United Policyholders
Empowering the Insured

Getting (Back To) Business Interruption Insurance

Section 1: Lost property and lost earnings are treated separately

Business interruption insurance (also known as business income protection, profit protection, or out-of-business coverage) provides funds to make up the difference between your business' normal income and its income during and immediately after a forced shutdown. When a business suffers a property loss – such as a fire, storm damage, theft or vandalism – it may be forced to close for some time or move to a new location, temporarily or permanently. A property insurance policy will cover the cost to repair or replace buildings, equipment, and inventory and it may contain special wording that covers loss of income. If it does not have that special wording, you need a separate business interruption insurance policy to cover lost income.

Even when a business has no income, it still must pay regular bills, such as rent or mortgage payments, utilities, taxes, insurance, loan payments, suppliers, and so forth. The company also may have to incur additional expenses related to the loss, such as employee overtime, moving and storage expenses, and rent on a temporary location. Business interruption coverage is designed to provide additional money to cover these kinds of losses and expenses.

Some business interruption policies also provide extra funds for the period of time after the business re-opens and until it gets back to its pre-loss income level. The coverage is designed to put a business back into the same financial position it would have occupied had the incident not occurred.

Section 2: Gross or Net? Lost profits or Lost revenues?

The specific language of your business interruption policy determines how much you can recover in insurance benefits after a loss. And, there are a series of requirements that must be met before coverage for loss of income gets triggered. These requirements will be explained in section 4.

Because it can be difficult to measure how much the business might have earned without the shutdown, the insurer usually will look at the company's income for a period of time (usually one or two years) before the loss and use that figure to project a monthly average of what the earnings would have been. The business owner will be expected to provide documentation to prove the income and expenses for this comparison period. If a business operated at a loss before the incident, most policies will only compensate the owner for fixed expenses, such as rent or certain payroll costs that must continue after the loss regardless of whether the business is operating.

Policies usually specify one or two overall formulas the insurer uses to calculate the amount of the replacement income and for how long coverage will continue after the loss and resulting shutdown. The loss may be calculated based on lost revenues or lost profits. When an actual claim occurs, numerous calculations will be necessary to arrive at the final number that will not be specified in the policy itself. The carrier will apply a variety of formulas, data and accounting principles to determine the actual amount of your covered loss. There are several generally accepted approaches, and different carriers do it differently.

How the loss is calculated, including the duration of the pre-loss period used to project what would have happened had there been no loss, **can make a big difference in what you are paid.**

Section 3: "Period of Restoration"

A critical provision in any business interruption policy is the length of time for which the policy will pay benefits immediately after the loss. This is called the "period of restoration." Typically the period begins on the first day the business must shut down. In certain circumstances there may be a "waiting period" of between 24 hours and a few days, which may be a period for which there will be no coverage, or the "waiting period" may just have to run before benefits become payable back to the first day of the shutdown.

The end of the period may be defined in several different ways. A typical provision provides that the period of restoration ends when the property should, with reasonable efforts, be expected to be repaired, rebuilt, or replaced, or the date business is resumed at a new permanent location. How long these periods will be depends almost entirely on the facts of each loss and each business.

Determining a reasonable period to rebuild is often a source of disputes between insureds and insurers because re-building projects, like construction projects generally, often take

longer than expected for any number of reasons, many of which may be outside the policyholder's control.

Surprisingly, many policies do not specify what happens when the time to rebuild becomes "unreasonable" due to factors beyond the insured's control such as a longer permitting process, construction delays or, where the policyholder leases the space, delays by the landlord in the re-building effort.

1 or 2 years or longer

Many policies provide an additional period, beyond the date when repairs should be completed, on the premise that the impact on revenues and/or profitability caused by having to shut down operations, even for a brief period, can continue beyond the time when repairs are completed and operations themselves return to normal levels. The end point for this period is usually based on a formula for determining when the insured's income has returned to pre-loss levels. Carriers use varying formulas for making that determination, and some are not actually specified in the policy.

Most policies contain a specified maximum limit on the "period of restoration," typically expressed as one or two years after the physical loss itself occurred. It is often possible to purchase extensions of this period for an additional premium. Some policies use a fixed period as the only definition of the "period of restoration" which, if the specified time period is long enough, may be beneficial to the insured because it avoids disputes, and unexpected surprises, that occur when the insurer decides, based on the formulas it uses, that the time for reasonable repairs has ended, or that the policyholder's financial performance has returned to "normal."

