

Commercial Insurance Update

Topics Affecting Buyers of Commercial Insurance

MSP C 12/2005 – “What You Need to Know About Crime Insurance”

December, 2005

What You Need to Know About Crime Insurance

By Jeffrey W. Cavignac, CPCU, RPLU, CRIS

If you have anything of value, it's likely that someone will try to steal it.

If you have a standard commercial property policy with a special peril coverage form, you're protected if your business personal property as defined in the policy is stolen. Unfortunately, the business personal property form specifically excludes the following types of property:

- | | |
|-----------------------|-----------------------|
| ➤ Accounts Receivable | ➤ Bills |
| ➤ Currency | ➤ Deeds |
| ➤ Food Stamps | ➤ Evidences of Debt |
| ➤ Money | ➤ Notes or Securities |

In order to cover these types of property, you need separate coverage specifically for crime.

It may come as no surprise to you that the people most likely to steal your property are your employees. The Association of Certified Fraud Examiners (ACFE) has estimated that the typical organization loses 6% of its annual revenues to occupational fraud. Six percent! At that rate, a firm with annual sales of \$10 million would lose \$600,000 a year to fraud caused by employees. “Occupational fraud,” as used here, is defined as “*use of one's occupation for personal enrichment through the deliberate misuse or misapplication of the employing organization's resources and assets.*”



According to the 2003 National Retail Security Survey Final Report, U.S. retailers lost over \$33 billion of inventory to theft, almost half of which was caused by employees. Surveys such as this reflect an unfortunate fact: a firm's own employees, acting on their own or with others, often represent the most significant crime exposure.

Types of Coverage Available

Numerous crime policies are available. Most commonly these are offered on a form filed by the

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2006 Seminars

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- **OSHA Record Keeping / Inspections & Citations**
Friday, January 6th, 2006 — 9:00—11:00 AM
- **Having the Right Safety Attitude / Changing Your Safety Culture**
Friday, January 20th, 2006 — 9:00—11:00 AM
- **OSHA 10-Hour Course — Part 1**
Friday, February 14th, 2006 — 8:00 AM — 12:00 Noon
**(Attendees receive Certificates of Completion for each part
OSHA will provide 10-Hour Card after ALL sessions
have been completed)**
- **How to Run an Effective Safety Meeting and Make Your Toolbox Talks Fun**
Friday, March 10th, 2006 — 9:00 — 11:00AM

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Insurance Services Office (ISO). This article will deal with the most common coverages that should be considered by most business organizations.

Employee Theft

Almost every company needs employee theft coverage, and many property forms automatically include a limited amount. Unfortunately, those limited amounts are often inadequate, and all employers should evaluate their exposures to loss to determine what an appropriate limit would be.

The preferred ISO Employee Dishonesty policy form provides coverage for all employees on a blanket basis. The policy pays for loss of covered property caused by theft committed by one or more employees, whether identified or not, acting alone or in collusion with one or more outsiders. Coverage also extends to employees who are temporarily outside of the policy territory (generally the United States of America, its territories, possessions and Canada) for up to 90 days.

The definition of "employee" is very important. An employee is defined as:

- A person, while he or she is in the named insured's service, and for 30 days thereafter
- Who is compensated directly by salary, wages or commissions
- Whom the named insured has the right to control

Note that all three of these conditions must be met for someone to be qualified as an employee. As mentioned above, the policy does extend to employees up to 30 days after their employment is terminated.

The definition of employee also extends to former employees while serving as a consultant to the named insured. Substitute, seasonal and short-term workers as well as leased employees and guests, students or interns are also included. Note that this latter group of people is only included when they are on your premises and not off your premises.

Employees, trustees, officers and administrators or managers of employee benefit plans are also included under the standard policy form. This allows employers to extend their employee dishonesty coverage to the employee benefit plan if it is listed on the policy.

