

Controlling Premium Audits to Eliminate Overcharges

By controlling the information used in the audit process, you can eliminate the possibility that overcharges and misclassification will lead to higher premium for your business.

Due to the volume of requests received, insurance companies have developed an efficient premium audit process. While insurance companies strive to be as accurate as possible, they don't have the time or resources to investigate and resolve every possible error or ambiguity. As a result, your company may experience multiple, unintentional overcharges. If you know the rules, you can take control of the process by anticipating and preparing the exact information your insurance company needs to prevent inadvertent overcharges, saving your company money in the process.

Properly Classify Employees

Your business should have one primary classification that is governed by the State. Outside sales, clerical employees and, in some states, drivers may be classified with a separate code. Any items the auditor cannot classify quickly with a lower-rated code remain in the governing code. This may result in overcharges due to the improper classification of employees who should be in standard class exemption groups (clerical, outside sales) common to all industries. For example, in a nursing home, the governing class is 8829, however, some of the employees could be classified as 8810 (clerical). The 8810 classification is a much lower rate, saving over \$3 per \$100 of payroll. Jobs that could be included in 8810 are: Dietician, Director of Nursing, Social Worker, etc. Please review classification descriptions for specifics.

Each company (with its own FEIN) that issues payroll could have its own governing classification. If the entity had its own FEIN, but otherwise was reported under the same payroll and tax filings as other entities, they would not have their own governing class. For example, in a nursing home the governing class code is 8829 and includes payrolls except clerical, including employees working in the pharmacy. However, if the pharmacy has a separate FEIN, then the pharmacy class code 8045 can be added, saving over \$2.00 per \$100 of payroll.

Review the classification assigned to each employee. If you have questions, please see your agent and/or refer to the classification description assigned to your policy. If an employee performs services in more than one classification, all payroll will be applied to the higher classification unless your payroll records separate hours by actual classification (not a percentage). If records note hours, then the employee's payroll can be split between the two classifications.

Please contact your M3 representative if the auditor wants to add any classifications.

Create an Accurate Premium Audit Package

To prevent overcharges, you need to take control of the process and create an "overcharge-proof" premium audit package that will give the auditor complete and accurate information to work with.

To begin, you will need to collect the following source material:

- Payroll records (employee-specific)
- Unemployment tax return
- 1040 Schedule C (if you are a sole proprietor)
- Federal and state payroll tax reports (940s and 941s)
- General ledger, subcontractor ledgers and journals (or 1099s)
- Certificates of insurance from subcontractor
- Your workers' compensation insurance

You may want to highlight overtime pay for the auditors so it can easily be discounted back to normal pay.



Executive Officers

In Wisconsin, executive officers of a corporation are automatically included unless they have been excluded by endorsement. When included there is a minimum and maximum remuneration for each officer (can only include those filed with company's articles of incorporation or organization filed with the Department of Financial Institutions). This minimum/maximum, set by the State, changes each year. In 2015, the minimum was \$14,196, and the maximum was \$71,084 annually.

Sole proprietors, partners and members of an LLC are automatically excluded from coverage unless they have been endorsed on the policy. The amount used for remuneration is set each year by the state. In 2015, the annual remuneration is \$47,372.

Executive officers of a corporation or an association are the president, vice president, secretary, treasurer, clerk or any other officer appointed in accordance with the charter or bylaws of such entity.

Remuneration means money or substitutes for money. Payroll means remuneration.

Excluded Remuneration

Certain forms of compensation are not used to determine workers' compensation premium. Tips are an example of this. Allowable exclusions differ from state to state, but typically fall within 18-20 categories. Once you've added up all the excluded remunerations (by employee code), make sure to deduct them from your reported payroll. See next page for items excluded from remuneration.

Subcontractors

It is recommended that you only use employee-insured subcontractors, requiring them to present relevant certificates of insurance before commencing work. In Wisconsin, if your subcontractors do not meet the 9 point independent contractor test, then you will be assessed their payroll.

Volunteers

In Wisconsin, workers' compensation does not provide coverage for volunteers, including volunteers of nonprofit organizations that receive money or other things of value totaling not more than \$10 per week.

If a volunteer receives or expects to receive almost anything of value including discounts, certificates, credits, etc. in exchange for services, then they are most likely considered an employee for workers' compensation purposes.

If you have a program allowing employees to volunteer time at a nonprofit, on company time, their pay for the volunteered time would be included on your payroll. Instead, you may want to consider giving them a vacation day, thereby minimizing your workers' compensation and liability exposure.

Students

Students are considered employees of the organization for which they are performing service. There are two minor exceptions:

- A high school student (described in Wisconsin State Statute 115.01 (1) or 115.001 (3r)) is an employee of the school district unless they are on the payroll of an employer for whom they are providing services.
- A student in a technical college district who is producing a product for the school or is performing services for which the school collects a fee is an employee of that school.

Contracts

In attempt to transfer the workers' compensation risk, some contracts have attempted to assign liability to another party. Keep in mind that the Workers' Compensation Statute will supersede any contract. For example, a training program may accept workers' compensation responsibility in a contract. However, the party that receives the services is actually responsible for the workers' compensation and therefore should include the remuneration on their Workers' Compensation policy.



