



Pennsylvania Compensation Rating Bureau

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PENNSYLVANIA TEST AUDIT PROGRAM **BULLETIN # 70**

TEST AUDIT APPEAL DECISION

Per Bureau Circular No. 1395, the result of an insurance carrier appeal to the Audit Committee is presented to the membership for their information.

“S” Fence & Iron Works

The carrier was appealing a test audit difference related to “S” Fence and Iron Works’ August 1, 1999 policy. The carrier’s representative brought written handouts that he presented to the Committee. The handouts recounted chronological actions that both the carrier and the Bureau staff undertook in the course of this test audit.

Bureau staff stated that since they were not given the handout prior to the meeting, they were unable to verify the chronology. One of the issues raised by the chronology was the fact that the difference notification was sent 290 days after the policy expiration date. Bureau staff explained that although the worksheets were requested in November 2000, they were not received from the carrier until March 19, 2001. Therefore, Bureau staff had to wait until the end of March to begin the process of comparing the carrier audit with the test audit.

The carrier’s appeal centered on the assertion that the Bureau test audit was not conducted according to the insured’s policy period (August 1, 1999 to August 1, 2000). The Bureau used an audit period of July 1, 1999 to July 1, 2000 with the Bureau auditor noting on his audit worksheets that the risk had misplaced their 1999 payroll records and that an audit by the policy period could not be completed. The carrier representative cited an educational program presented by the Bureau which contained the following language: “Test auditors are instructed to audit by policy period whenever possible. No more than a sixteen-day deviation from the policy period is permitted under the Test Audit Program.” As a result, the carrier representative argued that any audit not completed either on the policy period or within a sixteen-day deviation of the policy period should be rescinded from the Test Audit Program.

In response Bureau staff pointed out that the educational language states, “Test auditors are instructed to audit by policy period whenever possible.” Where it is not possible to audit by the policy period and in order to avoid the wasted time and expense of rescinding the audit, Bureau field representatives may on occasion audit by calendar quarter. If the carrier auditor was able to audit this same risk within 16 days of the policy period, then any payroll differences stemming from the policy period discrepancy would not be subject to criticism. That is what occurred with this test audit, Bureau staff noting that only three employee classification discrepancies were cited as differences. No differences in payroll were criticized.

Another critical aspect to this appeal was the fact that the carrier sent in a revised audit. Normal test audit procedure as well as precedence established by previous test audit appeals requires the Bureau to use the original billing notice for its test audit comparison, in this case dated October 24, 2001. Given this procedure the Bureau did not provide any guidance as to which of the worksheets and billing statements were being used in Bureau responses to the carrier’s letters as the original billing notice was presumably

understood to be the sole basis for comparison and discussion. On the other hand the carrier auditor believed they never had the opportunity to defend their payroll allocations on their audit worksheets since they did not know which set of workpapers were being used for comparison.

Bureau staff explained that carriers are provided with a thirty-day period to respond to a Bureau test audit decision, and it was up to the carrier to determine how to proceed in resolving any test audit difference. In this case the carrier never addressed the misclassification of the three employees causing the criticism of the carrier's audit. Accordingly, the test audit difference involving these three employees could not be dismissed. In essence, it was the carrier's decision to center its appeal based on the argument that the test audit was invalid instead of submitting for consideration rebuttal information on the proper classification of the three employees in question.

The carrier auditor was asked if he agreed with the way the three employees cited as differences by the Bureau were classified by the Bureau. He responded that he agreed with the Bureau on two of them but disagreed with the remaining one. However, the carrier auditor stated that besides the three employees cited there were an additional six employees that were inconsistently classified between the carrier's audit and the Bureau's audit. Also there were nine employees on the carrier audit that were not on the Bureau audit and five employees on the Bureau's audit that were not on the carrier's audit. Bureau staff responded that the payrolls developed by these inconsistently listed employees involved small amounts of payroll and contributed insignificantly to the overall premium difference (payrolls varied from as little as \$40 to \$300).

In conclusion, the carrier representative stated that since the Bureau test audit was not completed by the policy period, it should be rescinded. The three employee misclassifications were not addressed because the carrier representative thought it was a simple case of the Bureau invalidating the test audit by not using the policy period. The carrier auditor went on to state that his company does not contest test audit criticisms based on the policy period because they believe the only way to do a proper audit is by the policy period.

Bureau staff responded that the carrier was specifically told what the differences were, i.e., the misclassification of three employees. These differences were never addressed by the carrier. Payroll discrepancies were not cited as differences. Therefore the Bureau's non-use of the policy period did not invalidate the test audit.

In executive session the Committee reviewed the facts presented in this appeal. The Committee noted the following:

- The carrier did not address the payroll assignments of the disputed employees in question. The carrier audit should have addressed the original criticism noted on the test audit.
- The documentation surrounding the issues presented by both the Bureau and the carrier was confusing.
- The Committee believed the Bureau auditor should have been sent back to the insured to obtain the payroll by the policy period. The Committee reviewed a subsequent letter from the risk's accountant which appeared to indicate that the 1999 payroll records were available.
- The Committee believed that the difference in payroll periods could have resulted in additional payroll and premium being misallocated and that situation was not addressed by the responses provided by Bureau staff.

After some further discussion, upon motion made and duly seconded, it was voted to rescind the test audit from the Test Audit Program.