Business insurance: How coverage is triggered

How does business insurance work?

Unlike home insurance policies in Canada, business insurance has multiple variations. However, virtually all business insurance policies cover damage due to wildfire.

Property insurance for businesses is designed to protect the physical assets of a business against loss and/or damage from a broad range of causes. There are two basic policy types:

1. *Named perils* – covers only loss and/or damage caused by perils specifically listed in the policy. Loss and/or damage caused by any other peril is not covered.
2. *Comprehensive* – covers loss and/or damage caused by any peril, unless specifically excluded.

What is business interruption (BI) coverage?

BI coverage is an add-on to an existing business insurance policy. In the event of a business temporarily needing to shut down, BI covers continuing expenses or replaces lost profits. There are three types of BI policies:

1. *Gross earnings policy,* which pays only until property or damage is replaced or repaired, or stock is replaced
2. *Profits form policy,* which continues to pay until a business resumes its normal, pre-interruption level (subject to policy limits)
3. *Extra expense policy,* which is designed for businesses that can remain operational during periods affected by loss and/or damage.

How does BI insurance work?

BI policies are not standardized and include many variants, but most contain language indicating that the insurer will pay for the actual loss of "business income" due to the "necessary suspension" of operations during "the period of restoration." A number of concepts and nuances come into play, including:

- *Physical damage requirement:* Most policies require proof that the insured premises sustained physical damage (from fire, heat, flooding or firefighting efforts) that is covered under the policy, causing an interruption that resulted in a loss of business income. A business that is interrupted due to the loss of data or a loss of utilities may not have sustained a physical loss. (There is separate utility loss coverage.) Smoke damage likely qualifies as physical damage caused by a covered loss. Most policies would require proof that the presence of ash and smoke resulted in a BI that caused a loss of income.

- *Period of restoration:* If BI coverage is triggered, a significant issue is defining the period of indemnity or, as some policies refer to it, the period of restoration. Most policies will pay business income loss through to the point that the business is restored or when the coverage expires (usually 12 months from the beginning of the interruption).

Is an evacuation covered under BI?

A business that lost income solely because access was denied due to a mandatory evacuation order may be able to claim civil authority coverage, which is separate and apart from BI coverage.

If civil authority coverage is available, it will typically be offered if an insured affected by a mandatory evacuation order proves the:

- Issuance of the order and that it prohibited access to the covered premises; and
- The order caused a business loss.

Some policies state that the coverage applies only if the order is issued with respect to adjacent property or property within a certain geographical radius of an insured location. Some policies state that the indemnity period begins 72 hours after the issuance of the order and extends for a period of weeks (usually three or four weeks) but seldom for a period beyond that. The coverage terminates when the civil authority lifts its evacuation order or the limits have been exhausted – whichever comes first.

Are businesses outside of the fire zone that experienced a disruption in their business covered for BI?

Generally a reduction in customers related to an insurable disruption which results in reduced profits would be covered under a BI policy, subject to the terms of the policy.

Additionally, the BC wildfires may have disrupted the supply chains of businesses outside of the fire zone. Some businesses may have contingent BI coverage (CBI), or “dependent business coverage” for economic losses caused by property damage to a supplier’s premises or for a supplier shutdown due to an evacuation order.

What is the difference between limited and extended indemnity?

The indemnity period is the time period covered for loss of business. There are two basic forms of BI indemnities:

1. *Limited (or earnings).* This policy pays only until the damage is repaired or the property is replaced. As soon as the business resumes, the policy stops paying even if the business hasn’t regained its previous level of earnings.
2. *Extended (or profits).* This coverage continues to pay until a business resumes its normal, pre-interruption level subject to the maximum period of indemnity listed in the policy.

A few statistics on businesses reopening following a disaster

- Statistics from the Federal Emergency Management Agency in the U.S. indicate that after a significant local disaster, 40% of local businesses do not reopen, 25% fail after one year and 90% fail within two years.
- Following the 2013 southern Alberta flooding, 43% of small- and medium-sized businesses did not reopen. Of the businesses that did reopen, 29% failed within two years.

- According to the Calgary Chamber of Commerce report *Flood Resiliency: Insights from a survey of the Calgary business community* 29% of small businesses purchased BI insurance after the 2013 southern Alberta floods.