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Do business interruption policies cover small businesses affected by catastrophes like the Victorian bushfires? By Roslyn Atkinson

Imagine running a dry cleaning business in a town that is virtually wiped out by a bushfire. Even if the fire front passes by your shop, what will happen to your customers in the following weeks and months?

Or imagine if you're a restaurant that depends on locals, as well as tourist business, to survive. Following a catastrophe like the Black Saturday fires, who will be going out to dinner?

These were real problems that faced small business owners following the fires in Victoria one year ago that claimed 173 lives.

The fire may not have destroyed their buildings, but it damaged their livelihoods.

Catastrophes cause more than physical damage. Businesses in the surrounding areas can lose customers – whether it's through fewer people living in the area or fewer people travelling to the area.

The question for insurers is: where do you draw the line for a business that is directly affected by a catastrophe and a business that is indirectly affected?

Suncorp – the insurance group behind the Vero, GIO and AAMI brands – faced this conundrum when dealing with business interruption claims due to the ►



Victorian bushfires.

“Strictly speaking, the policy only responds to a claim for business interruption in conjunction with actual property damage at the situation,” said Darren O’Connell, Executive General Manager, Commercial Portfolio.

“Most policies do, however, have a premises in the vicinity/prevention of access additional benefit whereby the damage to premises in the immediate vicinity or intervention by a lawful authority (ie road block) prevents access to, and impacts, the gross profit of the business.”

Suncorp determined that a business had to be in – not just near – a bushfire-affected town to qualify for the additional benefit.

“There were incidents where our customers lodged claims because the fires in nearby areas restricted the access to their towns and consequently to their business premises,” Mr O’Connell said.

“This was deemed not to be in the vicinity of their premises and the claims [were] denied.”

Even for businesses that were deemed to be in the vicinity of the fires, questions arose about the indemnity period to claim loss of attraction.

“Vero took an overall approach that if damage prevented access to a business, the indemnity period would extend until this access was restored (ie the debris removed),” Mr O’Connell said.

“In the case of road blocks, we generally took the view that the indemnity period would be extended to the time the roadblocks were removed in the main areas affected, which was up until March in some cases.”

Those businesses that were able to make a successful business interruption claim due to the Victorian bushfires were among the lucky ones.

“Very few businesses have business interruption cover at all,” said Denis Morrissey, Senior Underwriter for Specialist Underwriting Agencies (SUA).

“The two things that can make or break a business are a large liability claim and the other is a business interruption claim. If they haven’t got enough cash flow, they have a double whammy. They can’t meet their mortgage payments. They lose their house as well as their business.”

Mr Morrissey said loss of attraction was usually considered to be an extension to a business pack. “A lot of people don’t even realise that it’s there.”

He said SUA automatically included loss of attraction in its business interruption policies.

“You’re probably comparing our product, being a Rolls-Royce product, to a standard Holden Commodore product. There’s an increase in costs because of adding additional covers to it ... We have put a lot of add-ons into our policies, so that brokers



A business had to be in a bushfire-affected town to qualify for the ‘prevention of access’ additional benefit.

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don’t have to go and think or ask whether they are necessary or not.”

SUA business interruption policies also include ‘loss of goodwill’, which pays out if the claimant can’t go back into business at all, for example, if they can’t find a suitable location or there are legal reasons that prevent them.

Many business interruption policies have an averaging clause. That is, if a business is only insured for 80% of the total cost if they suffer a total loss, it would only receive 80% of the payout for a partial loss under an average clause.

However Calliden’s Interruption Underwriting Agencies (IUA), which specialises in business interruption, has no averaging clause ensuring that businesses receive adequate cashflow even if they do not suffer a total loss.

“The most important aspect in any claim is the regular flow of claim payments to insureds to keep up their cashflow,” said Stephen Fay, Managing Director at IUA.

“The other important point with loss of attraction and prevention of access claims is to keep an eye on any sub-limits for additional benefits, which are in a lot of policies, as these can have a major impact on the amount that can be paid in the claim.