Section 4: Business Interruption Coverage Requirements

Standard business interruption insurance has a series of requirements that must be met before coverage for loss of income becomes available:

- **Usually there must be physical damage to your business property.** Because business interruption coverage has traditionally been included as part of, or an add-on to, property insurance, most policies require that your business property sustain physical loss or damage first.
- **The physical damage must occur at the location described in the property policy.** If a

business has not sustained damage, but access is restricted because of damage at a neighboring property, many policies afford only a very limited amount of coverage, usually for a period of between a few days and a month.

- **The physical damage itself must have been caused by an incident, typically called a "peril," the policy covers.** For example, if a fire damages the business, loss of income that results from having to shut down operations will probably be covered as well. If the physical damage is caused by an excluded peril, such as a flood (many property policies exclude, or severely limit, coverage for water-related damage), the resulting loss of income won't be covered either.
- **The physical damage must cause a necessary interruption, or "suspension" of operations.** An example of an unnecessary interruption would be when there is some damage that does not actually require the business to close, but the owner chooses that as an opportune time to shut down anyway to do remodeling work. This is a policy term that often leads to disputes because what closures are "necessary" is often a matter of differing judgments between the business owner and the claims adjuster.
- **Insurers usually interpret the policy to require an actual and complete cessation of your operations before coverage is triggered.** This is a controversial issue in business interruption coverage which comes up most frequently when there is physical damage to the insured's physical plant or equipment (including computer systems) that cuts into revenue but doesn't require a complete cessation of operations or a physical office closure. This issue usually has to be negotiated with the adjuster. In most circumstances, when the issue is whether an actual shutdown is going to be necessary, usually it's in the interests of both the insured and the insurer to avoid a complete shutdown by arranging for repairs to be done after hours or on weekends or days the business is usually closed, or providing temporary space. Often the carrier can be convinced to pay the costs of such measures, as "extra expense," on the assumption that without them there would be a shutdown that would cost the policyholder and the carrier more.
- **The claimed financial loss must be caused by the shutdown, and not by factors unrelated to the physical damage** such as external economic factors, or the owner's decision to do a major remodel requiring a two-month closure when simply fixing the damage would have required closure for only a week. This requirement is also frequently controversial, often because it is difficult or impossible to sort out exactly which of several possible causes compelled the closure.

Section 5: Other types of business interruption coverage

- “Contingent business” interruption extends the coverage to include income losses that are incurred *as a result of property loss at a key supplier or customer location.*
- Should the government deny access to a business due to another entity’s property loss, *“civil authority”* coverage may provide coverage for the loss.
- A business may look to “service interruption” coverage to protect against losses due to a disruption of *utilities or equipment breakdown.*
- “Extra expense” coverage can help businesses with *additional expenses,* such as rent for a temporary location, moving, hiring *additional temporary help,* or the cost of expediting replacement equipment. These are necessary extra expenses during the period of restoration that a business would not have incurred had there been no loss or damage to covered property. Some business interruption policies combine this with loss of business income coverage.
- Some business interruption policies also provide income protection in the event an accident or injury causes the disability of an owner or *key employee.* This type of policy is usually combined with basic individual disability coverage. Though this type of policy is important to help an owner or key employee cover living expenses, additional benefits—in the form of a business interruption insurance policy—are often needed to keep the business running in his or her absence.

Section 6: The Claim Process

Every claim is different. How yours will be handled depends on the wording of your policy, the laws in your state and the personality and training level of the adjuster assigned to your claim. However, if your business has lost income and you’re insured, you have basic rights and can expect the insurance company adjuster to:

- **Promptly and thoroughly investigate.** You can and should expect the claim adjuster to meet with you in person in the first days after the loss to explain the claims process, help you understand what information the carrier needs to resolve your claim, begin the investigation, and provide immediate funding for emergency or urgent services such as interim repairs to prevent further damage or injury or a temporary location to continue operating, as well as advances to cover ongoing expenses, payroll and extra expenses such as temporary help. The adjuster will also likely begin a discussion about what will be necessary to keep your business operating so as to avoid a shutdown and resulting income loss. Be prepared to address questions such as whether you are willing to have repairs/reconstruction done when your business is closed, the extent to which repair work will interfere with or completely halt your operations, what can be done to mitigate those problems, and whether temporary re-location is practical for your business.

