

Business Income Loss Exposure (Lecture 6)

Overview of Lecture 6 (chapter 7 CPCU 3)

- I. Business Income Loss (Time Element or Business Interruption)*
- II. Business Income Exposures*
- III. Basis for Coinsurance and Maximum Probable Loss*
- IV. Selecting a Coinsurance Percentage and Coverage Amounts*

I. Business Income Loss (Time Element or Business Interruption)

A. Business interruption

- 1. net income = revenues - expenses
- 2. "net income loss" versus "business income loss"

B. Continuing versus noncontinuing expense

- 1. continuing expense

2. noncontinuing expense

3. distinguishing between continuing and noncontinuing expenses
 - a. payroll expense

 - b. postage, telephone, heat, light and power

 - c. services performed by others and professional fees

 - d. lease or rental expense

 - e. interest expense

debt on property totally damaged will likely be retired by the insurance proceeds

f. taxes

property taxes - may be reduced if assessed value is reduced

g. advertising

depends on the contractual nature of the current advertising commitments and the need for future advertising

h. insurance

workers compensation will be reduced with a reduction in payroll

i. maintenance of property

4. extra expenses

II. Business Income Exposures

A. Types of business interruption

1. direct business interruption

temporary shutdown due to physical damage to insured's property

2. contingent business interruption

due to damage to another organization's property

B. Timing of a business income loss

1. time to replace damaged or destroyed property

2. time to resume normal income

3. identifying critical factors

- property requiring long replacement time (highly specialized equipment)

III. Basis for Coinsurance and Maximum Probable Loss

A. Business Income Worksheet

1. one purpose is the determine amount of insurance needed to comply with the coinsurance clause

Coinsurance requirement = Coinsurance % x coinsurance basis

Coinsurance basis = (net income + operating expenses)
for the twelve months following policy inception

2. Page 1 - Identification, instructions and signatures
3. Page 2 - Calculating total revenues

- See Exhibit 7-3

4. Page 3 - Calculating net income and expenses
 - See Exhibit 7-5
5. Page 4 - Coverage Modifications
 - See Exhibit 7-6
6. provision for income tax

7. projections based on the Business Income Worksheet

B. Estimating Maximum Probable Loss using the Business Income Worksheet

1. consideration of eliminating noncontinuing expenses

2. estimate maximum period of restoration

3. changes occurring during the period of restoration

worksheet is based upon the 12 months beginning with the policy inception; loss may occur at the end of the policy period and last for an additional 12 months

4. adjustments need to be considered for peak seasons
5. extra expense

IV. Selecting a Coinsurance Percentage and Coverage Amounts