It is important to recognize that anyone who does not qualify as an employee is not covered. This would include people such as independent contractors working for you, security guards and cleaning people. To appropriately cover this exposure, you can either require the employer of the independent contractor to post a bond, or alternatively, you can have the definition of "employee" redefined under your contract (but some underwriters may not be willing to do this).

You should be aware of some exclusions within the employee dishonesty coverage form. One significant exclusion pertains to employees who have previously committed a dishonest act. Any subsequent loss caused by that employee is not covered.

Inventory shortages are also excluded. There is no coverage if an inventory shortage is discovered by either an inventory computation or profit-and-loss computation. Coverage would only apply if you could establish "*wholly apart from such computations that you have sustained a loss.*"

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Crime Insurance (continued from page 2)

Theft by the named insured, partners, or LLC members is also not covered. You should also be aware that indirect losses, such as business interruption, are not covered.

In order to evaluate your employee dishonesty exposure and whether or not you have appropriate controls in place to manage this exposure, you might want to complete the employee dishonesty checklist following this article.

Forgery or Alteration Coverage

Forgery or alteration coverage protects you from loss arising out of forgery or alteration of checks, drafts, promissory notes, or similar written promises.

“Forgery” is defined as “signing the name of another person or organization with the intent to deceive.” You should be aware that signing one’s own name, with or without authority in any capacity for any purpose, is not forgery. You should also be aware that this coverage pertains to outgoing checks, drafts, and other written promises that are fraudulently drawn on your account.

For example, if checks or drafts were made out to a fictitious payee or payroll were endorsed in the name of the payee, those losses would be covered. Losses arising out of instruments that have been fraudulently altered are also covered (hence the name “forgery or alteration” coverage). However, coverage does **not** apply to fraudulent checks that your firm receives from others.

It is typically recommended that forgery or alteration coverage be purchased along with employee dishonesty protection. Sometimes forgery involves collusion between employees and others; if both coverages are provided by the same carrier, there is no question as to whether or not the loss is covered and, if so, which carrier is responsible.

Computer Fraud and Funds Transfer Fraud

You should also consider coverage for computer fraud committed by outsiders. Note that computer fraud committed by employees would be covered under the employee dishonesty policy.

Computer fraud covers loss or damage to money, securities and other property resulting directly from the use of the computer to fraudulently transfer property from inside the premises or banking premises to a person or a place outside the

premises. The computer fraud policy covers not only money and securities, but also other property. Therefore, computerized theft of stock, equipment and other items would be included.

An exclusion in the computer fraud coverage form eliminates coverage for computer fraud in connection with loss resulting from a fraudulent instruction directing a financial institution to transfer, pay or deliver funds from the named insured’s transfer account. In order to obtain this coverage, you need a separate insuring agreement called “funds transfer fraud.” Once again, we recommend that if you purchase computer fraud insurance, you should also purchase funds transfer fraud coverage.

Money and Securities

To the extent that your company has a significant cash exposure or deals in securities, you may need to consider money and securities coverage.

Typically, this coverage is broken down between on-premises (“inside”) and off-premises (“outside”) losses. **Inside** coverage protects against losses due to destruction, disappearance or wrongful abstraction of money or securities while on your premises or on a banking premises. **Outside** coverage extends to money and securities that are conveyed by a messenger or armored car, or while at the home of a messenger.

This type of exposure usually has high frequency but low severity. As such, it is an exposure that a lot of companies choose to retain.

Crime Insurance (continued on page 4)

Enjoy the Holidays!

- 1. Food shop early.** Make a meal plan to feed the troops, and invest in disposable dinnerware!
- 2. Travel light.** Ship gifts ahead of time. UPS boxes are just as much fun to open!
- 3. Don't eat — exercise!** Walking, sledding, building a bonfire, playing football, etc. cost nothing and alleviate stress.
- 4. Be realistic** in terms of both **time** and **money**. Don’t overbook! If you find you have too many activities, say “no” — you aren’t required to do everything. Make a budget, then stick to it.
- 5. Recharge your batteries.** Schedule “down time” for yourself. Let others share the work! 

