

# Business Interruption Insurance

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## Checklist

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Many businesses suffered a complete or temporary interruption of their business operations due to the damage and destruction caused by Hurricane Katrina.

The following **checklist of basic procedures and considerations** is by no means exhaustive, but is intended as an initial guide, in connection with other materials readily available, to assist in the preparation of business interruption claims. It is important to note that the items on this list may or may not apply to specific claims, depending upon the language of the actual insurance contracts involved and the facts of the claim.

### **STEP 1: Review your Policy**

Many business property policies include business interruption coverage to cover lost business income and at least some of the extra expenses associated with restoring business operations after a property loss. Such coverage's usually apply only to business losses caused by a covered cause of loss to covered property. Policy terms may vary greatly. As with any insurance claim, the first step is to review the applicable policy language.

1. What business interruption coverage do you have?
2. How does your policy define business interruption coverage?
3. What event(s) must occur to trigger business interruption coverage?
4. What time period must pass before coverage is available?
  - The policy may refer to this as the elimination period
  - This is similar to the "deductible amount" for property and casualty insurance.
5. How long does your policy provide business interruption insurance coverage?
  - The insurance company generally covers business interruption losses over the shorter of:
    - The time period the business sustains a loss, or
    - The time period specified in the policy.
  - The insurance company may limit business interruption losses to a maximum amount.

### **STEP 2: Prompt Notice to Insurance Carrier**

Give your insurance carrier prompt notice of the loss including a description of the property involved. It is important to know that property insurance policies, including business-interruption coverage, may include limitations on when a claim can be made. These time limits vary from policy to policy. Failure to give notice to the insurance company within these time limits, or otherwise satisfy such limitations, can invalidate a claim. Notice should provide the following basic information: name and address of insured, location of loss, date & time of loss, contact name, phone & fax number and a brief description of loss.

### **STEP 3: Proof of Loss**

Prepare and sign a sworn proof of loss. A proof of loss provides details identifying the property destroyed or damaged and documents the amount of loss incurred.

### **STEP 4: Mitigation and Recovery**

Take reasonable steps to protect the property from further damage. Policies generally require a policyholder to mitigate its losses.

1. Are you able to access alternative facilities?
2. Could sales or service be conducted elsewhere?
3. Can rental equipment, overtime or additional shift work be used? At what added cost?

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### **STEP 4: Mitigation and Recovery | continued**

4. How much production can be made up with overtime and how long will it take?
5. Will you be able to supply customers from inventory during loss period?
6. If you have to draw down on inventory to meet orders, how long will it take you to replenish inventories to the quantities before the loss?
7. Are there limited markets or major suppliers?
8. How much production can be deferred?
9. Are long-term contracts at risk?

### **STEP 5: Set up Separate Accounts**

Establish separate or sub accounts to maintain a record of the extra expenses incurred due to the property damage, such as:

1. Rent for a temporary location
2. Transportation expenses incurred to relocate
3. Debris cleanup
4. New computers installed at a temporary location
5. Additional marketing and advertising
6. Temporary repairs

### **STEP 6: Gather Pertinent Financial and Legal Documentation**

1. Annual income tax returns for the past five years (Returns that are lost or unavailable may be requested on Internal Revenue Service Form 4506)
2. Monthly sales tax returns for the past three years filed with state or local governments
3. Forms W-2 and Forms 1099 prepared for any employee or independent contractor for the past five years
4. Annual financial statements for the past five years
5. Monthly financial statements for the past three to five years
6. Aged accounts receivable schedules for most recent period
7. Depreciation schedules for the most recent period
8. Overview of business operations
9. Descriptions of products and/ or services offered
10. Customer lists
11. Aged accounts receivable schedules for most recent period
12. Depreciation schedules for the most recent period
13. Overview of business operations
14. Descriptions of products and/ or services offered
15. Customer lists
16. Supplier lists
17. Market share schedules
18. Equipment and facility replacement timetables and costs
19. Formal business plan
20. Budgets or projections of future operations

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### STEP 6: Gather Pertinent Financial and Legal Documentation | continued

21. Articles of incorporation and bylaws, or partnership agreements
22. Minutes of board of directors meetings for the past five years
23. Business lease and rental agreements
24. Business contracts and agreements

### STEP 7: Determine the Probable Period of Interruption

Under most business interruption policies, the period of loss is determined by the time it should reasonably take to repair, rebuild or replace the property after the initial damage has been sustained. In addition, many policies contain language holding that the period of loss does not include "idle periods" in which the business would have ceased operations for any other reason besides the insured risk. The period of loss is generally held to terminate when the repairs to the damaged property have been completed.

