

Forensic Accounting in Business Insurance Claims

When businesses are required to file insurance claims of various sorts, forensic accountants may be helpful in making certain that the company is able to claim the full and maximum amount under its coverage. It is important for the insured to begin the thought process with regard to insurance coverage almost as soon as a theft or disaster occurs. There are several issues that need to be understood in order to optimize the appropriate recompense under the existing insurance policies.

In the case of a fidelity bond loss (an employee theft), the issue generally relates to the timing of discovery, making certain that it is clear where the funds went, (not for the benefit of the insured/the company) in establishing a forensic trail of all funds as they left the company, and ascertaining the benefit that was derived by the employee.

Sometimes more complicated are the claims that occur with regard to business interruption and/or significant losses to a facility. Business interruption insurance is often based on either lost revenue and/or increased operating expenses. There are several issues that need to be taken into account and that need to be documented early on:

- The company needs to properly mitigate any of its losses – this is normally defined as making certain that those expenses that can be reduced or eliminated are controlled at an early date.
- The need for segregating those expenses that would have been on-going in any event, separate and apart from those which will be increased expenses because of the loss must be maintained in as strict a fashion as is possible. Often, it is necessary to modify the general ledger/accounting system for the company in order to properly classify the expenditures that relate to “new” issues and segregate those from on-going issues.

The ability to understand and document for the insurance company lost revenue/gross profit will be determined by the accounting system and by the comparison of historical information with the information after the occurrence of the disaster/event.

Forensic accountants will routinely be able to use the historical information from the company, sometimes by using the existing accounting system and existing reports from the general ledger, as well as by using data mining tools and other statistical analysis to properly show historical trends, including seasonal variations and the impact that the disaster has had. It is important for the company to understand and keep track of the difference, not just in lost revenue (which is one form of measurement) but rather lost gross profit. For many businesses, the cost of goods sold is a significant issue, and a lost sale of \$1,000 does not routinely generate a \$1,000 insurance claim, but rather a claim for the gross profit on that \$1,000 sale.

Getting the records in order, and fully understanding the insurance procedure early on, will normally result in a greater recovery in insurance proceeds, as well as a more rapid recovery. Routinely, the forensic accountant will work with legal counsel, sometimes with the insurance broker, and in some cases, with other professionals in putting the claim together. The claim itself will routinely be filed within 90 to 120 days of the event (the insurance policy and state law may control the timing phase of the submission). The detail that is required will vary from insurance company to insurance company.

Insurance companies generally have a requirement under contractual law as well as state insurance regulations to handle claims in a timely and efficient manner. Most insurance will respond within 30 to 60 days of the submission of a claim, either with a payment, with a request for additional information, with a partial payment and a partial rejection, or in some other fashion. Only in rare circumstances will insurance companies effectively ignore a claim and risk a “bad faith” action against them by the insured.

In the case of significant disasters, including those such as tornados, earthquakes, floods and fires, the company may have a lack of sufficient and significant data available. This is one of the many reasons why professionals recommend extensive disaster recovery plans be put in place, as well as business continuity plans. These two plans work hand-in-hand with the disaster recovery plan providing the ability to recover substantially all data from some back-up mechanism off-site, and the business continuity plan focused on returning the company to normal operations as quickly as possible.

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For companies that lack a disaster recovery plan, the forensic accountant may be able to resurrect lost data from a variety of sources. In addition, through the use of analytic software, the forensic accountant may be able to project revenue, expense and profit trends in the absence of concrete data.

Disasters, thefts and other circumstances may require businesses to pursue recovery of losses by filing business insurance claims. The services of a forensic accountant can prove useful in enabling such businesses to recover the full and maximum amount available under its insurance policies.