
Business Interruption Planning

The remains of the new independent living center dining facility are still smoldering from the massive fire that destroyed over \$5 million of new construction at the ABC Retirement Living campus. Board members, management, a few key donors, and the insurance agent are all on the scene shaking their heads, wondering how this could have happened. Fortunately, no one is injured, but this addition has been three years in development and has been a dream of some of these individuals for over ten years. "At least we had property insurance on this structure," says the Administrator. "We increased your Building & Business Personal Property limit just three weeks ago," says the insurance agent. "Great! We're covered for this loss," says the Board Chair and a deep sense of relief settles over the group.

Variations of this conversation periodically occur when fire, wind, or some other peril brings a loss to our door. The primary concerns that this group had at the time of the loss were related to the destruction of the physical building and its contents.

Several nights later, the CFO (who purchased the insurance policy), wakes up in the middle of the night in a cold sweat. He suddenly remembers that he had declined insurance coverage for "Business Interruption." That decision could cost him his job.

"Business Interruption" insurance is an additional coverage in a comprehensive property insurance program that provides coverage for the loss of income associated with the loss. The Property policy (in this case) has been well written and will address the direct damage (or replace the structure and personal property), less the deductible; however, the financial impact of the loss will not be covered because of the short-sightedness of the CFO.

What does "Business Interruption" insurance provide? When appropriately written, it will address:

- Lost "profit" that would have been made had the facility been in operation,
- Expenses that continue after the loss, and
- New "extra expenses" that come about to keep the facility operational and allow the facility to return to complete operation as soon as possible.

In the scenario described above, this facility included a dining facility and new independent living units. The dining facility could have been used by all residents on the campus and would have been something new for the existing residents. No new revenue would have necessarily come into the equation as a result of its existence; however, the 90 new independent living units would have generated \$2,500 per unit per month totaling \$2.7 annualized. The waiting list was long and would have allowed the fill-up on these units to be under 120 days. The budgeted revenue for the next 12 months was \$2,287,500.

Lost revenue does not mean that the bond interest payments do not need to be made. The efforts made to hire new staff for this addition (who now don't have anywhere to work) have been significant and costly. Layoffs will follow unless the organization chooses to cover the payroll. The expectation is that it will take at least a year to clean up and rebuild. By then, a reasonably good percentage of the future residents on the waiting list and those who have already moved in will have gone elsewhere and the marketing costs to rebuild the waiting list will be significant. The list could go on, but it is clear that the profit that "would have been made" will not be there for some time, some expenses will certainly continue (at least part of the payroll along with numerous other examples), and plenty of new expenses will arise to get back to what the pro-forma predicted in any kind of reasonable time frame.