Money Orders and Counterfeit Paper Currency

Another available coverage protects you against the acceptance by your firm of counterfeit U.S. or Canadian paper currency or money orders that are not honored. This is not a significant exposure for most firms.

How Much Coverage Should You Buy?

Recognize that the limit of coverage applies to any one occurrence, regardless of how many employees may have been involved in the event. Under forgery, an occurrence is defined as all loss involving a person, even if the loss involves one or more instruments.

In order to figure out how much coverage you really need, you have to figure out what the maximum probable loss will be. Note that this is not the maximum possible loss.

Employee Benefit Plans

The Employee Retirement Income Security Act of 1974 (ERISA) requires that an employer must have employee dishonesty coverage for all persons handling funds subject to ERISA in an amount equal to 10% of the assets in the plan or \$500,000, whichever is less.

In order to include the employee benefit plan on the employee dishonesty form, the plan must be listed as a named insured.

Managing Your Exposure

Crime coverage lends itself to being managed. While you'll never eliminate all crime losses, you can significantly reduce the frequency and manage the severity.

First, identify the exposures. Who might steal from your firm? What could they steal, and how might they do it?

As mentioned earlier, employees have the best opportunity to steal from you. Make certain that applicants for employment are carefully screened, especially those who will be working in management-level positions or other positions in which they will have opportunities to take advantage of their position. Background checks should be a part of a thorough interview process.

Make certain your accounting procedures are solid. Audit trails should help you keep track of your assets as they move through your company. Don't hesitate to use spot checks and surprise audits.

Obvious crime prevention measures include such things as alarms, watchmen, locked facilities, and security lights. Computers and Internet access add additional layers of complexity. Use the advice of experts to make certain that security risks are appropriately addressed. 

Jeff Cavignac, President and Principal of Cavignac & Associates, heads the agency's Professional Liability Department.

Disclaimer: This article is written from an insurance perspective and is meant to be used for informational purposes only. It is not the intent of this article to provide legal advice, or advice for any specific fact, situation or circumstance. Contact legal counsel for specific advice.

Managing the Employee Dishonesty Exposure

Employee dishonesty involves employees stealing their employers' assets. Although most employers feel that this could not happen to them, the fact is that it happens more often than people think, and the perpetrator is generally a long-term, trusted employee.

You can purchase employee dishonesty coverage to protect you from this exposure, but whether or not you purchase the insurance, there are steps you can take to significantly reduce your exposure to loss.

I encourage you to complete the checklist on pages 5 and 6. Any "no" answers are an opportunity for improvement in your current procedures.

Although you can't eliminate your employee dishonesty exposure (unless you get rid of all of your employees), you can significantly reduce the likelihood of such a claim through the implementation of internal processes and procedures. 

Employee Dishonesty Checklist

Receipts

- | | | |
|--|------------------------------|-----------------------------|
| 1. Where currency is a significant part of the daily mail receipts, are two employees, working together, assigned to the opening of the mail? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 2. Where cash sales are a significant part of the business volume, are cash registers with locked controls utilized? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 3. Does the department or person responsible for incoming receipts prepare a daily listing of all items received, showing the customer's name, the amount received, and whether check or currency? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 4. Is the listing prepared in the function described in Question 3 checked by a responsible employee other than the employee preparing the listing, and confirmed with the daily deposit slip to make certain that the receipts were accurately recorded and promptly deposited? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 5. Are the employees performing the functions described in Question 3 separated from the cashiering and the accounts receivable and payable functions? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 6. Are all receipts routed to the cashier's department intact and are receipts deposited intact daily? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 7. Are the receiving and paying cashiering functions segregated? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 8. Is the cashiering function segregated from the accounts receivable and payable functions? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |

