

Fraudulent Arson Detection: The Adjuster's Central Role

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This paper is developed from "Arson and the Insured" which was awarded the runner up prize in the 1992 Morgan Owen competition.

Arson—the criminal offence

IN ENGLAND, WALES AND Northern Island malicious fire raising-arson-is covered by the Criminal Damage Act 1971. In Scotland the offence is termed 'deliberate fire raising'.

Section 1(3) of the Criminal Damage Act 1971 states that:

An offence committed under this section by destroying or damaging property by fire shall be charged as arson.

The sentence on indictment under s. 1 is up to ten years' imprisonment but in the case of arson the sentence can be up to life imprisonment. As an aside. it is interesting to note that in the Japanese criminal code. arson is still among the most serious of crimes and entails the death penalty, based on the grounds that fire can cause considerable loss of life. This penalty has not been applied in recent years although during the Edo period, which preceded modern Japan. the penalty for arson was always burning at the stake!

Fraudulent arson

Arson per se is not an excepted peril in insurance policies.

If somebody causes a fire without the knowledge or consent of the insured then the policy would be liable to indemnify the insured. The cause of the fire is immaterial except where the fire was caused by:

- a peril which is excepted in the policy: or
- the willful act or connivance of the insured.

A claim submitted to insurers following a fire caused deliberately by the insured is known as arson for gain, or fraudulent arson.

The ABI has stated that fraudulent fire claims are thought to represent between 10 and 20 per cent of all fire claims,

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Cost to insurers

Unfortunately there is little actual evidence to prove or disprove the percentage of fire claims thought by the ABI to be fraudulent. Applying the 20 per cent estimate to the latest ABI figures suggests that fraudulent arson over the past five years cost insurers £862m. calculated as follows:

Year	Total Gross Incurred Claims	Fraudulent Arson 20%
1989	£792m	£158m
1990	£1007m	£201m
1991	£1018m	£204m
1992	£850m	£170m
1993	£648m	£129m
TOTAL=	£4315m	£862m

The above figures do not include business interruption losses or loss to the economy.

The chartered loss adjuster

The Chartered Institute of Loss Adjusters (CILA) is the sole professional body representing individual qualified loss adjusters in the UK. The Institute provides technical support to practicing adjusters and an examination structure offering specialisations in the disciplines of building, financial, misappropriation, liability and contractors.

The Associateship qualification (ACILA) is essentially a demanding second career examination; the minimum entry for admission to the finals is a professional qualification from one of a number of other related institutes.

The impartial independent approach is a fundamental rule of the CILA code of conduct.

On the basis that 10-20 per cent of fire claims are thought to be the result of a deliberate act or connivance by the insured, then conversely 80-90 per cent are not the result of any deliberate act by the insured. Insurers must therefore be sensitive in their approach to the investigation given that a large proportion of arson claims are thought to involve innocent insureds.

An adjuster's approach should involve the exercise of impartial scepticism:

keeping an open mind and constantly reassessing all the information coming from the investigation. The adjuster must show professional concern and courtesy while pursuing all necessary enquiries. Awareness of the customer service aspect of claims handling must be constantly maintained and a balance achieved.

Liability and quantum

During the claim assignment there are essentially two questions that an adjuster needs to answer:

—is the loss covered by the policy?, if so

—how much should be paid?

Other Considerations such as possible recovery aspects are involved but for the purposes of fraudulent arson the first question must be addressed.

Conflicts at the scene

The responsibility placed on the adjuster is heavy. The results of a fire investigation depend on site preservation and evidence integrity. However, these factors conflict with the demands often forthcoming from the insured in terms of agreeing to salvaging operations and debris removal. Pressures arising from requests for payment on account and business interruption considerations must also be attended to at a time when the adjuster is still not in a position to confirm that the fire has occurred fortuitously without any involvement by the insured.

Cause investigation

It is vital to identify properly the cause of a fire. There is a possibility that some arson fires are incorrectly attributed to:

- smokers' materials;
- electrical appliances and installations:
- unknown.

The adjuster's initial assessment of the cause should involve a close consideration of all the natural and common causes of fire. If difficulty is experienced in deciding upon the cause, or indeed if the fire appears to have been started deliberately, it is recommended that the adjuster retain the services of a forensic scientist immediately.

Parties involved

The number of interested parties is considerable and the adjuster may be involved with all or some of them:

- customer of the insured;
- fire brigade;
- forensic accountant;
- forensic scientist;
- health and safety inspectorate;
- insured:
- insureds accountant;
- insured's broker;
- insured's customer;
- insured's suppliers;
- landlord;
- police;
- representative from bankers:
- shareholders;
- suppliers to the insured:
- tenants;
- third parties and their insurers and adjusters:
- utilities;VAT inspector.

