



CORPORATE EXPOSURE: Business Interruption

Harry P. Mirijanian

The benefits of business interruption insurance can be measured by insureds through an internal review that begins with the question, "What if?" You should consult your broker once you have completed your internal review and ask for a cost-benefit analysis of adding business interruption coverage to your present property policy. Before you do that, we need to stress an important but often misunderstood point about business interruption insurance. Its purpose is not to put you back in the same position as if the loss did not occur, but to cover your losses during the period that you are making repairs. Only this time frame is covered; if you decide to make improvements or refinements in your operation, the delay caused by these activities is not calculated into your business interruption loss. Expenses to avert further losses, such as occupying an offsite location or repairing the roof so you can continue operating, are naturally covered since the carrier realizes these will reduce business interruption losses. Extra expense coverage to handle costs incurred to continue normal operations can also be purchased and endorsed to the policy. Examples of these expenses are purchasing waterproof tarps or overtime costs.

Insureds can also purchase "extended period" coverage, usually for a specified time period such as 90 days, to cover the additional time after completion of repairs for which losses will occur while they attempt to regain some of their customers. Not surprisingly, the extended

period usually does not begin until the insured is back in business. Determining the exact point at which an insured is back in business can be difficult. For manufacturing plants, the extended period can be the length of time it takes for production equipment to be back in full operation. If production was repaired sufficiently to meet the reduced sales volume resulting from a loss, the carrier could argue that there was no production loss. Fewer clients means fewer production demands. But if the company rented an offsite production facility, it could argue that production was not operational and the extended period should not conclude until the original production line was fully functional.

It is important to understand that just because a business may be interrupted by a loss, the policy does not respond until you can substantiate an "actual loss" or an increase in expenses to prevent further damage. For example, if your inventory was damaged by a covered peril and you could defer deliveries, damaged goods would be covered under the property policy, but there would be no business interruption claim since business was delayed, not lost. To trigger a business interruption loss, the insured must, at its expense, provide the carrier with its loss projections. These projections can be a real source of contention and negotiations are likely. Showing prior months' and even prior years' sales figures may be necessary to support your claim. As a result, how well your organization maintains its records will have a definite impact on your submitted claim. Independent auditing firms may be valuable in such cases. Remember that the cost of preparing these projections is incurred at your expense and is not part of the claim or reimbursable. Although these costs can be significant, they are not covered.

You should also realize that the carrier will require a credit or reduction in

the claim for non-continuing operating expenses due to your loss. Because of the complexity involved in presenting this sort of claim, some insureds retain the services of a public adjuster. This decision is not without its pitfalls. Some believe that because public adjusters take a percentage of the settlement as compensation, it is in their best interest to inflate the claim's true value. Carriers, aware of this, often scrutinize claims submitted by a public adjuster and take a hard line on compromise.

So what should you do? The most important step is to develop a contingency (emergency) plan that encompasses all possibilities. Plan for the availability of offsite facilities, warehouse establishments, etc. The next step is to submit a copy of the plan to your underwriter to demonstrate its thoroughness. This will lead to broader protection and better pricing. Be sure to incorporate your auditor or accountant into your plan. Business interruption claims are much easier to settle with independent, undisputable availability of financial records and reports. Also, be certain that any co-insurance requirements are properly maintained. All too often, we see accounts that fail to maintain the policy-stipulated co-insurance limits. Finally, be sure that your broker explains before a loss how the policy will respond and what records you will have to produce to substantiate your claim. ■

Harry P. Mirijanian is president of Applied Risk, an independent risk management services firm established to assist the business community in reducing exposure to loss and insurance costs. He is a frequent speaker at AMA seminars.



To order reprints call 1-800-644-2464. For photocopy permission see the masthead below. Ask for Article # 7616.

Published as a supplement to the January 1997 issue of *Management Review*.

Finance Forum Editor: George Milite.
Forum Group Editor: Florence Stone.
Senior Editorial Assistant: Grace Lander LoPinto.
Graphic Artist: Jason Klampert.

Copyright 1997, American Management

Association. All rights reserved. Editorial offices: 1601 Broadway, New York, NY 10019; tel: 212-903-8073; fax: 212-903-8083; e-mail: amapubs@aol.com.

For permission to reproduce articles, contact Theresa New at 1-212-903-8283; fax 1-212-903-8083.

For multiple reprints, call 1-800-644-2464; Canadian & foreign, 717-560-2001.

For a single copy request, telephone UMI InfoStore at 1-800-248-0360 (overseas, 415-433-5500).

Additional *Forum* subscriptions are available to members at \$40 each. Contact Diane Laurenzo, Membership Director, AMA, 1601 Broadway, New York, NY 10019. For sample issues, call the Editorial Office at (212) 903-8073.