**Business Interruption Insurance – a short guide**

Put simply Business Interruption policies protect your cash flow and the profits of your business.

The aim is for you to be placed back into the same position after a loss that you would have been in had the loss not occurred.

Usually your Business Interruption cover will be provided as a section of your farm combined policy.

Most BI policies are arranged to cover gross profit, gross revenue and increased cost of working plus if your business earns fees or rents, cover can be made for gross rentals or gross fees.

**Definitions**

A Business Interruption (BI) policy operates by agreed definitions. To make sure that your policy will respond to an insured interruption as intended you and your broker should go through the definitions section to make sure they are correct for your business. Here are the main ones to be aware of:

**“The Business”**

Any part of your business that may be affected by an interruption should be included in the definition of your “business”. If a certain activity is not identified then the policy cannot respond. It is important for example to make sure that if you generate electricity through solar panels on a roof of one of your buildings that ‘electricity generator’ is listed as part of your business description. Then if a fire occurred damaging those panels any income lost from the downtime of those panels could then be claimed for.

**“The Insured”**

BI policies will define “the insured” and so all entities that could be affected by an interruption to the business should be included. This is important for groups of companies that are under one umbrella. For example where there is a manufacturer producing goods; an interruption there will affect the sister company who sells the goods.

**“The Premises”**

Your BI Policy should cover all premises that are owned, occupied or used by your business. Most insurers will require premises to be listed.

**“Indemnity Period”**

BI policies are unique as liability is limited by time (the indemnity period) as well as by monetary amounts (sum insured). Care should be taken to consider the length of your indemnity period depending on the type of business that you have and it’s cycle of production. If your indemnity period is too short then you will not receive a full indemnity.

**Calculating the sum insured and indemnity period**

**Gross profit** is defined in a standard BI policy as:

Turnover plus closing stock and work in progress
Less
Uninsured working expenses plus opening stock and work in progress
Annual figures usually taken from your business’s Report and Accounts are used.

This is not the same definition of gross profit that an accountant would use and this can sometimes lead to confusion and underinsurance. Uninsured working expenses are deducted from turnover to produce the insurable gross profit figure required for your policy.

Uninsured working expenses should only be the costs of the business that vary in direct proportion to turnover. If turnover reduces by 50%, the cost reduces by 50% also. Deducting the incorrect variable expenses can lead to you being over or under-insured.

Being under-insured is more common as some businesses fail to understand the difference between insurable gross profit and accountant’s gross profit. For example wages are not generally included in an accountant’s gross profit but they are included in an insurable gross profit as they do not vary in direct proportion to turnover because of compulsory redundancy payments and the need to retain key staff.

When calculating possible variable costs it must be noted that most losses are partial and not total. In most circumstances you may find that you may need to spend more to keep the business going rather than reduce costs. There is often very little other than bad debts and purchasing that vary in direct proportion to loss of turnover.

When considering an adequate sum insured the anticipated turnover for the policy period needs to be identified and then projected forward so as to be adequate for an incident occurring on the last day of the policy. It must also take inflation in to account up to the expiry of the indemnity period. If this sum is inadequate then average will apply to the loss.

**Gross Revenue** is the total turnover of your business without any deductions for the length of the indemnity period.

So as to take inflation into account insurers use a “Declaration Linked Basis” and allow a maximum of 33.3% uplift in the sum insured and waive average. The figure must then be multiplied by the length of the indemnity period. So if your indemnity period is 24 months the annual figure would be doubled.

There are three main issues for you as the insured with a declaration linked policy:

- Rapidly growing businesses – new businesses often expand as at greater rate than the 33.3% factor so a review of the sum insured on a quarterly basis is required.
- Declining businesses – there is no need for the inflation factor and there may be insufficient return premium available should the decline be beyond 50%. So a review of the sum insured should be undertaken on a regular basis
- Cover placed on a first-loss basis – if the first loss basis is used, the inflation factor is meaningless as the policy limit will be the maximum amount claimable irrespective of inflation.

