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BUSINESS INTERRUPTION PLANNING REDUCES COVERED AND NON-COVERED LOSSES

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Rebecca Strickland

Business owners strive to grow their businesses and run them efficiently. However, what happens in the event of an emergency that temporarily closes the business, whether due to natural disasters, fire or a cyberattack? Some planning should be devoted to how they would handle a loss that could cause their business to close. According to the Federal Emergency Management Agency ("FEMA"), "almost 40 percent of small businesses never reopen their doors following a disaster." And according to the non-profit Insurance Institute for Business and Home Safety ("IBHS"), approximately 25 percent of businesses that close due to a disaster never reopen. In the uncertainty that follows a business interruption, a business is more likely to re-open and continue operating in the face of disaster if it has a robust plan in place.

Business Interruption Plans

Insurance policies provide coverage for some aspects of a business interruption. However, insurance is only one component of a comprehensive business interruption plan. Insurance may provide coverage for lost income suffered during the specific period of restoration but restoring business operations quickly reduces long-term effects that insurance cannot cover, such as minimizing the loss of customers and contracts. Therefore, a business interruption plan will help mitigate covered and non-covered aspects of the loss, set forth a plan to resume partial operations or re-open as quickly as possible, and preserve the documentation necessary to present a business interruption claim.

A business interruption plan should identify the most critical business functions to preserve or restore. The IBHS recommends that business owners consider the critical and time-sensitive functions that are necessary to stay in business, prioritize those functions and determine the amount of downtime that is acceptable. The prioritization may depend on which business functions are needed to fulfill legal obligations, maintain cash flow, maintain market share and preserve the company's reputation. A proprietor might perform a business impact analysis to analyze the consequences of different types of disasters.

Critical Business Function Restoration

Once key business functions have been identified and prioritized, the business interruption plan should document the physical and human resources necessary to restore the most critical business functions.

- Where will the business operate?
- What equipment is needed?
- Will the company need to install software on new computers to keep running?
- What data will need to be restored and in what order?
- Is specialized equipment needed?
- Can some product that is usually self-produced be purchased from a supplier or competitor on a temporary basis?
- Which employees and owners are needed to secure the space and equipment?
- Who are the key personnel to oversee the plan?
- Who are the key employees who are needed to perform the business functions on a day-to-day basis?

- What vendors will be needed to help implement the plan?

Depending on the type of loss, the business may need to account for interruptions in supplies, labor, transportation, or technology. The plan must address whether an alternative labor source is available, if needed, or how existing human resources will be reallocated to cover any gaps. A business interruption plan should also address how to protect and recover the business's computer systems and data. Critical computer files, such as accounting records, customer contacts and software, should be proactively backed up regularly before an interruption and stored so that back-ups are accessible in the event of an interruption. In the event that the company's hardware is compromised, the business interruption plan should identify vendors to restore computer hardware, software, and networks.

Insurance Coverage

Business owners who have business interruption coverage for the loss of income during the period of restoration for a covered cause of loss must place their insurance carrier on notice of the loss immediately. In order to recover under the policy, the insured must establish (1) that the loss was a covered cause of loss and (2) the amount of the loss. Proving the amount of the loss can be challenging. The business interruption plan should include an evaluation of the policy requirements to facilitate compliance with the policy conditions after a loss. What is the insured required to do to preserve coverage? What information will be required to present a claim under the policy? By considering the information necessary to present a claim before the loss occurs, a business can include preserving and restoring that information as part of its business interruption plan.

Policies generally provide coverage from the date the loss occurs until the business is back in operation but coverage will end when the period of restoration expires. The method for calculating the amount of the loss during that time period depends on the policy language. In some policies, the loss is calculated as the gross income the insured would have earned were it not for the loss minus the costs and expenses that the insured did not incur. In other policies, the loss is calculated as the net income the insured would have earned were it not for the interruption plus the amount of continuing expenses during the restoration period. Regardless of the method used to calculate the loss, the insured must have documentation of pre-loss income and expenses in order to establish the amount of the loss. Accounting records should be kept current so that pre-loss income and expenses are well-documented and preserved in the event of a loss.

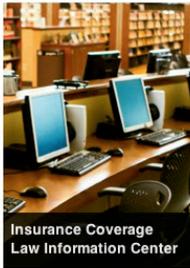
Since business interruption coverage is limited to a reasonable period of restoration, delay in the restoration process could result in a period of business interruption for which no insurance coverage applies. Further, if a policy provides coverage for expedited repairs, then it may reduce the reasonable restoration period if the business fails to expedite repairs. Under the policy, the business may be required to mitigate its losses by resuming partial operations in a temporary facility or by using an undamaged portion of the business. The type of business and core business functions will drive what is necessary to resume partial operations. A manufacturing facility may be able to maintain production levels by adding shifts. A business that relies on face-to-face interactions may be able to reschedule appointments. Some policies provide coverage for extra expenses incurred, such as extra rent. However, the extra expense coverage available may be limited.

Conclusion

In summary, a business interruption plan sets forth practical methods to restore physical facilities, human resources, software and logistical systems as soon as possible. Efficient business restoration minimizes the impact to the business, increases the likelihood that business will be restored during a reasonable period of restoration and maximizes the available business interruption insurance coverage.

About the Author

Rebecca Strickland is an associate at **Swift, Currie, McGhee & Hiers LLP** in Atlanta. Ms. Strickland practices in the areas of insurance coverage, commercial litigation, and intellectual property. She may be reached at rebecca.strickland@swiftcurrie.com.



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