



## **Are You Ready for an Audit?**

### **What is an Audit?**

The money you pay at the beginning of your insurance policy year is an estimate of the cost of your coverage for the next 12 months. The estimate is based on payroll, cost of subcontractors and/or gross receipts.

Your insurance company is allowed under the terms of your policies to examine your books and records for the purpose of determining the proper charge for your insurance. These examinations, known as audits, are performed after the close of the policy year. They look back to see what actually happened and adjust the estimated cost that was charged in the beginning of the policy year. Some companies do not return premium, using the audit only to determine if any amounts in excess of the estimate are due. Other companies adjust the premium either up or down based on audit results, returning premium or charging additional amounts as determined by the audit. Your company's approach is determined when coverage is written. An adjustment in billing consistent with their approach will be made following the audit.

### **Why you need to be ready**

Liability and Worker's Compensation rules allow payroll to be allocated to the types of work being performed. Some types of work cost more to insure than others. If your records are not properly arranged all payroll will be assigned to the most expensive work you do.

If your employees perform several types of work within the scope of their jobs, please discuss this with us. We can explain in detail the records you must keep to ensure your assessment is fair.

## What the rules say

### Original Payroll Records

An insurance auditor must be able to determine how much payroll is assigned to a type of work from the original payroll records. This means your daily job sheets (whatever you use to track jobs and the hours worked by people assigned to them) must show the hours worked by each individual, the type of work they were assigned to, and their rate of straight time pay.

An individual's time and payroll may not be derived by estimating the percentage of time spent on various categories of work.

### What is included in Payroll?

- A. Regular wages.
- B. Commissions.
- C. Bonuses.
- D. Straight time rate for overtime hours. (see Overtime below)
- E. Pay for holidays, vacations or period of sickness.
- F. Payment by an employer of amounts otherwise required by law to be paid by employees to statutory insurance or Pension Plans, such as Federal Security Act.
- G. Payment to employees on any basis other than time worked, such as piecework, profit sharing or incentive plans.
- H. Payment or allowance for hand tools or power tools provided by employees and used in their work or operations for the insured.
- I. The rental value of an apartment or a house provided for an employee based on comparable accommodations.
- J. The value of lodging, other than an apartment or house, received by employees as part of their pay, to the extent shown in the insured's records.
- K. The value of meals received by employees as part of their pay to the extent shown in their insured's records.
- L. The value of store certificates, merchandise, credits or any other substitute for money received by employees as part of their pay.

### What is not included in Payroll?

- A. Tips and other gratuities received by employees.
- B. Payments by an employer to group insurance or group pension plans for employees, other than those required by law such as Social Security.
- C. The value of special rewards for individual invention or discovery.
- D. Dismissal or severance payments except for time worked or accrued vacation.

### Overtime

The extra paid for overtime will be excluded and may be handled in either of the following ways:

- A. If the records show separately the extra earned for overtime, the entire extra amount will be excluded.
- B. If the records show the total pay earned for overtime (regular pay plus overtime pay) and time and one half is paid for overtime, 1/3 of the total will be excluded. If double time is paid for overtime, 1/2 of the total will be excluded.

### Special considerations for Liability Audits

In addition to the foregoing exclusions, the following are not included in payroll used to calculate liability insurance costs:

- A. Wages of drivers (some classes specifically include drivers)
- B. Wages of clerical office workers
- C. Wages of people involved primarily in outside sales

### **Certificates of Insurance & Subcontractors**

Be prepared to present certificates for all subcontractors. The certificate should show insurance in force for General Liability, Worker's Compensation and Automobile, both owned and non-owned. The effective dates of coverage must encompass the period when the sub was working for you. The limits for general liability coverage should be at least equal to your limits. If you have additional questions about what your insurance company(s) require from subcontractors, please do not hesitate to ask us.

You must also be prepared to present the total cost of all insured subcontractors that have worked during your policy period. Included in the total cost is the amount paid to the subs plus any money spent by you on materials to be used by the subs.

**If the insured is a sole proprietor or partnership, the certificate must indicate whether the owner or owners are included or excluded from coverage. If the owner or owners are excluded from coverage, expect that your workers compensation carrier will be adding this payroll to your audit.**