Six Risk Management Mistakes CPA Firms Make

by Tim Huggins

Managing CPA liability risk exposures is a complex process, and it's easy to underestimate the potential for risk along the way. The following six mistakes can be avoided by being aware and taking the right steps.

1. **Not discussing questions about the insurance application with your underwriter or agent.**

   Whether it's for a new or renewal policy, the more communication you have with your representative at the agency or carrier, the better your chances are for securing the appropriate coverage at the most attractive premium rate for the firm. Take time to review the questions and determine what information and data you will need for it; if you're unsure about a question or the information being asked, give your agent or underwriter a call to have them explain it to you. As with any insurance application, you will want to answer all questions truthfully and accurately. CAMICO encourages firms to call their underwriters or agents with questions about the application and the information requested. A phone call is an easy way to address any concerns and to strengthen the relationship between you and your provider.

2. **Not having appropriate policy limits for your firm profile.**

   Excessively high limits of insurance offered at a bargain prices are red flags. High limits will often put a bigger bullseye on your firm and potentially lengthen the claims process. However, you also need to carry enough limit to be able to protect yourself in the event of a bad claim, or to fight a frivolous claim. A specialized underwriter, agent or account executive can discuss your firm's specific risk exposures, policy limits, and coverage options. Each accounting practice is unique—tax specialists have exposures that are different from those of auditors. An underwriter or agent experienced in CPA firms will work with you to create a policy that addresses your specific risk areas, with the appropriate limits and cost structure.

3. **Admitting liability, assuming damages, voluntarily making any payments, or incurring claims expenses.**

   These are all actions a CPA firm must avoid without the prior written consent of the insurance company. Such actions will likely violate policy conditions, which may result in a denial of coverage. Policyholders should not take action without first receiving guidance from a risk adviser with the insurance company. Avoid agreements that include "hold harmless" or indemnification provisions that are one sided and not in the firm's favor. Firms that go along with clients in attempting to a handle problem internally without reporting it are sometimes surprised to find out later that the problem is much larger than it appeared to be. If the problem was not reported timely in accordance with the policy, the damages might not be covered.

4. **Not reporting a potential claim as early as possible.**

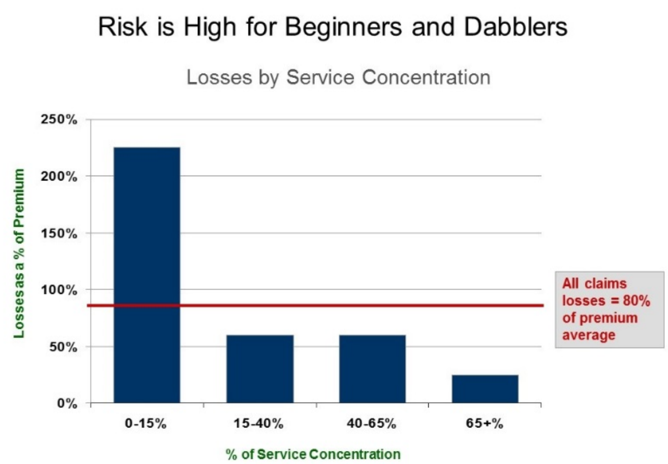
   The sooner claims and potential claims are reported, the more effective an insurer can be at achieving an early resolution. Early reporting will also help assure coverage for the potential claim. Some insurers encourage the early reporting of claims by reducing the deductible for any potential claim that is reported before a claim is made. Further, if it is determined that it is appropriate to retain legal counsel to assist with a pre-claim situation, some insurers will absorb the legal expenses, help policyholders achieve a resolution with the client, prepare a tax penalty abatement request, draft talking points for communicating the facts of the situation with the client, and provide subpoena and other services if the need arises.

CPAs are often so busy that they don't recognize or acknowledge a potential claim as it is developing. This can be particularly devastating when the damages claimed are significant and are not covered because of late reporting. It's important for CPAs to pay attention to potential issues and to report to their carriers as soon as they think there may be a problem. Also new for CPA firms is "continuity of coverage for potential claims," which helps eliminate coverage gaps for potential claims known to an insured and not timely reported by the insured, while coverage is consecutively renewed with CAMICO.

5. **Not utilizing the insurance program's advisory, loss prevention, and risk management services.**

   The best way to avoid a claim is to manage the risks that lead to claims. Some of the basic risk management tools, such as client screening, engagement letters and follow-up documentation, are crucial in managing potentially major problems into minor problems. The more tools and resources an insurance program provides its policyholders, the better those policyholders will be at avoiding or minimizing problems and disputes. A good insurance program will also advise you on how to utilize its resources to help your firm improve its practices. You can also get a good feel for a company's service and attitude toward its policyholders by using its services. If you are interested in a good partnership with your company, the company should do its best to help you minimize your losses and control your premiums.

6. **"Dabbling" in high-risk work without doing enough to stay proficient at it.**



   Claims data show high loss ratios for services that comprise less than 15 percent of a firm's work. By the same token, loss ratios are low for services that comprise 65 percent or more of a firm's work. (See chart on "Risk is High for Beginners and Dabblers.")

   Also, part of the client screening process includes making sure that the engagement is a good fit for the firm's expertise. Proficiency in any type of engagement includes the ability to identify risk stress points in the engagement. CPAs are expected to possess a thorough understanding of the client's business and industry in order to identify those stress points. Establish a policy for what types of engagements the firm will avoid because of a lack of technical expertise. Firms with sound risk management practices tend to write a description of the engagements they accept and the way they conduct business and perform services, including steps for controlling liability exposures (such as engagement letters and other forms of documentation).

The CPA firm should always feel comfortable about contacting its liability carrier and asking questions about any matters, regardless of how small they may appear to be. If the company is committed to providing good services and helping CPAs solve problems, you will discover this just by reaching out with an email or phone call.

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