

# YOUR INSURANCE AUDIT - HOW TO SAVE TIME AND MONEY

## WHAT IS AN INSURANCE AUDIT?

Insurance audits are typically performed on commercial insurance policies providing automobile, general liability, garage liability, umbrella and workers compensation coverages. When these policies are issued, you are asked to pay an *estimated*, or deposit premium. Estimated premiums are based on the nature of your business and your estimated annual exposures (i.e. payroll, gross sales or receipts, cost of sub-contractors, etc.) for the policy term.

Once your policy expires, the insurance company will conduct an audit to collect information on the *actual* exposures and operations for the policy term. They then determine the actual earned premium. Premium adjustments are then determined by comparing the audited exposures and operations with the original policy estimates.

## WHAT RECORDS ARE NEEDED FOR THE AUDIT?

It's important for you to maintain payroll, overtime, sales and cost summaries – preferably on a monthly, quarterly and annual basis. Your records are very important to the audit process. They provide and verify information, save time and minimize your insurance costs. The auditor will let you know which of the following records will be needed for your audit when the audit appointment is made.

- **PAYROLL RECORDS** include payroll journals and summary, federal tax reports (941's), state unemployment reports and individual earnings records. Totals should be kept for overtime when applicable.
- **EMPLOYEE RECORDS** include the number of employees and hours, days or weeks worked annually.
- **SALES JOURNAL** includes all goods or products sold, rented and/or distributed as well as service, repair and installation. Sales or excise taxes collected separately and submitted to the government need to be identified in order to be excluded.
- **CASH DISBURSEMENTS** show subcontractors, materials and casual labor.
- **CERTIFICATES OF INSURANCE** show the subcontractors used during the policy period for construction, erection and/or structural alteration for general liability and workers compensation insurance coverages. They are also used for commercial automobile hired auto coverage.
- **INCOME STATEMENTS** include subcontracted costs used to determine the cost of hired autos for commercial automobile audits.

## WHEN AND HOW WILL THE AUDIT BE DONE?

The insurance company will collect audit information from you shortly after your policy expires.

Smaller, less complex policies may only require that you assemble and send the necessary information to the insurance company, or have the information available when a telephone auditor calls.

Larger and more complicated policies are generally assigned to a field auditor, or independent auditing firm, who will schedule an appointment with you shortly after the policy expires.

If you must change or cancel a scheduled appointment, please let the auditor know as far in advance as you can. It's best to schedule and complete the audit within 30 days from the date you are contacted by the auditor.

It is important for the auditor to ask questions about your operations. If you cannot be present to answer questions, someone who is familiar with the specifics of your entire business should be available.

If you direct the auditor to your accountant, they will obtain as much information as possible from him/her and contact you for any additional questions.

Most audits take an average of a half hour or less, but audits of larger policies may take longer. Though the auditor will have a number of questions, you will not have to be directly involved during the entire audit if adequate records are kept and made available.

## HOW CAN YOU SAVE MONEY?

There are several ways you can save on premium dollars depending on the type of business and coverages that you have. Not all of the following may apply to your particular business.

- **PAYROLL DIVISION** – A single employee’s payroll can be divided, except when the employee works in a clerical or sales position. Proper records must be kept, in dollar amounts, that reflect work actually performed before a breakdown can be applied. Without adequate records, the entire payroll for the employee must be placed in the highest rated classification.
- **EMPLOYEE TIPS** – Tips declared by employees may be excluded from their gross payroll only if separately identified.
- **CERTIFICATES OF INSURANCE** – Have certificates available for the audit at your premises (or your accountant’s) to ensure that charges are not made unnecessarily. Certificates must cover the period when the subcontractor worked for you. This may require certificates covering two different policy terms for the subcontractor in some cases. For commercial automobile hired auto coverage, certificates of insurance covering the insured on a direct-primary basis will reduce rates by 95%.
- **DRIVERS** – (For general liability coverage) employees with the sole responsibility of driving may often be excluded from chargeable payroll if their wages are shown separately. However, employees who perform other duties besides driving must be placed in the highest rated class describing their duties.
- **COST OF HIRE** is commonly used on commercial automobile policies as a premium basis for hired auto coverage. This includes automobiles and trailers used under contract on behalf of or loaned to you, which may include rental units as well as subcontracted hauling done for you.

Your business is unique. You can request a preliminary audit, at any time, to pinpoint factors that could help you find ways to control your insurance cost. If you have questions about how your specific circumstances will affect savings, please contact us at your convenience.