Disbursements

- | | | |
|---|------------------------------|-----------------------------|
| 9. Are all disbursements made by check? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 10. Are all checks countersigned? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 11. Where facsimile signatures are used, are the plates and the affixing of the facsimile controlled by responsible employees, other than employee(s) affixing the written signature? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 12. Are authorized check signers segregated from the accounts receivable and payable functions? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 13. Are the documents underlying the payments being made attached to the checks for review when they are signed, and do they provide for departmental approvals and audits? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 14. Are paying documents properly cancelled to preclude their reuse? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 15. Is the mailing of checks under the control of responsible employees, other than the employees originating, approving or reviewing the payments? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 16. Is the bank reconciliation function segregated from the receiving and paying cashiering functions and also segregated from the general ledger, cash receipts and disbursements functions and the accounts receivable and payable functions? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 17. Are the monthly bank statements received from the banks with the cancelled checks delivered unopened to the person responsible for the reconciliation function at the end of the month? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |

Petty Cash

- | | | |
|---|------------------------------|-----------------------------|
| 18. Is a separate petty cash fund maintained in a fixed amount and is the responsibility for this fund restricted to one custodian? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 19. Is the fund reimbursed at regular intervals by issuing a check for the total amount of paid vouchers? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 20. Is the custodian required to record a daily or weekly balance showing the detail of the fund balance? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |
| 21. Is the fund counted, on a surprise basis, by someone other than the custodian? | <input type="checkbox"/> Yes | <input type="checkbox"/> No |

Dishonesty Checklist (continued from page 5)

Accounts Receivable

- | | | | | |
|---|--------------------------|-----|--------------------------|----|
| 22. Are all sales invoices pre-numbered and accounted for over a sales register? | <input type="checkbox"/> | Yes | <input type="checkbox"/> | No |
| Are subsidiary ledger accounts maintained showing the activity in the customer's accounts? | <input type="checkbox"/> | Yes | <input type="checkbox"/> | No |
| 23. Is a monthly trial balance of customer's accounts taken and reconciled with the general ledger control account? | <input type="checkbox"/> | Yes | <input type="checkbox"/> | No |
| 24. Is an aged trial balance prepared by accounting personnel, other than those responsible for the collection function, for the use of management, and is this trial balance reconciled with the general ledger control account? | <input type="checkbox"/> | Yes | <input type="checkbox"/> | No |
| 25. Is the billing and collection function segregated from the accounts receivable accounting function? | <input type="checkbox"/> | Yes | <input type="checkbox"/> | No |

Payroll

- | | | | | |
|---|--------------------------|-----|--------------------------|----|
| 26. Is a separate payroll bank account maintained in a fixed amount and reimbursed in the exact amounts charged against it? | <input type="checkbox"/> | Yes | <input type="checkbox"/> | No |
| 27. Does this firm observe all the controls outlined under the cash disbursements questions above? | <input type="checkbox"/> | Yes | <input type="checkbox"/> | No |
| 28. Are pay checks distributed to employees by someone not in the payroll department, and are any undistributed checks returned to the management (<i>not</i> the payroll department)? | <input type="checkbox"/> | Yes | <input type="checkbox"/> | No |
| 29. Does this firm use time clocks, time sheets or job reports which are periodically spot checked against the payroll checks? | <input type="checkbox"/> | Yes | <input type="checkbox"/> | No |
| 30. Are the authorized check signers segregated from the detail payroll function? | <input type="checkbox"/> | Yes | <input type="checkbox"/> | No |