**Calculating your Indemnity Period**

The length of your indemnity period is important and the worst case scenario should be considered. Items to consider include:

- **Thinking/decision time** – you may have a business continuity plan but a major loss can cause changes. For example you may decide to transfer production to another site.
• **Planning consents and enquiries** – local authorities can take a long time to come to decisions on planning consent. They may even refuse permission to reinstate a building if their overall planning as changed from the use of the area from commercial to residential.

• **Rebuilding/building time** – reinstatement on site may have difficulties for example due to lengthy clear up time for debris removal or pollution clear up. Or it may take a long time to source materials for listed buildings.

• **Lead time for replacement machinery/plant** – some machines may be bespoke and can take a year to replace

• **Re-training staff** – staff may have been laid off so it is important to build in time to train new staff and to re-train existing staff in any new processes

• **Recommissioning plant/systems** – sometimes trying to integrate new replacement kit with pre-existing undamaged items causes more trouble than starting up a whole new plant or system

• **Regaining anticipated pre-loss trading levels** – extra time to regain market position must be allowed for. However pure “loss of market” is not covered.

• **Seasonality** – you may depend on trade from a particular “season” and if a loss occurs immediately before it could miss not one but possibly two seasons, so the indemnity period would need to be 12 months longer than normal.

**Increase in costs of working (ICOW)**

ICOW is already included as an option in the settlement of a gross profit/revenue loss and examples of cover include: additional overtime costs, additional rent for alternative accommodation, removal or additional storage costs, cost of advertising “business as normal”, hire and installation of furniture and other fixtures and fittings, and cost of additional temporary staff.

**Additional increase in cost of working (AICOW)**

AICOW is purchased in addition to the usual ICOW cover and is required where expenditure is necessary and reasonably incurred for the sole purpose of maintaining the turnover of the business. Loss adjusters find this cover helpful as they can agree expenditure of AICOW within the pre-agreed limit without worrying as to whether it will be economic or not. If it does then transpire to be economic then the expense can be moved from the AICOW item to the ICOW item releasing more expenditure, if necessary, to the AICOW item.

The benefit of the AICOW expenditure has to accrue within the AICOW indemnity period. You may need a longer indemnity period for AICOW if costs could continue after resumption of activities.

**Extensions**

When looking at your business interruption cover it is possible to include a number of extensions to ensure that you policy can respond when you need it to. Here are a few examples of extensions that may be available for you to consider.

**Suppliers**

You may be reliant on a supply chain for your final product. If your supplier’s business suffers damage then the interruption could actually be more serious than an interruption at your premises. Failure to obtain key raw materials or service could affect your turnover considerably. Your BI cover can be extended to cover the perils under your policy to cover damage at supplier’s premises.

**Customers**
If you rely on a few key customers then you may have an exposure to your business if a customer can no longer take delivery of your product or service due to damage at their premises.

**Third-party storage premises**
Should damage occur at a third party’s storage premises that you use then turnover may be lost. Insurers can offer an extension to cover such premises treating them as if they were occupied by you.

**Utilities**
Cover is available as an extension as you may rely to some degree on the supply of electricity, gas, water or telecoms to maintain your turnover. You can obtain cover either in respect of damage to the land-based generating station supplying the service or in respect of failure of supply anywhere up to the terminal ends of the supply lines to your premises. The later may be of more benefit as supply can frequently be interrupted due to contractors accidentally digging up cables and interrupting supply.

**Murder, suicide and human contagious disease**
This extension provides cover should you suffer a loss of profit or revenue following a tragic event or the closure of your premises by the authorities due to an outbreak of a notifiable contagious human disease.

**Denial of Access**
Cover here is to protect you for any resulting loss due to prohibited access to your premises due to damage in the “vicinity” (usually defined as a mile) of your premises.

**Cattle Passports**
This extension may be available in order to cover loss resulting from damage to cattle passports from any of the perils under your BI policy.

**Agricultural Vehicles Loss of Use**
This extension may be available to cover the cost of hiring replacement vehicles used in connection with your business should they be damaged by fire, impact, theft or attempted theft.