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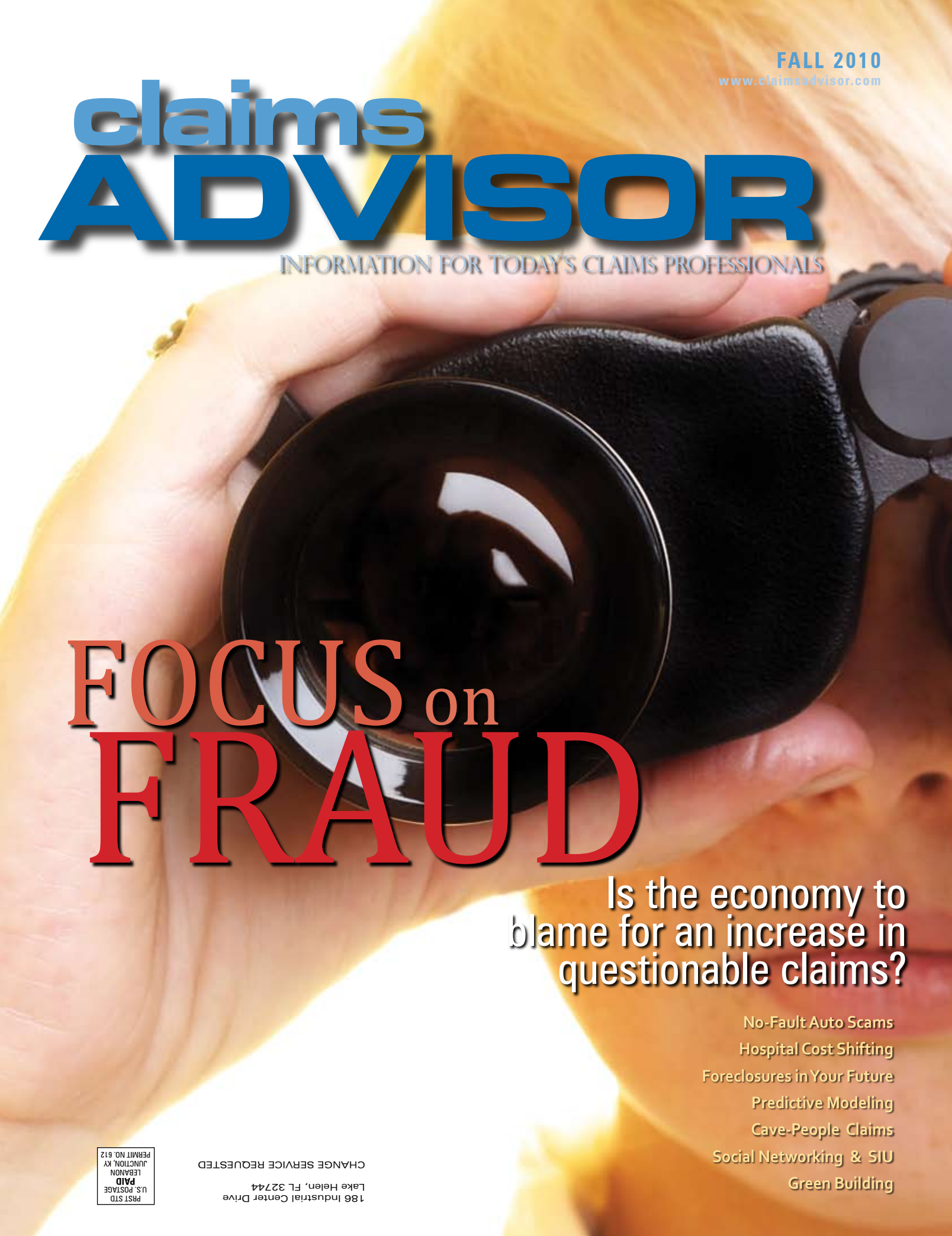

FOCUS on FRAUD

Is the economy to blame for an increase in questionable claims?