Miscellaneous

- | | | | | |
|--|--------------------------|-----|--------------------------|----|
| 31. Are all negotiable securities deposited in a safe deposit box subject to joint control? | <input type="checkbox"/> | Yes | <input type="checkbox"/> | No |
| 32. Is the purchasing function segregated from the paying and receiving function? | <input type="checkbox"/> | Yes | <input type="checkbox"/> | No |
| 33. Where inventories are a significant item on the balance sheet, are perpetual inventory records maintained? | <input type="checkbox"/> | Yes | <input type="checkbox"/> | No |
| 34. Are surprise physical inventories taken periodically by someone not in the stock department? | <input type="checkbox"/> | Yes | <input type="checkbox"/> | No |
| 35. Are procedures reviewed by an accounting or audit function for internal control checks and balances prior to implementation? | <input type="checkbox"/> | Yes | <input type="checkbox"/> | No |
| 36. Are the planning, procedures, accounting and audit review functions segregated from the operating function? | <input type="checkbox"/> | Yes | <input type="checkbox"/> | No |



Driving Safely in Traffic

By Stuart Nakutin, PHR, AIC, WCCP, CDMC
Director of Claims and Loss Control

Long-distance drivers know that fatigue is responsible for numerous accidents. But what other factors can cause accidents when you're simply commuting, or driving for short distances around town, making frequent stops?

Some jobs require people to spend a lot of time on the road. On any city street you are likely to see delivery vans, couriers, salespeople, and utility persons making frequent stops. Commuters can spend many hours in traffic going to and from work. Every hour you spend on the road increases your chance of having an accident.

Many accidents occur simply because the driver is going **too fast**. City streets usually have speed limits of 25 miles per hour or less, and you'll often see posted limits as low as 5 or 10 miles per hour.

Speed limits are carefully selected to minimize the chances of accidents. When traffic is heavy, there isn't much distance to stop between you and the next vehicle. The slower you go, the less distance it takes to stop. You'll also be better able to observe your surroundings, taking note of cyclists, pedestrians, and other vehicles. Observing the speed limit is one sure way to reduce your chance of an accident. On rainy, foggy, or snowy days drop your speed even lower.

When you make stops, **park your vehicle carefully**. Avoid leaving it where it will block traffic or create a blind spot for oncoming motorists. Look both ways before exiting to avoid collisions with other vehicles as well as bicycles and passersby.

If you must carry things in your vehicle, be sure the load doesn't obstruct your view. It's safer to make several trips with smaller loads than to pack your vehicle to the point you can't see other vehicles, bicycles or pedestrians clearly.

Another common cause of accidents is **not paying attention**. It's easy to become distracted, frustrated, and annoyed. Any of these can cause you to pay less attention than you should, which then results in rear-end collisions when the vehicle in front of you stops. Running stop lights and stop signs can occur if you're not paying attention.

Paying attention to the wrong things can cause accidents, too. Reading street signs, maps and addresses on buildings while driving can lead to accidents. Find a safe place to pull over to read signs and addresses. Even better, pinpoint the exact location of your destination when you plan your trip — **before** you begin driving.

As with long-distance drivers, **fatigue** also contributes to traffic accidents. Fatigue causes you to become distracted easily and slows your reflexes. Don't take chances driving if you feel too tired. If fatigue is a frequent problem, see your doctor. Combat occasional fatigue with adequate rest, nutrition and exercise.

Many accidents and injuries can be prevented if you keep your speed down, pay attention, and avoid driving when tired. Keep these in mind when you drive and keep yourself safe! 

Generic Medications Keep You and Your Wallet Healthy

Article courtesy of Employee Benefits Department

The majority of generics are typically sold at 15% to 50% less than brand-name drugs.

A generic drug is identical to a brand name drug in dosage form, safety, strength, route of administration, quality, performance characteristics, and intended use.

You can be assured that FDA approved generic drugs have met the same rigid standards as the innovator drug. To gain FDA approval, a generic drug must:

- Contain the same active ingredients as the innovator drug
- Be identical in strength, dosage form, and route of administration
- Have the same use indications
- Be bioequivalent
- Meet the same batch requirements of identity, strength, purity, and quality
- Be manufactured under the same strict standards of the FDA's good manufacturer practice regulations required for innovator products

Contact your physician or pharmacist for information on generic drugs. 