Reservation of insurer's rights

From the moment they are instructed to deal with a claim, adjusters will be faced

with pressures from all directions. The insurers will want to know whether the claim is genuine and what reserve should be established. The insured will be pressing for advice on salvaging and interim payments. Until such time as the investigations produce an indication as to the cause, and discount or confirm involvement of the insured, it is recommended that the insured be advised in writing that the adjuster's involvement does not affect or waive insurers' rights under the policy.

Onus of proof

It is for the insurer to prove that the insured started the fire or caused it to be started.

Slattery v. Mance held that once it was shown that loss was caused by fire. The plaintiff had made out a prima facie case and the onus was therefore on the insurer to show that. On balance of probabilities, the fire was caused or connived at by the plaintiff.

Balance of probabilities

Whereas the police in their investigations are obliged to satisfy the criminal onus of proof, i.e. 'beyond reasonable doubt' insurers will only need to prove on 'a balance of probability' basis. However, there is a heavy burden of proof which rests on the insurers' according to Neill. J. who also said in Watkins v. Legal & General.

"I should not make a finding that Mr Watkins deliberately set fire to this warehouse unless I am satisfied that there is a high degree of probability that he did so."

Fire brigade

In the event of a fire the fire brigade is required to produce a report which should include the supposed cause. However, the fire brigade does not appear to have:

- any training or interest in assessing the state of a business at the time of a fire;
- any obligation to co-operate with insurers;
- the resources to salvage property and preserve evidence.

The fire brigade's role is to protect life and property. Occasions may therefore arise when the extent of fire damage increases because the fire brigade is concentrating on saving life or protecting adjacent high-value property. Evidence at the scene may be disturbed during damping down and post-fire activities.

Police

If the fire brigade suspects arson the police will be involved. Arson is a criminal offence and the police are the only organisation empowered to investigate and prosecute. However, the police are not trained in fire science and need to rely on reports either from crime officers or forensic investigators.

There is no obligation to assist or co-operate with insurers and in many cases the police have a policy of non-response to enquiries from insurers and loss adjusters.

Co-operation with brigade and police

It is vital for the adjuster to seek a close and confidential working relationship with the officers involved. It should however be recognised that even though criminal charges may have failed against the insured it may still be possible for insurers to defend successfully the civil case. For example, in Blackmans Glass v. New Zealand Insurance the insurers alleged that the fire had been started deliberately by two members of the insured Company. This allegation was made despite the fact that criminal charges against both men to conspiracy to commit arson had been dismissed by magistrates at the committal stage in January 1990. The earlier case of S&M Carpets v. Cornhill also resulted in a successful defence for the insurers despite the CID's decision not to prosecute two key suspects. One of whom was the insured company's managing director.

Adjuster's investigations

Investigations by the adjuster can be briefly considered under the headings of cause, motive, opportunity, means of investigation and extent of loss.

Cause

The cause investigation will involve the adjuster in forming an early view on whether a forensic investigation should take place. However, the adjuster should not lose control of the cause investigation. A team approach with the adjuster and the forensic scientist working closely together will enable the forensic scientist to gain the information required while at the same time enabling the loss adjuster to maintain full awareness of the cause investigation.

Motive

Considerable thought and enquiry needs to be exercised. Possible motives with regard to arson by the insured include:

- reduced performance of business:
- requirement to upgrade machinery:
- requirement to change and modernise premises.

It is advisable to secure the accounting records as soon as possible. The insured company's insurance files should be located not only for the current period of insurance but also for the previous three years or so. These files will enable the adjuster to gain a picture of the insurance history and the extent of coverage. Any discrepancies between the insured's copy of the current policy and the information from insurers should therefore be identified at an early stage. Previous correspondence and policies will also assist in producing information relating to sum insured levels and claims history.

Opportunity

The adjuster's investigations can be of vital importance not only in terms of the insurance claim but also to support the police investigation. Close and careful questioning of all parties together with detailed enquiries into any significant changes in behavior must be conducted.

The following can provide important information to assist a reconstruction of events, verification of fire development and spread, timings in general and security in particular:

- alarm devices and circuitry:
- clocks, flexitime/clock card systems:
- vehicle tachographs:
- premises and mobile telephone call sheets;
- electrical wiring and fuses:
- memory chips in alarm and other control panels:
- debris and partly damaged property:
- fire brigade, police and central station records

Care should be taken to avoid prejudicing the integrity of anything that might be used in evidence.

The police may be able to give assistance from their records and knowledge. The issue is extremely sensitive but potential fraudulent arsonists should be aware that if they are already known to the police that information may well enter the domain of the adjuster's knowledge. It is clearly of paramount importance that any information received in such a fashion is dealt with confidentially by the adjuster. It should serve to point the adjuster in the right direction rather than form the basis for rash comments or premature and unsound policy repudiation.

Means of investigation

The means used should serve the detection as well as resolution aspects.

A full photographic record should be secured shortly after arrival at the site, but this information should not be relied on to the detriment of scene preservation.

This is especially important where minute objects of considerable significance such as electrical wiring and items contaminated with accelerant may still be in the debris.