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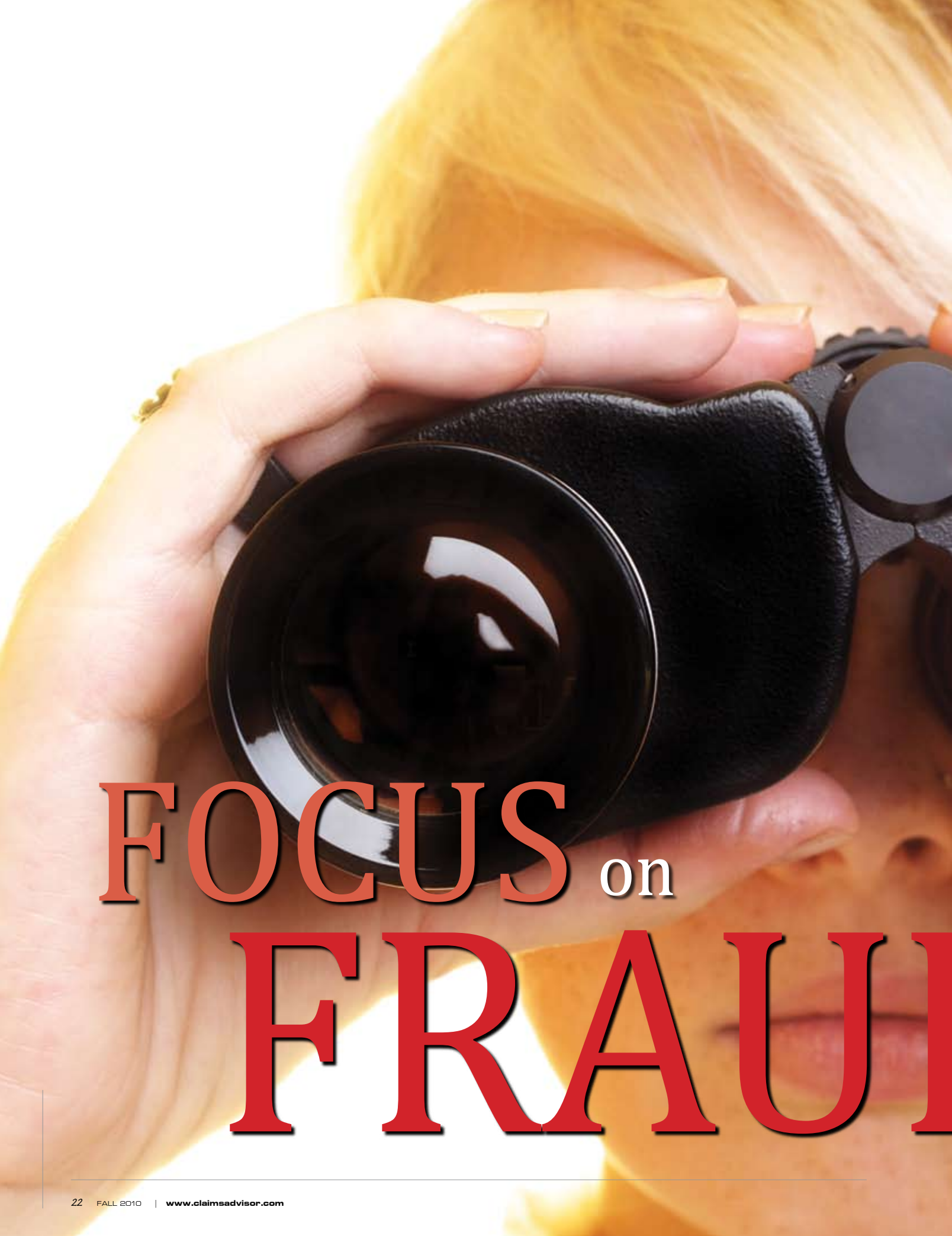

FOCUS on FRAUD

QUICK LOOK

- If you say something often enough, it becomes fact—or at least it gets accepted, whether true or false.
- There is a paucity of data and analysis supporting the assertion that the economy drives insurance fraud.
- Claims data hold the key to verifying or debunking the narrative.

> "We have said the economy may—and the operative word there is 'may'—be a factor. But there isn't any empirical data or study that specifically addresses the economy and a higher incidence of fraud."
>
> *—Frank Scafidi, director of Public Affairs for the National Insurance Crime Bureau*

Is the economy to blame for an increase in reports of questionable claims?

By Dave Pelland and Maureen Latimer

There is a recession. Insurance fraud referrals are up. Recessions cause insurance fraud.

The logic is broadly accepted. To wit, insurance fraud referrals and investigations are up, but there are simply no studies correlating economic conditions with fraud convictions or successful fraud-based claims denials. If declining economic conditions were truly generative of insurance fraud, there should be a verifiable, inverse correlation between economic indicators—such as solid employment, GDP growth, stock earnings, and purchasing power—and the commission of fraud. Unfortunately for the argument, GDP is up, market returns are up, and the rate of increase for job losses is abating. It doesn't look on the surface like recessions cause insurance fraud.

