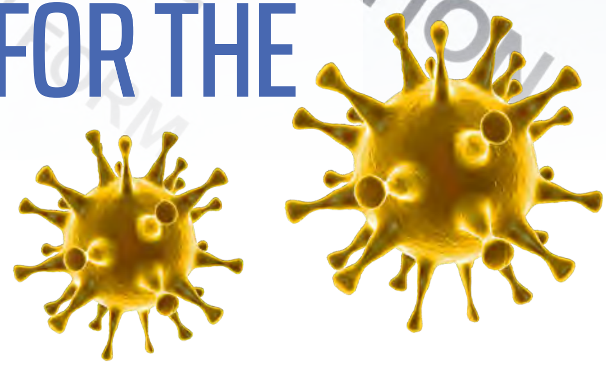
INSURANCE ISSUES FOR THE COVID-19 PANDEMIC



By Ben Morgan and Sheri Wilson

COVID-19 has left many organizations that were growing and thriving a short time ago with the challenge of figuring out how to keep their doors open and their employees paid. After several months of federal, state and local mandates, closures and shelter-in-place orders began to relax in early June. However, as new cases of COVID-19 took a sharp rise in the fall, many businesses faced additional shutdowns. The civil unrest and violent protests that many cities across the country experienced posed an additional threat, with physical harm and actual loss and destruction of business property taking place.

Organizations and business owners alike have turned to their insurance coverage looking for answers to the financial struggles brought on by both COVID-19 and the civil unrest that was experienced by much of the country in 2020. Coverages such as business interruption, civil authority, ingress/egress and protection/preservation of property have all been thrust into the spotlight by local and national news outlets.

These reports only muddy the waters about what relief might be available within an organization's insurance policies.

To brighten the spotlight, many states began to have their own interpretation of the insurance wording, trying to force claims related to COVID-19 to be paid out. For example, California introduced a bill that put the burden of proof on insurers, instead of the insured, requiring the insurer to pay out on many claims for which they may not have collected premium for a specific type of risk, such as COVID-19. New Jersey introduced Bill A-3844, forcing insurers to cover losses from COVID-19 on all small businesses with less than 100 employees that had a business interruption coverage policy in place from March 9, 2020.

Like California and New Jersey, six additional states introduced bills addressing coverage for business interruption claims due to COVID-19. Most were met with fierce opposition from the insurance industry and from many lawmakers on both sides, who expressed their concerns regarding the long-term economic impacts such bills could have on the insurance industry.

As of this writing, most courts have sided with the insurers and upheld the language written in the policies. However, the list of claims and lawsuits being filed against insurers continues to grow, including such companies as Ralph Lauren, which sued FM Global (insurer) for $700 million for their business income losses.

Understanding Business Interruption Insurance

With the global spotlight focused on business interruption (BI) coverage over the past several months, what is the fact and fiction regarding what business interruption coverage is designed for? What, if anything, can and should an organization do in the event it feels it has suffered a loss due to COVID-19 or as a result of the recent civil unrest events around the country?

It is important to understand that BI insurance does not stand alone and is not a mutually exclusive coverage, but rather is attached to a property insurance policy. A property policy, by design, is generally placed to make sure that the assets of a business are insured against loss or destruction, commonly referred to as "direct physical loss or damage."

If a loss such as a fire, lightning strike, windstorm, hail event or flood causes damage to the insured asset, the economic or business revenue generated by the asset could be impacted as well. It is this impact to business revenue generation that property insurance business interruption provisions intend to address for the policyholder.

Since BI coverage is part of a property policy, the losses must be measured according to some generally accepted practices of measuring a loss. A policyholder (insured) sustains a loss and the property policy is activated. The documentation required for recovery is as follows:

1. Event of physical loss or damage;
2. To whom the loss occurred and the location of the insured;
3. Insured peril or event of physical loss or damage;
4. No policy exclusions apply;
5. Insurance company representatives measure the loss.

These steps are commonly called the Chain Rule and at each step, the situation is evaluated. If insureds make it to Step 4 above, they are very close to being made financially whole from the event.

How CPAs Can Help

If clients come to you as their trusted advisor, how do you help? First, ensure they are reaching out concurrently with their insurance broker to get any claim reported and to assist them with understanding what coverages they purchased in the last renewal term. Then, get to work collecting all the right documents.

Accounting documents that will be needed to support a recoverable financial loss include:

- Monthly profit and loss statements in months prior to the closure;
- The strategic operating budget (to include sales and production forecasts);
- Monthly inventory reports;
- Monthly production reports;
- General ledgers;
- Cost accounting reports; and
- Invoices and purchase orders pertaining to the COVID response by the business.

Why the long list? The calculation of any business interruption or other time element insurance loss event is a measurement of costs that are fixed in nature and continue in the absence of any income, the measurement of any loss of profit, and the measure of any extraordinary expenses that are related to the event.

Any costs that vary with sales or revenue, or costs that are not typically incurred during closures, are not considered in the calculations. The recurring statement that insurance companies articulate is that "business interruption recovery is supposed to do for the policy holder what their business would have done had no loss occurred." The policy cannot make an insured in better condition than it was prior to the loss.

What makes COVID-19 so unique is that many of the coverages in the policies, such as BI, ingress/egress, acts of closure from civil authority rulings and others, require that an event of physical loss or damage precedes or "triggers" the other coverages that are within the policy.

Go back again to Step 4 above and consider a policy that has an exclusion for contamination or virus. This exclusion, if well written, can serve to throw out all the other coverages under the policy.

If not well written or otherwise vague, the exclusion can leave the door open for insured businesses to access the full breadth of coverage. The exclusions and their wording are the components that are being litigated, argued, worked around, and otherwise the focus for COVID-19 BI coverage.

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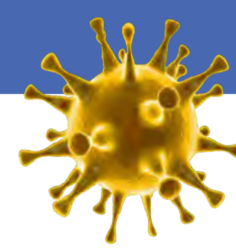

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