### STEP 8: Calculating the Business Interruption Loss

Your insurance policy will define the terms of your coverage:

- Coverage may be provided for your lost profits during the interruption period.
- Coverage of lost profits is generally not coverage for lost revenues, but is coverage for lost profits.
- Coverage of lost profits is generally the amount of lost revenues less the expenses that would have been incurred to produce the lost revenues.

Calculation of business interruption insurance coverage for lost profits: Lost Revenues

- What is the loss period according to the terms of the insurance policy?
- What revenues would have been produced during the loss period had there been no hurricane?
- What revenues were actually produced during the loss period?
- The difference equals LOST REVENUES.

Calculation of business interruption insurance coverage for lost profits: Saved Expenses

- What expenses would have been incurred to produce all revenues during the loss period had there been no hurricane?
- What expenses were incurred to produce actual revenues during the loss period?
- The difference is SAVED EXPENSES.

Calculation of business interruption insurance coverage for lost profits:

$$\text{LOST REVENUES} - \text{SAVED EXPENSES} = \text{LOST PROFIT}$$

Does the insurance policy provide coverage for "extra expenses?"

Extra expenses are generally defined as expenses that would not have been incurred if there had not been the hurricane.

The following list sets forth some representative questions that should be reviewed in calculating the extent of a business interruption loss. This list is not necessarily exclusive, nor does each of the items necessarily apply to every claim.

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### Impact

1. What type of operation is affected (office, store, restaurant, plant)?
2. Is there interdependency with other operations?
3. Is operation partially or totally disrupted?
4. Are sales affected? Partially? Totally?
5. How long will you need to continue paying salaried employees until the business is restored? Can they assist with restoration of the premises and business operation?
6. Do you need to pay hourly employees to retain them during the time the business is not operating?
7. Can they help with clean-up and repair during restoration?

### Civil Authority

Coverage may also be available for loss of business income and extra expenses sustained as a result of government denial of access to your property, due to a covered loss at a location not owned by you. There may be a 2 or 3 day waiting period before coverage begins, and coverage generally only applies for a few weeks.

### Possible Coverage Adjustments

Extended Period of Indemnity: May extend period for loss of income coverage for a specified time beyond completion of repairs.

- Requirement of a Business “Suspension”: May determine whether a complete or partial cessation of business is needed to trigger coverage.
- Resumption of Operations: May limit business interruption loss to the point at which operations can be even partially resumed, even though the business may not be able to fully sustain itself.
- Coinsurance Provision: Requires that policyholder must pay a share of business income loss if the actual loss sustained is substantially higher than the estimated income established at the time insurance was purchased.
- Agreed Value: Establishes in advance a maximum for recovery in any given month.
- Covered Locations: Identifies what locations are covered. There may be extensions of coverage for “newly acquired locations” to cover property recently acquired, and for property at locations not owned by the insured.
- Ingress/Egress: Coverage may be provided for loss of business income and extra expense when you cannot gain access to your property without the government action required under the coverage for closure by a civil authority.
- Building Ordinances: May provide coverage for the additional time required to rebuild due to compliance with building ordinances.
- Electronic Media and Records Limitation: May limit replacement period for such data and documents.

### Possible Exclusions

- Property exclusions: Since there typically must be a covered loss to covered property for business income coverage to apply, all of the exclusions in the property section of the policy are generally relevant.
- Loss of contracts: Income loss on long-term contracts may be limited to period ending with completion of repair or replacement.

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### Possible Exclusions | continued

- Consequential losses: Coverage for consequential losses is generally excluded, unless the policy contains an extension of coverage for such losses.
- Utility service interruption: Coverage generally does not extend to utility service interruption.

### Special Conditions and Limitations

- Appraisal: In addition to loss conditions of the property policy, business interruption coverage may include specific appraisal provisions for valuing the loss of income and extra expenses.
- Loss Determination: Policies typically contain general provisions for determining the amount of business income loss and extra expense incurred. However, you may need to engage the assistance of your agent/broker, accountant, or attorney to provide clarification of some provisions.

During the aftermath of Hurricane Katrina, our firm remains strong and stable and is fully committed to rebuilding the New Orleans metro region. If we can be of service in any way, please contact us.

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