

Business Interruption Values | Insure Your Exposure, Not Your Values

We recently attended an informative panel discussion hosted by the New York Chapter of the Risk and Insurance Management Society. The theme was “Getting Your Values Right Can Save Your Big Dough!” The panel, moderated by Aon Risk Services’ John Bayeux, included a risk manager, a property underwriter, a broker and the presenter, John Dempsey, the Managing Partner of [Dempsey Partners](#), a business interruption claim consulting and forensic accounting firm.

On this occasion, Mr. Dempsey clearly laid down the premise: When you apply for business interruption insurance coverage, it is more important to insure your *exposure* than your *value*. Insured value is the calculated number at the bottom line of a business income “BI” worksheet. This BI number has two purposes. First, it is used by the insurance company to determine what your insurance limits will be. Second, multiplied by the applicable premium rate, the BI number determines how much the BI portion of your insurance premium will be.

To see what we’re talking about, Zurich Insurance Company has made available on line BI worksheets tailored to six different kinds of business. Follow the link below.

http://www.zurichna.com/zna/online-services/online_agent/business_interruption.htm

As the theme of the RIMS meeting suggests: Report too much BI value, pay too much premium. Mr. Dempsey gave a couple of examples of how he was able to argue with an insurance company for a lower BI value, thereby saving big dough.

Although we haven’t seen too many big dough savings opportunities in the performance of our Diagnostic Reviews, we often discover that our customers really don’t understand how their premium is determined and whether their BI limit is adequate. In the exposure identification phase of our analysis, we generally draw our clients into a discussion of their business and how it might be impacted by a fire, hurricane or other peril.

One slide that Mr. Dempsey showed that caught our eye is approximated by the diagram below. In his hypothetical example, a plant had a physical damage loss due to a covered peril and had to be shut down. Since other plants in the manufacturing chain depended upon this plant to supply them components, this caused those to suffer a loss of production.

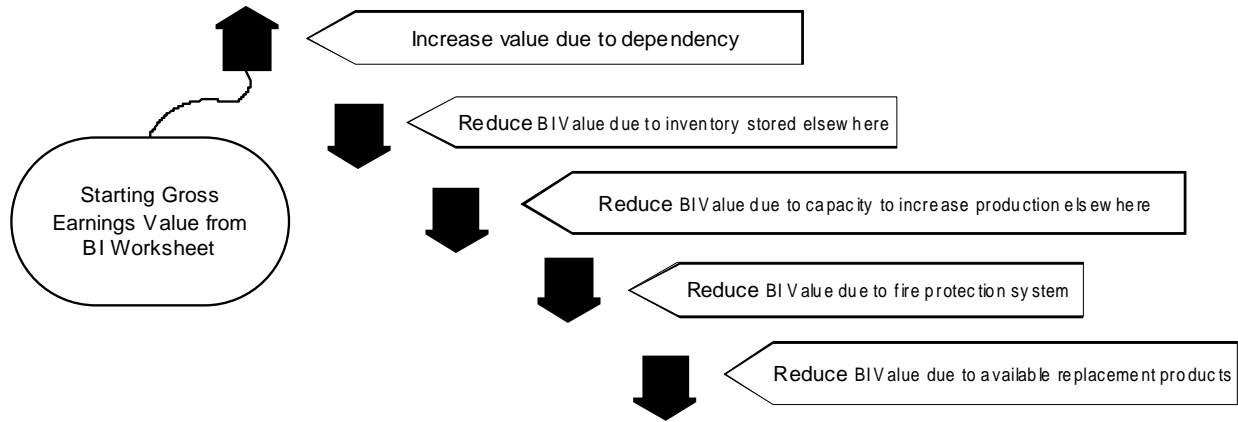
Therefore, in this hypothetical example, the exposure to economic loss exceeded the insured value. Not to worry, some inventory had already been shipped and warehoused at another location. This inventory reduced the exposure. Additionally, another plant could also be re-tooled to manufacture products or components thereby further mitigating the loss.

Yet another mitigating factor is fire protection systems designed to reduce the severity of the loss and its duration. Finally, this business had suppliers lined up that could replace the

product made at the damaged factory albeit at a higher cost but nonetheless enabling the business to fill orders.

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Exposure Factors That Can Increase Or Reduce Insured Values



As the panel's risk manager, Moody's Christine Merkle explained, it was important for Moody's to go through this process in a study conducted by Dempsey Partners. While this study did not save any big dough, management derived a better measure their exposure losses caused by insured perils.

We totally agree with this. Not only do we guide our clients through this process in reviewing their insurance coverage, we also use this approach in conducting Insurance Due Diligence for our private equity clients. In so doing we're looking to avoid the loss of big dough, dough that lenders will be looking for in leveraged transactions. For more information about our Diagnostic Review, Insurance Due Diligence and Business Interruption claim consulting services, visit our Services Menu.