If possible a video recording should be made at the earliest opportunity. At the time of such recording the significance of the areas being recorded may not be clear. However, if a full video record is prepared it can be referred to as other information becomes available during the investigation.

Statements recorded in writing at the scene as soon as possible after the incident with careful attention to timings and whereabouts should prove to be most helpful.

Extent of loss

Site preservation will not only enable a comprehensive forensic investigation to proceed but also produce valuable information relating to the quantities and quality of property destroyed or damaged in the fire. As a forensic investigation proceeds the adjuster should 'shadow' the forensic scientist and produce a plan indicating the identity, potential quantity and any identifying features of the debris. A particular characteristic of fraudulent arson fires is that substandard or out-of-date stock has been placed in the building and quite often sufficient identifiable debris is available to reveal inconsistencies against the claim submitted.

Financial aspects

If the policy also covers business interruption then it is likely that the adjuster will look closer at the insured's financial history and potential. Independent financial analysis and comment should also be sought to supplement the adjusters knowledge when necessary.

Working as part of a team the claims accountant can provide specialist Support.

Just as a specialist engineer may be required to deal with a technical problem so an accountant can be of value when dealing with the financial assessment.

The involvement of specialist forensic accountants can give the insured the impression that the claim is suspect. This is especially so if the accounting personnel are not sensitive to the fact that many claimants are genuine. Enquiries therefore need to be conducted properly, fully, but in a sensitive and courteous manner. As with all outside specialists the brief for the accountant should be clearly set at the time of instruction to avoid unnecessary activities, duplication and cost. Communication channels should be established, with the accountant reporting frequently to the adjuster.

In addition to the micro financial aspects the adjuster should consider the macro issues relating to the insured's markets and competitors. It is often the future prospects of a business that are of more significance than the historical accounts, Accounting and management information that should be gathered at the earliest opportunity include:

- audited accounts;
- auditors' reports and correspondence;
- bank statements;
- board meeting minutes;
- budgets;
- bank debentures and guarantees;
- cashflow forecasts;
- company register;
- creditors with aged analysis;
- cashbook;
- correspondence with authorities over corporation tax, PAYE and VAT;
- cheque book counterfoils;
- debtors with aged analysis;

- paying-in book counterfoils;
- payroll summaries and records;
- stock check papers.

Simple accounting ratio analysis can give indications of trends such as rate of stock turnover and solvency. In the event that the insured refuses to provide information considered necessary by the adjuster reference should be made to the policy condition often termed 'insurer's rights following a claim'. The reason for this condition is generally explained as being to the benefit of both the insured and insurers in terms of damage minimisation, salvaging, etc. However, an important purpose as far as the adjuster is concerned is that this condition can be used to support action to:

- secure the premises;
- gain access to all such property that is required for a full and objective investigation;
- establish any involvement of the insured.

Close attention should be paid to the relationship between the insured company and its bankers especially with regard to the provision of overdraft, finance, capital and security requirements during the previous years.

Experience in recent years has shown that banks have not always exercised the prudence which traditionally has been expected of them. Lending has sometimes been to excess and often at levels well beyond the ability of a business to meet repayment and interest charges. The basis of asset valuation as security for finance should be checked for authenticity and accuracy. The way in which the bank's interest has been noted in the policy should also be examined.

The situation where the bank has become a named insured on the policy is of particular concern where a claim appears to result from arson by the insured. The case of *Samuel & Co. v. Dumas* held that

....if two persons insured under the one policy had interests that were separate and distinct, the willful misconduct of one would not affect the rights of the other. If, therefore, a bank becomes a named insured on the customer's policy, it is regarded as a co-insured and would not suffer from the wilful misconduct of its customer.

Adjuster's central role

The response of a survey of UK insurance and reinsurance companies conducted by the writer confirmed that the loss adjuster continues to be regarded as fulfilling a central role in the investigation of fire claims.

However, in recognition of the need for continuous improvement the CILA examination syllabus is to be extended to include arson and fraud topics. CILA has recently decided to encourage qualified members to participate in the activities of their local fire liaison panel. It is hoped that this initiative will help to improve the levels of communication between adjusters, fire brigade and police. It also provides opportunities to disseminate information to CILA members.

The early formation of a multi-disciplinary team with the adjuster coordinating and working closely with the forensic scientist, accountant, and! Solicitor is an efficient and proven approach. It helps to conclude genuine claims efficiently. Fraudulent arson claims can be identified at an early stage and evidence properly collected. This should benefit not only the defence of a fraudulent claim by insurers but could also assist police in the prosecution.

A prompt and co-ordinated approach, including close liaison with the fire brigade and police, should become the 'norm' as it can only be of benefit to genuine policyholders, shareholders of insurance companies and Lloyd's names.

TABLE OF CASES

Blackmans Glass Import Co. Ltd V New Zealand Ins p/c. Unreported. 1991
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