Nationally, GDP has been rising since the second quarter of 2009, with a 2.2% increase in the third quarter and a 5.6% spike in the fourth. This year's second quarter has shown solid growth after a first-quarter increase of 2.7%. The stock market dropped precipitously from 2007 to early 2009, but since then has rebounded dramatically. The Dow Jones Industrial Index grew more than 20% in early March 2009, and the Standard and Poor's Index was up 30% by mid-May and up over 60% by the end of 2009. By April 2010, the

market surge was 80%. If the narrative is correct, insurance fraud should be moving in the opposite direction, inversely correlating with these improving broad economic indicators.

One of the problems that dogs generalized statements about economic conditions and insurance fraud is that fraud is a microeconomic phenomenon. It happens at a very low level of the economy, not the national level. Broad conditions, such as a recession—especially one with conflicting indicators, may have very little to do with actual commission of insurance crime. Studying regional or local economic conditions as they relate to insurance fraud is probably a more germane approach.

Adding to the problem of validating the "economic downturns cause upswings in fraud" argument is the vagueness of the fraud language. Commonly, industry experts commingle the concepts of criminal commission of fraud and fraud referrals or suspicious claims. One is not necessarily the other, and they need to be separated in a true analysis.

Other drivers of potential spurious conclusions are the coincidence of improved reporting technology, persistent un- and under-employment that isn't reflected in Bureau of Labor Statistics pronouncements, and the lack of uniformity in insurance fraud law across the states. The frustrating part of the whole statistical and research dearth is that the data exist buried in insurer claims databases nationwide; there's just been no serious effort to dissect that information and correlate it to pertinent regional and national economic data.

> **"Those with criminal minds are always looking for opportunities. They view committing fraud as a business, and they're always looking at what's happening now and thinking about how they can steal from it."**
>
> *—Joseph Toscano, Chilworth Technology*

What We Know

Insurance fraud referrals are up. According to the Pennsylvania Insurance Fraud Prevention Agency (IFPA), law enforcement agencies in the state received 862 reports of suspected insurance fraud and insurance-related crime in the first quarter of 2010 (a 31% year-over-year increase). Auto insurance accounted for 47% of those referrals, with workers' compensation accounting for 14%.

Of those reports, 144 resulted in arrests in the first quarter: 28% involved allegations of falsely claiming an injury after an auto accident, and 12% alleged buying auto coverage after an accident and lying about the date of loss. Another 9% were charged with falsely claiming the theft of a motor vehicle. Conviction rates from these arrests are unknown, and the year-over-year rate change for arrests is not documented.

> **"Insurers go on high alert during down economies and look at claims very closely."**
>
> *—James Quiggle, director of communications for the Coalition Against Insurance Fraud*

In New York, the state's Insurance Fraud Bureau said the number of criminal convictions for insurance-related crimes rose 24% from 402 in 2008 to 499 in 2009 (after falling from 495 in 2007). The bureau received 24,920 suspected-fraud reports in 2009, an 8% increase over the 23,054 received in 2008 and a nearly 13% increase over 2007's reports.

According to a Coalition Against Insurance Fraud survey of 37 state insurance fraud bureaus last October, referrals and investigations rose in 15 fraud categories during 2009. More than half of the states reported higher numbers of inflated auto claims, and

Empowering Our Advocates

In today's society, lawmakers, regulators, judges, juries, and attorneys are heavily influenced by data. If you want action, you'd better be prepared with numbers and analysis that back up your argument. So far, it has been hit or miss in the state legislatures, and the feds, while making some progress on medical insurance fraud, aren't really on board with—or even capable of—building a zero-tolerance culture on insurance fraud.

What's missing at the state level? Well, maybe the best way to approach that question is from the flipside: What has the industry done in states where significant fraud legislation has passed?

Twenty-five states passed insurance fraud legislation this year. Some of that targeted insureds; some targeted insurers; and some mandated changes to insurance fraud oversight by the state. In Arizona, the legislature tackled auto glass repair shop billing fraud (H.B. 2463). In Colorado, lawmakers raised funding assessments for the attorney general's fraud unit and doubled the penalty for committing workers' comp premium fraud to $1,000 per day (S.B. 12). Also in Colorado, the Senate Judiciary Committee killed a bill, sponsored by its chairman, that would have restricted video surveillance by insurers on suspected WC fraudsters. In Maine, the workers' comp board can now issue stop work orders against construction firms that misclassify workers (H.P. 1102). Roofers in Minnesota are now forbidden to rebate an insurance deductible to a claimant (S.F. 1886). New York (S.B. 5847) and Oklahoma (H.B. 2911) also passed workers' comp anti-fraud measures. What went right?