- **Gather a reasonable amount of documentation.** The adjuster will explain the information needed to resolve the business income portion of your claim. If the claim is substantial, you will likely be required to produce detailed records of your pre-loss income and expenses, daily or monthly revenues, payroll costs, your usual hours of operation pre-loss, “variable” costs that can be reduced or stopped while business is suspended or reduced, and other data. The carrier will usually want the bookkeeping records you keep in the ordinary course of business and, in cases where this documentation is viewed as incomplete or unreliable sometimes your business tax returns.
- **Work with you to determine the amount of your business income loss.** You can expect the adjuster to work with you, your accountant or representative, and possibly a “forensic accountant” to determine the business income loss. Adjusters often hire one and you may need one too to back up your accountant’s calculations. A forensic accountant combines accounting and auditing with investigative expertise to produce a calculation of business income loss for the carrier. You have the right to hire your own accountant (at your expense) to calculate your loss and to work with the adjuster or the carrier’s accountant. When the loss is substantial, it’s penny-wise and pound-foolish not to get your own accountant or other financial professional involved to assure that the loss is calculated most favorably to you.

An insurance lawyer or public adjuster experienced with business interruption claims can help you maximize your recovery by insisting that the loss be calculated in accordance with policy terms, the law, and applicable insurance regulations, and that where there is ambiguity, room for interpretation, or doubt, that those matters be resolved in your favor.

- The amount of time it takes to complete these steps depends on the complexity of the loss, the availability of documentation, and other factors. You can expect that with a larger loss, there will be significant demands on your time or that of your employees or outside advisors.

What you will need to prove your claim:

If you have a property loss that requires you to close your business, you should be prepared to provide your insurer proof of your business income and expenses for a period of at least one to two years before the loss. The key documents you should have are:

- Financial statements (profit and loss and balance sheet) for at least two calendar years before the loss
- Payroll records you are required to maintain by law
- Sales records for the two prior accounting years (if available)
- Copies of real property and equipment leases, major customer and vendor contracts, and significant contracts material to the performance of your business
- Records that will allow you to establish the “continuing expenses” you will have to bear even while your operations are shut down or reduced.
- Inventory records

You may also need to provide:

• Background details about the business and its products and services including the impact on your monthly revenues and profit of seasonal or other fluctuations unique to your business. This information would likely be important in selecting the particular period of time, prior to the loss, the insurer selects to project what your revenues or profit would have been but for the loss.

- Financial projections you prepared prior to the loss.
- Monthly sales and production summaries
- Inventory detail
- Business income and sales tax returns

In many property loss situations, business records are also lost or damaged, including those maintained on computers. If you maintained a second copy of important records in off-site storage and they are available when the loss occurs, this will raise your credibility with the carrier and its accountant, avoid disputes, and make it harder for an adjuster or insurer to withhold benefits. If accounting records are destroyed, it may be necessary to rebuild financial information from offsite backup files, vendors, customers, and others who may have relevant data. *Property insurance policies typically afford a supplemental coverage, often called “valuable papers and records coverage” for some of those costs.*

Steps you can take to help resolve your claim favorably:

- Do your best to read your policy carefully. If you do not understand how the insurer will calculate the income loss, ask for an explanation and insist that the method of calculation be consistent with

policy terms and applicable laws and regulations.
- Start gathering data immediately following the incident. Don't throw anything away, even if it's damaged, until you determine whether it may be needed to support your claim, including your claim for the physical damage.
- Involve your accountant or other financial expert in any significant financial loss.
- Keep accurate records of sales and operations expenses that continue after a loss. Lost revenue and extra expenses caused by the business interruption should be tracked from day one. You may want to track the extra expenses in a separate ledger or account. Get professional help if necessary.
- Take photographs of the damage before you make any repairs or remove any damaged items.
- Take reasonable steps to avoid or minimize your loss. For example, you may consider re-opening your business at a temporary location, outsourcing of some operations to other organizations, continuing to operate using only part of your business space, etc.
- Keep a log of all your communications with the insurance company during the claim process. Also keep copies of all letters and e-mails you receive from and send to the insurer or its representatives.
- To avoid misunderstandings, ask the insurance company to request documents in writing.
- **Consider hiring an independent insurance adjuster or insurance attorney (at your expense) to deal with the insurance company and advise you regarding how best to prove your claim and maximize your recovery consistent with policy terms.**

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