Everything you thought you knew about business-interruption insurance is wrong

Anthony Natole

Bloomberg

A key business survival tool—business-interruption insurance—remains underappreciated and shrouded in confusion, despite the ravages of Covid-19.

Early in the pandemic we learned two basic facts about the insurance: Most small-business owners don't have it, and the policies of those who do have it generally exclude pandemics anyway.

The result was a barrage of lawsuits against insurance carriers filed by frustrated business owners—followed by a return to relative obscurity for business-interruption insurance.

Pandemics aside, in the vast and growing realm of existential business threats—including cyberattacks, looting and power outages—business-interruption insurance is a vital risk-management tool for even the smallest business. It sometimes is the difference between staying afloat and drowning. Carriers, their agents and their brokers should do more to encourage widespread adoption.

Unfortunately, there is a generally poor understanding of what the insurance does. Serving as an extension to a conventional commercial property policy, it insures against the loss of revenue when a covered peril forces a business to cease operating for a period of time. It enables the business to pay its continuing—usually fixed—expenses including payroll and mortgage. It also helps recover the profit that reasonably could have been expected if the business had continued operating. Furthermore, it covers related extra expenses, such as for temporary relocation and expedited shipment of critical equipment, and it can indemnify for abnormal items, like the need for a generator.

What if your enterprise is dependent on another business for a product or service that cannot be easily obtained from another source, and that business encounters operational difficulties? That kind of potentially critical coverage is available under what's known as contingent business-interruption insurance.

Businesses with such a dependency must evaluate the potential perils facing the company on which they depend. Global supply chains are a key element in any such evaluation. And if a business is interconnected to another enterprise online, it likely has a contingent cyber risk if there is a hack to the other firm's system.

An important caveat about business-interruption insurance and contingent business insurance is that to make effective use of them, a small business must be able to produce financial records that prove its claims. Data management and retrieval capabilities are critical. Every aspect of the claim must be documented in order to realize the full benefits of coverage. Therefore, it's imperative for the policyholder to ensure that it has timely access to all relevant data.

Covid-19, we must hope, is a once-in-a-century type of event. But Hurricane Katrina and Superstorm Sandy also were thought to be in that category, and the current century is still young. Keep in mind that disasters can take all sorts of shape and form.

In today's complex and volatile world, business-interruption insurance gives small businesses a chance to prepare for, and transfer, risks that threaten their long-term sustainability. It's a tool that deserves far more consideration than it currently receives.

Anthony Natole is the managing principal of Risk Accountants, a forensic accounting firm in Pleasantville, N.Y.