The Role of the Forensic Accountant in Insurance Claims/Bad Faith

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Financial expertise that matches that of the insurance company is critical when challenging a proposed settlement by an insurance company. Most conscientious business owners buy coverage for fire, business interruption, earthquake damage, etc. Paying the premium and feeling secure as a result are easy. Collecting on the policy when disaster strikes can be difficult and complex. Some examples:

Fire!
A financial services business rented office space directly above a restaurant. The owner of the financial services business received a phone call at 4:00am and raced down to the office to see it fully engulfed in flames. It turns out that the restaurant wasn't doing so well so the owner torched it. The result was the complete destruction of our client's business and all of the records. Nothing was left that could be used.

The business owner was admittedly covered for everything – but the fight had just begun. The insurance company lined up lawyers and adjusters to claim that only a fraction of the dollar loss was covered by the policy. The tenant was left with no choice but to file litigation against the insurance company. An experienced lawyer and a forensic accountant competently developed evidence and presented it to the insurance company. The insurance company decided not to go to trial and settled for hundreds of thousands of dollars more than they originally were willing to offer.

The key in this case was for the accountant to develop accurate historical accounting (when all the records had been burned) and a reasonable and rational interpretation of the insurance contract. There was little doubt that the insurance company was willing and eager to go to trial – until confronted with compelling evidence from an experienced forensic accountant.

Armed Robbery!
At the "Jewelry Mart" in Los Angeles an armed robbery after business hours resulted in several vendors losing everything. This typically meant loss of their safes containing inventory, cash, and all accounting records. While law enforcement pursued the "bad guys," the vendors were forced to hire lawyers and forensic accountants to chase reimbursement from insurance policies that they believed were purchased for just such an event.

Since the inventory was gone the insurance company placed the burden on the vendors to prove that they had any inventory at all. In other words, they took the position that there was no inventory loss. Since all the accounting records were stolen with the inventory the vendors began to believe they were out of luck.

With the assistance of a forensic accountant, purchase and sale records were obtained from third parties and historic financial statements were recreated to establish gross profit percentages, etc. Through hours of hard work and application of accounting formulas the value of inventory was reasonably established. In fact, the insurance company paid the claim having abandoned plans to litigate the matter.

Conclusion

Insurance companies often use the unique circumstances of a disaster to reduce or eliminate their financial responsibility to the policyholder. Often, they are in a position where if the policyholder cannot prove a loss they will not pay. Too many victims of a disaster throw up their hands and give up. An experienced forensic accountant can be critical to resolving the matter. The expert must understand insurance contracts, have a solid background in forensics (developing reasonable conclusions without all the supporting evidence) and be a clear, articulate, and convincing advocate of their opinions. The cost of the expert is often offset by a settlement that is multiples greater than the accountant may have cost.

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