon this biased appraisal in settling the claim and later obtains an inconsistent appraisal of the damage during a Certified Appraisal to establish salvage value, the insurer may have a first party fraud action against the insured.

However, in most damage claims involving inconsistent appraisals, the insured are acting in good faith and are, themselves, victim of jeweler negligence or deceit. In most cases, the jeweler will either (a) incorrectly appraise the base value of the stone before appraising the nature and extent of the damage; (b) incorrectly appraise the nature and extent of the damage; or, (c) incorrectly appraise both the base value of the stone and the nature and extent of the damage.

Occasionally, the claims representative will independently obtain a GIA report on the damaged stone to establish base qualities and the nature and extent of damage.⁵ More frequently, however, the insured will submit the damage appraisal that merely identifies damage to the stone. In this instance, the adjuster must first confirm damage and the qualities of the stone before proceeding to settle the claim.

However, when the damage appraisal mirrors the underwriting appraisal on base characteristics, the adjuster is faced with a damage appraisal that is facially valid. Nevertheless, these cases present the problem of credibility on the nature and extent of damage. It is not uncommon for an insured's appraisal to overstate the nature and extent of gemstone damage. On occasion, a damage appraisal will identify nonexistent damage, or incorrectly identify an inclusion as damage to the stone.⁶

In each of these instances, the insured are asking the adjuster to rely upon an appraisal by the insured's jeweler who may be biased, incompetent, or corrupt. Although the adjuster can obtain a GIA certificate to independently corroborate the insured's appraisal, the economics of volume adjusting and per claim loss discourage this additional step. Accordingly, only in the most extreme cases will the adjuster obtain a GIA report to dispute the underwriting appraisal, damage appraisal, or both.

Once the insurer settles the jewelry claim, the insurer's ability to mitigate its loss is usually limited to recovering salvage value on the stone. If the insured obtained the policy of insurance by knowingly submitting a false underwriting appraisal, or was paid policy proceeds by knowingly submitting a false damage appraisal, the insurer may rescind the insurance policy, deny the claim, or recover paid proceeds.⁷ However, if the insured have no personal knowledge of the actual gemstone value and believe the underwriting or damage appraisal to be true, then the insured may submit the appraisal to the insurer without liability for the truth of the representations. If the insurer later discovers false statements or misrepresentations in the appraisal, the insurer may not proceed against the insured in a first party suit unless the insurer can establish that the underlying information was provided by an agent of the insured bound by a legal duty to provide truthful information.⁸

Where the insurer relies upon the underwriting or damage appraisal of the insured's

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jeweler to adjust and pay proceeds on a claim, the insurer may have no recourse against the jeweler if it later discovers jeweler fraud or negligent misrepresentation. Under California law, a party damaged by fraud or negligent misrepresentation must prove that its reliance upon the falsity was reasonable.⁹ A property insurer is in the business of risk assessment and allocation, and possesses the financial resources necessary to independently establish the value of the insured risk.¹⁰ An insurer would be hard pressed to convince a jury that it reasonably relied upon the now disputed value appraisal prepared by an unknown third party jeweler with unknown education and experience, and with inherent bias. Accordingly, for purposes of affixing third party liability for jeweler fraud or negligent misrepresentation, the insurer's reliance upon the insured's underwriting and damage appraisal is facially unreasonable.

If the insurance industry is to control its losses in jewelry claims, it will be necessary to establish reliable standards for underwriting and loss appraisal. The insurance industry may also wish to certify jewelers to conduct appraisals. Underwriting can require customers to obtain an appraisal from a jeweler in the insured's geographical area that is GIA trained and complies with reasonable industry requirements for appraising and certifying gemstone jewelry. At time of loss or damage, the claims adjuster can then reasonably rely upon the underwriting appraisal for a basis of characteristics for valuation, and in the case of a damaged stone, can require the insured to obtain a damage appraisal from a similarly qualified independent jeweler. The claims representative may then reasonably rely upon the insurer certified appraisal, in conjunction with the report of other independent claim consultants such as jewelry claim specialists, to adjust the claim.

