

SHIFT

AI-Powered Subrogation Detection and its Impact on the Combined Ratio

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The third in a [series of commentaries](#) addressing the [combined ratio problem](#) facing the global insurance industry.

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Executive Summary

- Approximately 15% of P&C claims are closed with missed opportunities for recovery from other liable parties, costing the insurance industry between £12-16 billion annually
- It takes an average of 6 months for insurers to complete the liability determination and recovery process
- Best in class liability and recovery efforts can positively impact the combined ratio by up to 4%
- Insurers stand to recoup up to an additional 7% of a claim's total value when AI is applied to the liability and recovery problem

The insurance industry faced an average combined ratio of nearly 102% exiting 2023. And according to widely accepted industry estimates, approximately 15% of P&C claims are closed with missed recovery opportunities. That represents a cost of between £12-16 billion annually, with some calculations putting the cost at closer to £24 billion. Since those missed opportunities directly impact the bottom line, and ultimately the combined ratio, it stands to reason that more effective liability determination and recovery can have a profound impact on an insurer's bottom line.

As an industry we have also seen that a strategy that relies only on raising premiums is not enough to have the desired effect on the combined ratio. Furthermore, focusing solely on increasing premiums also creates the real risk of driving customer dissatisfaction if policyholders believe they are being treated unfairly. This can create churn and the new problem of replacing top-line revenue and consumer duty complications. As such, applying best practices to the liability determination and recovery process represents an excellent opportunity to shave points off of the combined ratio.

Using artificial intelligence (AI) generally, and generative AI (Gen AI) more specifically, to help insurers detect hidden recovery opportunities, assess liability and likelihood of recovery, as well as surface and apply relevant negligence/fault legislation is one of the most effective ways to modernise this important process. The result is fast, accurate, and fair recovery that benefits both insurers and their customers and helps to address the continuing combined ratio problem.

Solving the Time Gap

One of the most interesting aspects of the relationship between premiums and recovery is the impact time has on claims. If we look simply at the divide between premiums and claims costs, it is important to remember that even if an insurer does raise rates, the majority of claims on the books will have been made on premiums that were already paid. And since premium increases cannot be applied retroactively, the only way to bridge the divide is through effective recovery. The ability to maximise not only the number of opportunities, but also the likelihood of recovery is just one powerful way AI can benefit efforts, and in turn positively impact the combined ratio.

Time can also affect the ultimate value of recovered claims. Insurers typically have between 2-5 years (and in some jurisdictions up to 10) to pursue recovery opportunities. On the surface, this seems to benefit insurers in that it provides a long runway to recover costs from a third-party. However, the same inflationary pressures that are driving the industry's combined ratio challenge are driving down the real value of the amount recovered. Considering that it takes an average of 6 months for insurers to complete the process, insurers who are able to more efficiently and effectively execute recovery are more likely to retain as close to full claim value as possible.

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Bridging the Skills Gap

It can take years of experience for a claims professional to build the expertise required for true effectiveness associated with improving viability and timely pursuit of recovery opportunities. At the same time, the expertise of individual experts is incredibly difficult to scale. And due to factors such as “The Great Resignation” and other related talent issues, insurers find themselves facing a lack of skilled employees able to execute liability determination and recovery to an extent where it meaningfully impacts the combined ratio.

Fortunately, AI has proven itself valuable in this area. Insurers augmenting recovery efforts with AI inject significant efficiency into the process, effectively applying the expertise and experience of their best specialists at scale. And since advanced AI can not only detect, but also explain the reasons and rationale for alerting on a specific claim, less experienced team members can make a larger impact. This is critically important when you consider that insurers stand to recoup up to an additional 7% of a claim’s total value when AI is applied to the problem.

Subrogation and Recovery in Different Jurisdictions

Insurance is a highly regulated industry and the regulations that govern it often differ greatly depending on which countries you are doing business in. How fault is assigned, especially in the case of motor accidents, can also vary according to local laws. These factors can complicate how recovery opportunities are pursued across international divisions and countries, or even if they are.

AI can be used to mitigate these factors by applying the correct analysis to the claim based on the laws and regulations of the jurisdiction in which the incident occurred. For insurers doing business in multiple jurisdictions, but who may employ a centralised approach to claims handling, having AI know which scenarios to apply to which claims ensures recovery opportunities are surfaced correctly regardless of which handler is working them and where.

This kind of situation can also result when an insurer established in one jurisdiction decides to begin doing business in another, and may be unfamiliar with the nuances of local regulations with which they are not familiar. Due to a fundamental lack of understanding, claims handlers may believe a recovery opportunity does not exist, and thus identifies the claims as such. Each missed opportunity results in hard pounds that could be recovered which instead increases the combined ratio. AI-powered liability and recovery makes it easier to retroactively identify claims that may have been mislabeled and pursue recovery. As important, analysis using AI models tuned to the nuances of all the jurisdictions in which an insurer does business can help avoid this situation in the first place by automatically, and accurately, identifying claims with a high probability of recovery.

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Conclusion

Difficult liability determination and missed recovery opportunities have long been viewed by the insurance industry as a whole as simply the cost of doing business. Whatever pounds they could recoup were seen as a bonus as opposed to having a meaningful impact on the bottom line. However, as insurers faced burgeoning combined ratios, it became clear that driving best-in-class recovery efforts could truly benefit the business. Our own research has shown that doing so can positively impact the combined ratio by up to 4%, which for many insurers could be the difference between operating in the red versus the black. Liability determination and recovery is not easy. It is a complicated and nuanced process shaped by local laws and regulations. Applying AI to the problem allows insurers to augment the skills and expertise of their employees, accurately and efficiently uncover hidden opportunities, understand liability sooner in the process, and even improve the policyholder experience.



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