Howard Goldblatt, director of government affairs at the Coalition Against Insurance Fraud, says, "The key is grass roots action. Parties with a local interest getting the word to their own state legislatures is what gets the lawmakers moving. National organizations, like the Coalition, can support with expertise—research and arguments that can help get their measures passed. For instance, in Louisiana, we helped the insurance department by giving a national perspective indicating that what they wanted to do wasn't out of the mainstream nationally."

The problems local activists and national organizations keep encountering is the general paucity of research on fraud and conflicting language in what industry pronouncements are out there. And that can undermine the case being made for funding, new regulations or rigorous enforcement.

"A lot of information appears to be anecdotal," Goldblatt says, " and we don't have the validated research or data to prove how much fraud is really out there."

Interestingly, in a handful of states, funding was passed or mandates were enacted to support research, studies or fraud plans. Legislators want to know exactly what is going on out there before they cast a vote that could come back to bite them.

59% said they saw more reports of padding of homeowner claims. Workers' compensation fraud reporting was flat, and bogus health coverage cases rose in 57% of the surveyed states.

Okay, so referrals are up. Is that because of the "economic downturn"? Several state insurance commissioners have been touting those statistics as the result of their improved reporting technology. Look at New York, for example. The increase in the number of suspicious claims filed there may have been influenced by the implementation of a Web-based case management system that made reporting easier. Moreover, government analysts and pundits nationwide keep pushing the line that the economy is on an upswing. If the economy is improving and economic downturns cause insurance fraud, shouldn't we see the converse: Shouldn't fraud numbers in 2009—the year the market and GDP began improving—have declined? Maybe there's a lag time, but how long? Don't look for statistical analysis on that either.

And there are other problems with the data. For instance, fire statistics from Michigan indicating suspicious fires rose 13.5% from 2008 to 2009 don't make a distinction between insurance fraud and vandalism. Then there is the Coalition Against Insurance Fraud's statistics on workers' compensation referrals. At the height of new unemployment claims and fear over job safety, workers' comp fraud referrals went flat. The data just don't make the case for a correlation between economic indicators and insurance fraud.

What's Needed

Accurate data make up the skeletal structure of the insurance industry. No carrier can make intelligent strategy without sound analysis. While many industry veterans have that critical institutional knowledge, that can't be the lynchpin of strategy. The departure of seasoned professionals will cause a depletion of that knowledge base; moreover, the new technology of predictive analytics doesn't run off of anecdotes—it uses rich sources of data.

> **"We can get a feel for claims activity in one part of the country that companies may not have seen in another part. If we identify a fraudulent activity trend, we can let insurers know that they may not have seen something yet but it's coming."**
>
> *—James Schweitzer, COO at the National Insurance Crime Bureau*

The call for data and analytics on the correlation between economic trends and fraud—attempted or proven—does not in any way diminish the value of existing institutional knowledge. In fact, proactive insurers will, at the earliest signs of economic distress, start examining claims from economically depressed areas more carefully and reduce the internal thresholds at which claims receive closer examination. Additionally, those with the deepest experience should be called upon to cull through the data and the analysis from independent research firms to validate findings.

"Many claims professionals have been in the business long enough to see a number of economic downturns. They've seen the fraud trends and can predict an increase," says Jim Quiggle, director of Communications at the Coalition Against Insurance Fraud. "Whenever the economy spikes down, institutional memory kicks in. Insurance companies know what kinds of scams to watch for."

That gut instinct is what distinguishes the claims pro from the run-of-the-mill claims processor. Mentoring and training regarding the history of insurance fraud and the red flags to watch for are important in making data and research reports come alive.

"Certainly history repeats itself, and you consistently see things like upcoding or billing for services not rendered," says Lou Saccoccio, executive director of the National Health Care Anti-Fraud Association. "Many times there's nothing new, just an old scheme approached in a different way. The fundamentals are the same, but the details change from time to time."

So what's needed, ultimately, is the marriage of that personal expertise and data, wrapped up in a professional analysis and reported in such a way that it can be digested. We've got the expertise. It's time to compile the data, feed it into computer models and generate cogent and coherent reports. Decision makers need quality, verifiable information to devise and budget for fraud-busting resources for their regions of operations, lines of business, and market segments and sizes. It all starts with dumping our assumptions and focusing on the right questions. CA

Dave Pelland is a contributing writer and Maureen Latimer is managing editor for Claims Advisor.