The problems of jewelry claim underwriting and adjusting are many and diverse. This article has only attempted to illustrate the most pervasive problems facing the claims representative in valuing gemstone claims for settlement. The only viable long term solution to eliminating waste and mitigating claim losses is for the insurance industry to integrate the underwriting and claims departments under a program of credible valuation standards and procedures that can be reasonably relied upon when adjusting and paying jewelry claims.

Notes:

1. John J. Camozzi received a B.A. degree from the University of California, Berkeley in 1982, a J.D. degree from Golden Gate University, San Francisco in 1987, and an M.B.A. with emphasis in International Banking from Golden Gate University, San Francisco in 1990. He served for four years as house counsel for Farmers Insurance Group, and is now in private practice in Walnut Creek, California, specializing in business law.
2. Hendry, Jewelry Insurance - The Underwriting and Claims Reference Manual (1992) p.CLAIM 3. See also: Dauer, Jewelry Co. Can Cut Claims Costs (June 10, 1991) National Underwriter.
3. California law establishes the value of lost or destroyed personal property as "the fair market value of such property at the time of its loss or destruction." (BAJI No. 14.21 (1986 Revision).) (**Please note:** The legal analysis in this paper is based upon California law. The law of the jurisdiction in which you conduct business may be different. You are encouraged to consult with a local attorney experienced in the law of your business forum.

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4. California Insurance Code Section 790.03 and the cases interpreting it require an insurer to pay benefits under a first party claim unless the insurer can reasonably deny the claim. Opsal v. United Services Auto. Ass'n (App. 4 Dist. 1991) 10 Cal. Rptr.2d 352, publication ordered 10 Cal.Rptr.2d 351, 833 P.2d 1, review dismissed, cause remanded 6 Cal.Rptr.2d 276, 826 P.2d 274, review granted and opinion superseded 231 Cal.App.3d 1530, 286 Cal.Rptr. 282, 816 P.2d 1308, reprinted without change to permit tracking pending review by the Supreme Court 2 Cal.App.4th 1197; 283 Cal.Rptr. 212.
5. California jury instructions provide alternate measures of personal property damage where the property has been damaged but not lost or destroyed. The damage calculation's most applicable to gemstones establish value as a function of fair market value on the date of loss. (BAJI No. 14.20 (1992 Revision).)
6. An inclusion is an imperfection enclosed in the stone, or appearing as a surface chip to the untrained eye. Normally, the cutter will polish a surface inclusion (commonly referred to as a "natural") out of the finished stone. However, depending upon the size of both the stone and the inclusion, the cutter will often leave some part of the natural in the final cut to preserve overall gemstone size. An inclusion is an inherent vice to the stone that preexisted the policy of insurance and is not a recoverable loss.
7. California Insurance Code Section 359; Maggini v. West Coast Life Ins. Co. (1934) 136 Cal.App. 472, 29 P.2d 263.
8. California Insurance Code Section 357 provides in its entirety: When an insured has no personal knowledge of a fact, he may nevertheless repeat information which he has upon the subject, and which he believes to be true, with the explanation that he does so on the information of others; or he may submit the information, in its whole extent, to the insurer. In neither case is he responsible for its truth, unless it proceeds from an agent of the insured, whose duty it is to give the information.
9. McGonigle v. Combs (1991) 968 F.2d 810; Chicago Title Ins. Co. v. Superior Court (California Canadian Bank), (1985) 220 Cal. Rptr. 507, 174 Cal.App.3d 1142, review denied; 5 Witkin, Summary of California Law (9th ed. 1988) Sections 711-717, pp. 810-817.
10. As of this writing, a full independent report by a Certified Appraiser be obtained by overnight courier within five business days and at a cost of approximately \$80.