Insurance Claim Account

Introduction-
There may be abnormal losses due to natural hazards or human hazards like earthquake, flood, theft, fire in business. Due to these hazards business may suffer losses and disturb its normal activities. In case of fire broke out in any business premises, it can damage or destroy the Goods/Stocks, Furniture, Plant and Machinery and that can affects profit. To cover these losses company files a claim to insurance company for compensations. According to insurance agreement company pays yearly or quarterly premium to insurance company. After any fire accident insurance company collects information about the reasons of fire accident then calculate the claim amount.

Types of Insurance claim-
1. Loss of Stock (Asset) Policy
Stock is most important asset which is included in working capital. Working capital indicate liquidity of business. In Trading Company stock is more important for liquidity of business. When fire occurs in business it turn into damage of stock and suffering from losses. To cover losses business takes a sock of insurance policy.

2. Loss of Profit Policy
Fire does not affect only stocks it also affected profit. Hence business take the profit policy for affected period called as Loss of profit policy.

Loss of Stock Policy-
*Steps to find out points which are given in problem
1. Find out fire broke out date.
2. Find out Previous financial year starting date and year ending date.
3. Find out Memorandum Trading Account period - which is related to current year starting date upto the fire broke out date.
4. Find out the value at which stock were given whether it was at cost price or under cost or above cost
5. Find out abnormal items or free samples that were given out.
6. To Separate the given information according to Trading Account (for Previous financial year) and Memorandum Trading Account (from the start of current year to the date of fire break out)

Steps for problem solving-
1. Prepare Trading Account- to find out Gross Profit.
2. Calculate Gross Profit Ratio using following formula

   \[
   \text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Sales}} \times 100
   \]

3. Prepare Memorandum Trading Account-to find out stock on date of fire
4. Prepare Statement of **Loss of Stock** using following format

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stock on date of fire</td>
<td></td>
</tr>
<tr>
<td>- Salvaged of Stock</td>
<td></td>
</tr>
<tr>
<td>Loss of Stock</td>
<td></td>
</tr>
</tbody>
</table>

*Whenever the Average Clause is not applied, Loss of Stock amount is applicable for the claim.*

5. **Average Clause Calculation**- If the Insurance Policy Amount is given and the Average Clause is included then the claim amount calculate using to following Average Clause formula

\[
\text{Insurance Claim Account} = \frac{\text{Claim Amount}}{\text{Loss Of Stock}}
\]

*Loss of Profit*

Steps to find out point which are given

1. Find out Fire broke out date
2. Find out Indemnity period or dislocation period
3. Find out upward trends or downward trends in business.

**Problem solving Steps**-

1. **Calculate Short sales**- Using following format

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Rs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales for corresponding period</td>
<td></td>
</tr>
<tr>
<td>-/+ downward /Upward Trend</td>
<td></td>
</tr>
<tr>
<td>-Sales for Indemnity/Dislocation period</td>
<td></td>
</tr>
<tr>
<td>Short Sales</td>
<td></td>
</tr>
</tbody>
</table>

*Least time between Indemnity Period or Dislocation period should be selected.*

2. **Calculate the Gross Profit Rate**- Using the following formula

\[
\text{Gross Profit Rate} = \frac{\text{Net Profit Insured Standing Charges}}{\text{Sales for last Accounting year}} \times 100
\]

3. **Calculate the Loss Of Profit on Sales**- Using the following formula

\[
\text{Loss Of Profit on Sales} = \text{Gross Profit Rate} \times \text{Short Sales}
\]
4. Calculate Amount of Claim
   A. Calculate Insurance Cover Required-Using following formula

   Gross Profit Rate*Sales for 12 months upto date of fire(if upward trend in business Add %)

   *If Average Clause is not applicable Insurance Cover Required Amount is applicable for Insurance Claim.

   B. Average Clause-If Insurance Cover Required is less than Insurance policy Amount then Average Clause is not applicable.
   If Insurance Cover Required is more than Insurance policy amount then following formula is used-

   Amount of Policy
   Amount of Claim = ------------------------*Loss of Profit
                    Insurance Cover
                    Required