

INSURANCE BULLETIN

BULLETIN #5

Save Time and Money by Being Prepared for Premium Audit

CNA and NESPA are proud to provide you with this information. We trust that you will find it useful in understanding the insurance and risk management issues associated with your business.

When business owners hear the word *audit*, they usually have an unfavorable reaction. They often equate this term with an Internal Revenue Service (IRS) tax audit. However, in the world of insurance, there is something called a premium audit, and it's not nearly as painful as an IRS tax audit.

When your insurance policies are issued, the premiums are *estimated* based on assessments of your business exposures (payroll, sales or subcontract costs) for the upcoming policy term. A premium audit is necessary at the end of the policy term to determine the *actual* payroll, sales or subcontract costs for your business. If appropriate, an adjustment will be made either upwards or downwards to the premium that was estimated when the policy was originally issued.

In this way, business insurance premiums are adjusted in relation to the size of business and its operations. The larger the business the more work they do or the more products they sell, the larger the final premiums at audit. The smaller the business, the smaller the final premiums will be. This is a fair approach because a business that sells more products or services, or performs more spa and swimming pool work is likely to incur more insurance claims than a smaller business doing less work or selling fewer products or services.

Some coverages that are subject to audit are:

- Workers' Compensation
- General Liability (premises operation liability/products and completed operations liability)
- Automobile Liability (large, composite-rated vehicle schedules)

At the end of the policy term, a premium auditor will examine and audit all of a business' records that relate to its insurance policy. The records needed will vary depending on the type of insurance coverage being audited. In most cases, the premium auditor is able to obtain the necessary audit data from two or more of the following records:

- Payroll Journals
- Sales Ledgers
- Tax Reports
- Individual Earning Cards
- Vehicle Titles
- Registrations
- Ownership Tax Receipts

Most commonly, premiums for contractor's insurance are calculated based on payroll and subcontract costs. Payroll is defined as *total remuneration for services performed by employees*. In most states *remuneration* means money or substitutes for money and includes items such as wages, bonuses, commissions, vacation, holiday and sick pay, overtime, profit sharing plans, tool allowances and other dollar-value substitutes.

By maintaining accurate, detailed payroll records in accordance with the following guidelines, spa and swimming pool companies may reduce the time and expense associated with performing the final premium audit.

Overtime

In most states, the amount paid in excess of straight time can be deducted if the excess or overtime can be verified in records. A business must maintain records to show overtime pay separately by employee and in summary by classification of work by state.

Division of Payroll

In construction, division of an individual employee's payroll into different rating classifications is allowed. However, records must show the number of hours and amount of payroll for each type or class of work the employee performed. If such a breakdown is not kept, the full salary for the employee must be charged to the *highest rated* classifications to which the employee is exposed.

Subcontractors

Under the laws in some jurisdictions, a contractor may be obligated to provide workers' compensation benefits to the injured employee of an *uninsured* subcontractor. However, contractors can take steps to help protect themselves. One way is to regularly secure and examine *Certificates of Insurance* evidencing appropriate and adequate workers' compensation coverage for each and every subcontractor hired. If such evidence of insurance is not available at the time of the premium audit, the subcontractor's payroll may be added to the hiring contractor's payroll under its policy, increasing your business insurance premiums.

Similar rules may also apply to general liability coverage. Your insurance carrier may require you to ensure that all of your subcontractors carry general liability limits in a certain amount, such as \$1,000,000 per occurrence. Again, you should regularly obtain and examine *Certificates of Insurance* evidencing appropriate and adequate general liability coverage from each and every subcontractor you hire. If such evidence of insurance is not available at the time of the premium audit, the subcontract costs related to that subcontractor may be converted to payroll and added to your policy, increasing your general liability premiums.

Through the SPLASH program, CNA can provide a business insurance program that offers comprehensive risk control (safety) services, expert claim handling and property/liability insurance coverages designed specifically for spa and swimming pool professionals. So when your business is insured with the CNA/SPLASH program, you'll have peace of mind knowing it's a program backed by a carrier with more than 60 years experience in the construction industry. Give us an opportunity to earn your business – ask your insurance agent to obtain a quote from CNA and discover how you can benefit from this partnership.

For more information, contact your local independent agent or visit www.cna.com.

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