## BASIC DEFINITIONS

**REMUNERATION** is commonly called payroll. It includes wages, commissions, bonuses, overtime pay, pay for holidays, vacations and sickness, payment for piece work, tool allowances, incentive plans, profit sharing, contributions to individual retirement accounts, employee contributions to employee benefit plans, value of meals and lodging, store certificates, merchandise and other substitutes for money.

It does not include employer contributions to a group insurance or pension plan, special awards for individual inventions or discoveries, or overtime.

**OVERTIME** is defined as the hours worked for which there is an increase in the rate of pay. In most states, the amount paid in excess of straight time pay can be deducted if it can be verified in your records. It includes:

- Work in excess of 8 hours per day, or 40 hours per week.
- Work on Saturdays, Sundays or holidays.
- Work in any day, or week, in excess of a guaranteed wage agreement.

Extra pay for shift differential is not considered overtime.

Ordinarily, overtime pay is equal to 1-1/2 times the regular hourly rate. For example, a regular pay rate of \$10 per hour at time and a half generates a \$15 per hour overtime rate.

If the extra \$5 of pay is shown separately, it is excluded in the total. If the total overtime wage is shown in a combined amount of \$15 (regular pay plus increase) and included in the gross payroll, one third (\$5) will be deducted from the gross pay amount.

If the overtime wage is calculated at double time, one half will be deducted from the gross pay amount.

**GROSS SALES** is the gross amount charged by you or others trading under your name for all goods or products sold or distributed, operations performed and rentals. Some deductions from gross sales include sales or excise tax, returns and allowances and finance charges for items sold on installments.

**SUBCONTRACTOR** is often used interchangeably with “independent contractor”. We ordinarily apply the definition to subcontractors performing construction, erection or structural alteration for a general contractor. Most workers compensation laws hold you responsible for employees of an uninsured subcontractor. In some states, they may extend to an uninsured subcontractor without employees if an employee-employer relationship can be established. A liability policy will also include a charge for subcontractors as though they were your employees if there is no certificate of insurance showing evidence of insurance. Subcontractors can easily obtain a certificate of insurance through their insurance agent.

The actual working relationship between you and the subcontractor will be examined. Items such as, but not limited to: whether the work performed is an integral part of your operations, whether you have the right to control the details of the work, the method of payment, who supplied the materials used, does the person regularly work for others, whose regulatory authority did the person operate under, whether the person is involved in a separate and distinct business offering the same services to the public.

**TOTAL COST** is the cost of all work let or sublet in connection with each specific project including:

- The cost of all labor, materials and equipment furnished, used or delivered for use in the execution of the work.
- All fees, bonuses or commissions made, paid or due.
- The rates apply per \$1,000 of total cost.

## COMMONLY ASKED QUESTIONS

**Q:** Why is an audit necessary?

**A:** Unlike coverage for tangible assets, the premiums for the policy is based on estimated variables such as payroll, sales revenues or subcontracted costs – often called premium exposures. Since these variables can be difficult to predict, you are asked to estimate your exposures on the application, and the premiums are set according to those estimates. It isn't until the policy term has expired that the actual data becomes available and the insurer's exposure can be accurately calculated. For this reason, audits are performed after the policy term has expired. The estimated premiums are compared with the actually premiums and adjusted accordingly.

**Q:** If overtime is not summarized, will I still get credit?

**A:** Overtime records must show overtime pay separately by employee or classification or it will not be deducted.

**Q:** If I do not have certificates of insurance from subcontractors for the audit, will I be able to get them?

**A:** It is in your best interest to request certificates from subs at the time the work is performed rather than at the time of the audit. You will be charged for employees of those subcontractors not providing certificates as though they were your own employees.

**Q:** Several of my employees do more than one type of work. How should I assign their payrolls?

**A:** Payrolls may be divided in appropriate classifications, provided the division is reflected on the original records in dollar amounts.

**Q:** Some of my work could be considered clerical and sales. Should I separate it?

**A:** The clerical and sales classifications cannot be used with any other class for division of a single employee's payroll.

**Q:** Is it necessary to provide audit information if my renewal policy has been cancelled?

**A:** Yes, policies are issued using estimated payroll or sales. Actual payroll or sales needs to be known to determine if any additional premium is due to the insurance company, or a return premium is due to you, the policyholder.

**Q:** When will I receive a final audit statement?

**A:** In most cases, the insurance company will send a billing statement shortly after the audit is completed. The statement will summarize your audited (actual) classification and premium exposure. It will also include your actual premium, and the net difference between that figure and your estimated premium.

**NOTE:** The contents of this publication are not intended to supersede any definitions or conditions of your policy, state statutes or legal rulings in your state.