How to insure your business against loss of earnings due to fire, property damage or other mishaps

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Shelter from the storm … extreme weather conditions can interrupt upstream supplies, threatening revenue. About two thirds of SMEs have no business interruption cover in place. **Photo: Tamara Voninski**

Ruth Liew

From fire and theft to property damages, many Australians understand the value of insurance to protect businesses, but for many small to medium enterprises, business interruption cover is under the radar.

BI insurance, which protects businesses from loss of income, is often cited as a complex product that unfortunately falls into the “too hard” basket for time-poor business owners.

Data from Cameron Research shows around 23 per cent of small companies have not heard of BI insurance.

A further 39 per cent say they have heard of BI products but don’t hold these policies, the 2012 data showed.

The research, which had been conducted on a periodic basis since the early 1990s, showed little change in the take up of BI products among smaller companies in Australia since the survey’s inception.

Impact of a broken link

“It’s a very complicated area because it requires the person, the business owner, to understand not just the immediate issue of something happening to the company but the implication of that event,” Cameron research managing director Ross Cameron said.

“If your place burnt to the ground, you have fire insurance. But if you can’t pay your rent, or you still have ongoing costs from [for example] one of your suppliers getting flooded and it affects your income, that’s when business interruption comes in,” he said.

Unlike the “tangibility” of property protection or liability cover, which are better understood, BI insurance requires company owners and their brokers to understand how a potential broken link in their business chain could impact income streams.

While insurers might fork out payments to cover the physical damages of fire to a particular property, they will not protect businesses from loss of revenue without BI insurance.

According to the National Insurance Brokers Association, BI insurance complements cover on material assets such as buildings, plant and stock.

“It is designed to provide protection against loss consequent upon interruption of the turnover to a business as a result of damage to these assets by fire and other contingencies insured under a material damage policy,” the association said on its website.

While BI cover is not designed to improve a company’s profits, it is there to cover the income gap to help policy holders back on their feet.

“The costs associated with retaining customers and market share and cash flow may create a drain on the financial resources of a business already stretched because of the material losses.

“It is to offset these costs and expenses to maintain the … revenue that all businesses should take out business interruption insurance cover.”

Lack of knowledge

One of the biggest challenges facing Australian SME owners is having in-depth financial knowledge of the companies, including profit and losses and accounting information about their revenue flow.

While big corporations often have a bevy of accountants to audit their finances, some smaller companies may struggle to meet their accountants more than a few times a year.

And even when they do, some owners might not be fully across the in-depth details or projections of their income flows.

“They are time poor, and to be honest, many are busy running their business,” Mr Cameron said.

“Certainly they do need an adviser to talk to them about this. Most of them still deal with an insurance broker, but it’s quite complicated … some [brokers say] it’s a complicated category to sell because it requires key understanding of the business and the mechanics of it.”

BI insurance might be difficult to understand, but industry experts argue that it’s one of the most vital forms of protection for businesses.

“[There is] an education issue around this, a lack of knowledge amongst the community,” said John Phillips, chief underwriting and portfolio manager of commercial at Suncorp.

Mr Phillips argued some of the essential insurance covers for SMEs included fire, liability, BI and management liability.

“They’re four covers we believe every single small business should have, and unfortunately having BI is only one in two [among SMEs] – it’s not where it should be.”

Insurers as educators

Zurich Australia general insurance boss Daniel Fogarty has also argued that insurers should play a bigger role in educating companies about BI cover.

About 61 per cent of SMEs failed to have these protections in place, Mr Fogarty said.

“It’s a problem because that’s when you actually need it – [following a natural disaster],” he said previously.

Darren Maher, chief underwriting officer on BI at commercial insurer CGU, said accountants should advocate the take-up of BI insurance.

Both accountants and brokers played some of the most important roles in the link between SMEs and their insurers.

“Brokers do play a critical role in helping the client to understand their risk and help them to purchase a product that best fits the risks they’re trying to address,” Mr Maher said.

“And every SME should have an accountant. What are the expenses that are ongoing, fully variable? The accountants are in the best position to speak with them on what they should be insuring for.”

BI eases recovery

While industry leaders debate solutions to the issue, one stark reminder of the need for adequate insurance cover came in the form of the Queensland floods earlier this year.

As ex-cyclone Oswald ravaged parts of Queensland, bushfires also swept through parts of Tasmania.

Data from the Insurance Council of Australia last month showed flooding in Queensland wreaked overall insurance losses of about $553 million.

Insurers received more than 65,000 claims and netted $674 million in insurance losses from natural catastrophes this summer to February.

The recent events come after a devastating year for natural perils in 2011, when three-quarters of Queensland was declared a disaster zone.

Both households and businesses needed to pick up the pieces after each catastrophe. But for those holding appropriate insurance cover, including BI policies, the recovery process was much easier.

Earlier this month, the federal government also announced a $185 million package aimed at reducing the costs of insurance for households, mitigating flood risks and repairing flood-damaged Queensland.

A recent survey by global insurer Allianz found 46 per cent of Australian risk managers said natural catastrophes represented the biggest corporate risk facing local businesses.

Around 33 per cent said BI was a big worry to business operations.

“After a relatively benign year for extreme weather events in 2012, the fires and floods of early 2013 have proved that the fears of business are well founded,” Allianz Global Corporate and Specialty Pacific general manager Holger Schaefer said.

Affordability issue

While businesses were worried about the risks of getting back on their feet following a big catastrophe, the trend did not translate to bigger insurance take-up.

Data from Roy Morgan showed that only one third of Queensland businesses had property cover, and only 14 per cent held BI insurance.

Affordability is a key issue fuelling Australia’s under-insurance problem.

Suncorp’s latest Vero SME Insurance Index showed three out of four SME owners expected their insurance costs to jump this year, with more than half bracing for a rise of 10 per cent or more.

The index showed SMEs appeared to have reached “breaking point” in terms of what increases in insurance costs they could bear, and some were beginning to question the value of their cover.

Two years ago around one in three businesses said they were able to absorb the costs of higher premiums. Last year only 15 per cent of business owners said they could do the same.

Mr Phillips says the issue of insurance affordability was particularly evident at the smaller end of the SME spectrum.

Some business owners may also hold the belief that they have little profit to protect, especially if the companies are just starting.

“Start ups and entrepreneurs . . . I think there’s this perception around that young businesses . . . have little profit to protect.

“The $2000 [in insurance premiums] could be the difference of me surviving and not surviving,” he said of some businesses’ views on costs.

There are two ways of viewing affordability and it’s not just about the dollars and cents of the cover, Mr Maher argued.

“Yes, one is the affordability of buying the right cover . . . [the other is] what you can afford not to have in the event of losing that asset. You have to weigh them up.”

Mr Maher said one ways to improve the take up of BI cover was through education.

“Risk matters,” he said. “We should look at partnerships with institutes to promote understanding risk.”

“It’s not just an insurer challenge, it’s a business challenge. We need to get professional managers involved . . . and collectively look to educate people that are just starting out in their business life about the need for insurance.”

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