“With the IUA policy claims are paid weekly and there are no sub-limits on any of our additional benefits, including prevention of access.”

Calculating the loss

Another challenge when determining a claim for business interruption following a catastrophe is working out how much business has been lost.

Forensic accountants such as Chris Ehlers, Director of Matson, Driscoll & Damico, specialise in this field. He notes that damage is usually defined as “physical loss, destruction or damage” to property “used by the Insured at the Premises for the purpose of the Business”.

A hole lot of help

The owner of a carpet business in Sydney was surprised to discover a massive hole had appeared in the road outside his shop – and relieved that he had full business interruption insurance.

On 29 May, 2009, David Raines got a phone call any business owner would dread – and would certainly never expect in their wildest dreams.

“There’s a big hole in the road,” he was told. “It’s outside your store.”

Mr Raines, CEO of Sydney’s three-store chain Raines Carpets, looked with horror when he turned on the TV.

It was more than a hole: a 25m wide crater had swallowed two cars and a telegraph pole, caused by a broken water pipe.

Mr Raines had only taken over the family business a year earlier. Thanks to the foresight of his mother, the financial controller and “the brains behind the business” according to her son, the company had full business interruption insurance.

The Bellevue Hill store is on the corner of Bellevue and Victoria Roads in Sydney’s eastern suburbs. Both roads were closed immediately that the crater occurred.

The roads reopened once the subsiding land was stabilised, but the store suffered a 50% to 70% downturn in traffic because the road was frequently blocked as Sydney Water repaired the crater

Then the council proceeded with previously scheduled beautification works.

“While, theoretically, people could still come in the door, they couldn’t get to the door,” Mr Raines said.

One of his first calls was to his broker, JMD Ross Director John Duncan, on whose recommendation the chain had bought business interruption insurance – a cover it had had in place for about a decade.

Raines Carpets’ claim was paid promptly, which Mr Raines said demonstrated that brokers were “worth their weight in gold”.

This is an edited version of the story that appeared in the JMD Ross newsletter, Spring 2009.



The road collapse in Sydney's Bellevue Hill last May.

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“Whilst insureds can suffer financial damage as a result of the event, or as a result of damage to property owned by others, the trigger for indemnity requires damage to the insured’s own property,” Mr Ehlers said.

He said several policies include extensions of cover that respond to other triggers. Some of these are:

- Service Interruption
- Acts of Civil Authority
- Ingress/Egress (Denial of Access)
- Loss of Attraction, and
- Contingent Business Interruption.

“When a business interruption claim arises as a result of physical damage in conjunction with a CAT event, a forensic accountant’s role is to value the actual loss sustained by the insured had the physical damage not occurred,” Mr Ehlers said.

Interestingly, a catastrophe can cause an increase in business just outside the affected areas.

For example, a major high street retail chain, which had several stores damaged by Hurricane Katrina in 2005, achieved a boost in sales at undamaged locations near the hurricane affected areas. In this case, the increase in revenues represented normal make-up from the loss-affected locations in addition to increased revenues resulting from

consumers replacing their storm-damaged contents.

“It is crucial for the forensic accountant to identify and quantify any increase or make-up in business at these alternate locations,” Mr Ehlers said.

“A further issue that can arise is whether it is economically reasonable to expedite the repair of the physical damage.

“Following the Asian tsunami in 2004, many hotels paid premiums to repair their rooms as quickly as possible; however, in most cases, the demand for these rooms was low and it was therefore not urgent to repair every room on an accelerated schedule.”

Even for businesses with the right insurance, a catastrophe can be too traumatic for a business owner to continue anyway – as was the case with the Victorian bushfires, according to Mr O’Connell from Suncorp.

“We have had customers where it has become apparent that it will take longer than a 12-month indemnity period to reinstate their businesses and get back up and running – and they are persevering,” Mr O’Connell said.

“Others have decided that due to the nature of what happened, they cannot carry on with their businesses. In other instances, businesses are not reopening at all due to the loss of family members, or for personal or safety reasons.”