

# Making sense of Business Interruption Insurance



**Guest editorial**  
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**W**hen we think of property losses in manufacturing or distribution industries, fire damage to the facility, as well as inventory and equipment inside, often come to mind. How will your insurance policy respond to such a loss? What will it pay to rebuild the facility and replenish inventory? Although these are good questions that need to be answered, it's also critical to know your options with Business Interruption coverage (often called Business Income or Loss of Income), which is sometimes overlooked and therefore not well understood.

What if your building had a fire and you were unable to conduct business there? Your property policy would likely pay to rebuild the facility and its contents, but what would happen to your livelihood during the process? Would your employees leave to work for a competitor? How would you retain the customer base you worked so hard to develop? This is the scenario where Business Interruption steps

to the foreground. Coverage can include several things, depending on how it's structured for your operation.

- Loss of revenues from total inability to use the facility
- Reduction of revenues due to the ability to only use the facility at a fraction of its capacity
- Payroll for key employees so they don't go to a competitor during the rebuilding phase
- Payroll for all employees so they don't go to a competitor during the rebuilding phase

In addition, Business Interruption can be structured to include extra expenses incurred from conducting operations at an alternative facility while yours is being repaired or rebuilt. This is referred to as Business Interruption Including Extra Expense. Such expenses may involve rental space for a temporary location; installation of phones, computers, etc.; and advertising that you're still in operation at the temporary location. Extra Expense coverage is provided to help retain as many clients and as much revenue as possible following a property loss. Note, Extra Expense coverage can be purchased by itself, not in addition to Business Interruption coverage. This may be a good option for companies that don't require a specialized facility or have an operation that can be conducted essentially anywhere — but that's typically not the case with manufacturing.

Business Interruption can be extended for a period of time after the facility is rebuilt and you're back to work. This option is offered because it often takes time for revenue to return to

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pre-loss levels. For instance, you may need to contact customers who went to a different facility while you were rebuilding, or re-staff at some level in order to get your building to 100% capacity. A key tenet of this insurance policy is to restore you to “pre-loss condition” — and it often takes more than just repairing or rebuilding and resuming operations.

Once you've reviewed options with your agent and selected the Business Interruption coverage most appropriate for your operations, you'll need to decide how the coverage will pay after a covered loss occurs. Coverage can pay based on length of time you're unable to conduct business or on a dollar amount for a specific time period. Following are examples of both scenarios.

- You can estimate your dollar exposure is about \$1,000,000 per year and that it will take about six months to restore the business to pre-loss condition. In this instance, you choose a limit of \$500,000 at 50% coinsurance, which

tells the insurance company the \$500,000 limit represents half a year. With this example, there is no limitation on the amount you could receive per month — understanding the policy will not pay more than the \$500,000 limit. (You can also choose up to a year or more if estimated restoration time is longer.)

- Using the same \$1,000,000 of exposure, you can choose to receive a certain dollar amount per month. If you think it will take six months to restore your business, you could opt to receive the \$500,000 at 1/6 monthly limit of indemnity. In this scenario, the policy would pay no more than \$83,333 per month for a maximum of six months, or 1/6 of \$500,000. (You can choose other monthly limits such as 1/3 or 1/4 depending on estimated restoration time.)
- When considering coverage needed for your business and method the policy will pay in the event of a covered loss, talk with your agent to determine options that will best protect your business.

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