Inclusions

- Wages or salaries including retroactive wages or salaries
- Total cash received by employees for commissions and draws against commissions
- Bonuses including stock bonus plans
- Extra pay for overtime work except as provided in Rule V-E
- Pay for holidays, vacations, periods of sickness or unused accrued sick and vacation time
- Payment by an employer of amounts otherwise required by law to be paid by employees to statutory insurance or pension plans, such as the Federal Social Security Act
- Payment to employees on any basis other than time worked such as piecework, profit sharing or incentive plans
- Payment or allowance for hand tools or power tools used by hand provided by employees either directly or through a third party and used in their work or operations for the insured
- The rental value of an apartment or a house provided for an employee based on comparable accommodations
- The value of lodging, other than an apartment or house, received by employees as part of their pay will be the amount shown in the Miscellaneous Values page
- The value of meals received by employees as part of their pay will be the amount shown in the Miscellaneous Values page
- The value of school tuition, store certificates, merchandise, credits or any other substitute for money received by employees as part of their pay (refer to exclusions below for certain fringe benefits [substitutes for money] not considered to be remuneration)
- Payments for salary reduction, retirement, Wisconsin Retirement Plan, or cafeteria plans (IRC 125) that are made through deductions from the employee's gross pay
- Wages paid to employees as salary in conjunction with the Davis-Bacon Act or other prevailing wage laws
- Annuity plans
- Expense reimbursements to employees to the extent that an employer's records do not substantiate that the expense was incurred as a valid business expense

Exception: *When it can be verified that the employee was away from home overnight on the business of the employer, but the employer did not maintain verifiable receipts for incurred expenses, a reasonable expense allowance, limited to IRS per diem guidelines, will be permitted.*

- Payment for filming of commercials excluding subsequent residuals which are earned by the commercial's participant(s) each time the commercial appears in print or is broadcast

Exclusions

- Tips and other gratuities received by employees
- Payments by an employer to group insurance or group pension plans for employees, other than payments covered by Rule V-E in the Work Comp; "Overtime means hours worked for which there is an increase in the rate of pay: a. For work in any day or in any week in excess of the hours normally worked; or b. For hours worked in excess of 8 hours in any day or 40 hours in any week, or; c. For work on Saturdays, Sundays or Holidays."
- Payments by an employer into third-party trusts for the Davis-Bacon Act or a similar prevailing wage law provided the pension trust is qualified under IRC Section 401(a) and 501(a)
- The value of special rewards for individual invention or discovery
- Dismissal or severance pay except for time worked or accrued vacation
- Payments for active military duty
- Employee discounts on goods purchased from the employee's employer
- Expense reimbursements to employees to the extent that an employer's records substantiate the expense was incurred as a valid business expense; reimbursed expense and flat expense allowances, except for hand or power tools, paid to employees may be excluded from the audit, provided that all three of the following conditions are met:
 - The reimbursed expenses or expenses for which allowances were paid were incurred upon the business of the employer, and
 - The amount of each employee's expense payments or allowances is shown separately in the records of the employer, and
 - The amount of each expense reimbursement or allowance payment approximates the actual expenses incurred by the employee in the conduct of the employee's work.
- Supper money for late work
- Work uniform allowances
- Sick pay paid to an employee by a third party such as an insured's group insurance carrier that is paying disability income benefits to a disabled employee
- Employer provided perquisites (perks) such as:
 - An automobile
 - An airplane flight
 - An incentive vacation (e.g., contest winner)
 - A discount on property or services
 - Club memberships
 - Tickets to entertainment events
- Employer contributions to employee benefit plans such as:
 - Employee savings plan
 - Retirement plans
 - Cafeteria plans (IRC 125)

These include contributions made by the employer, at the employer's expense, determined by the amount contributed by the employee.

Once the Audit is Complete

Once the audit is completed, you will want to review the auditor's worksheets. (These can be requested directly from the auditor or ask M3 to have them sent to you.)

- M3 will assist you in comparing the audit statement with your original policy.
- Balance the total audited payroll figures to the documentation provided. Check for any significant changes between the total estimated payroll shown on the policy and the actual figures on the audit.
- Compare the payroll by classification code on the policy to that on the audit. The payroll by classification codes shown on the audit should not contain any significant fluctuations in comparison to the policy.
- Compare the experience modification factor on the original policy to the one shown on the audit. Make sure the auditor applied the factor for the audited period.
- Review the rates charged for each classification code. There should be no changes between the rates on the audit versus the original rates on the policy.
- Officers' payroll should be adequately capped.

A NOTE ABOUT: DEFERRED COMPENSATION

If the deferred amounts are reported as taxable in the current term, they should be included for payroll. If the amounts are deferred, paid and taxed in a future year, though, the amount should not be included for remuneration in the current term.

If you have questions on or would like clarification about the information presented in this article, please **contact your M3 representative**.

About M3

M3 Insurance offers insight, advice and strategies to help clients manage risk, purchase insurance and provide employee benefits. We are committed to being experts in both the products we represent and the industries we serve. Our people advance M3's competitive advantage in the marketplace, and our focus on community builds better places live and work. M3 is consistently ranked a top 100 broker in America.

