



The Chartered Institute of Loss Adjusters

Associateship Examination 2010 (April)

Paper C3

**Adjustment of Claims
Business Interruption**

3 ½ Hours

Maximum Marks 200

Answer ALL questions *in Part 1 and 2 questions from Part 2*
Where appropriate, answers should make reference to relevant case law or statute

PLEASE ENSURE THAT QUESTION NUMBERS ARE ENTERED CLEARLY AND IN FULL ON THE COVER OF YOUR ANSWER BOOK AND IN YOUR ANSWER BOOK



PART 1

ANSWER ALL QUESTIONS

QUESTION 1

a) In a typical Business Interruption Policy explain briefly what is meant by the following terms:

1. Gross Profit
2. Additional Increased Costs of Working
3. Alternative trading clause
4. Professional Accountants Clause
5. Denial of access extension

(15 marks)

b) You are dealing with a claim for fire damage which has occurred in a local suburban licensed restaurant. The restaurant is in family ownership and has been established for several years. It is open for business seven days a week providing lunch and evening meals. The same family members also own a fast food takeaway only restaurant located about one mile away from the licensed restaurant.

The fire has caused severe damage to the building and to trade fixtures, fittings and equipment. All the stock comprising foodstuffs and beverages etc has been destroyed. The Insured will not be able to trade from the premises again until the necessary building repairs have been carried out and the various trade contents and the stock has been replaced.

Your Principals' policy covers all the trade contents including stock and provides cover for business interruption with a twelve month indemnity period. The building is insured by the Landlords and their Insurers have appointed their own Loss Adjusters. Your principals' Insured have not engaged Loss Assessors or other advisors to act on their behalf and, for the purposes of the claim negotiations, it has been agreed that you will be dealing direct with two of the family members who own the business.

With specific reference to the Business Interruption element of the claim, the following issues arise:

1. You are told that the building owners wish to take the opportunity to incorporate certain improvements and alterations during the course of the work. Some of these improvements etc will be carried out to enhance the premises for the subsequent benefit of the Landlords but certain others will be necessary to comply with current



statutory requirements. If reinstatement had been carried out to the original specification then a contract period of approximately eight months would have been anticipated but to allow for the additional work a revised contact period of approximately eleven months has been projected. Explain how you would deal with this situation and detail what advice you would provide to your Principals and their Insured.

2. Explain the measures that could be taken to mitigate the effect of the interruption to the Insured's business and the ultimate financial liability of your Principals.

3. Following the closure of the restaurant the Insured have laid off a number of casual and part time staff. However, they also employ a number of key staff including their head chef. They wish to continue to employ them whilst the business is temporarily suspended so that they are immediately available once normal trading can be resumed. Detail the likely cover and explain how you would deal with this.

4. In relation to the Material Damage element, the sum insured on trade fixtures and fittings etc was not adequate. Following the application of average the Insured have incurred a shortfall of £10,000 on that part of the claim. They now seek to include the shortfall within the Business Interruption item on the basis that this is a "consequential loss resulting directly from the fire". Explain the response you would provide to the Insured.

(25 marks)

40 MARKS



QUESTION 2

1. Explain the difference between contribution at Common Law and Contribution in accordance with ABI Rules.

Give one example of each.

Give two examples where contribution is specifically excluded by ABI rules.

(10 Marks)

2. Where applicable, in all parts of the following questions all workings must be shown:

a) In a policy with a pro rata average condition calculate the amount payable:

(i)

Agreed Loss	£100,000.00
Sum Insured	£150,000.00
Value at Risk	£200,000.00
Salvage	Nil
Excess	£500.00

(6 Marks)

(ii)

Agreed Loss (subject to salvage)	£150,000.00
Sum Insured	£100,000.00
Value at Risk	£150,000.00
Salvage	£ 20,000.00
Excess	£ 250.00

(6 Marks)

b) In a policy with a 20% Co-Insurance Clause calculate the sum payable for loss of stock:

Agreed Loss	£ 50,000.00
Sum Insured on Stock	£100,000.00
Value at Risk	£100,000.00
Salvage Value	NIL
Excess	£ 1,000.00

(6 Marks)



c) Using the same figures as detailed in b) above explain if any different considerations would apply if the Insured had arranged additional cover for stock with separate Insurers. The Sum Insured on the said policy is £25,000.00.

(6 Marks)

d) In dealing with a business interruption claim with cover arranged on a declaration basis, calculate the amount payable:

Agreed Loss of Gross Profit	£150,000.00
Sum Insured	£200,000.00 (declaration linked)
Insurable amount	£250,000.00
Accountant's fees for certifying turnover at Insurers' request	£ 1,000.00
Loss Assessor's fees	£ 3,500.00

(6 Marks)

40 MARKS



QUESTION 3

1. a) Define warranty in relation to an Insurance Policy. *(4 Marks)*
b) List six warranties which might typically apply in a Commercial Policy. *(6 Marks)*

2. Discuss briefly the effect of breach of warranty when dealing with a claim under a domestic policy. *(6 Marks)*

3. Explain briefly the relevance of the following legislation and how it might apply to the adjustment of a claim:
 - Third Parties (Rights Against Insurers) Act (1930)
 - Water Industry Act (1991)
 - Rehabilitation of Offenders Act (1974)
 - Hotel Proprietors Act (1956)*(16 Marks)*

4. Explain briefly how you would deal with any salvage realisation in the following cases:
 - Fire damage which has occurred to stock at a retail pharmacy
 - Flood damage which has occurred to the contents of a private dwelling*(8 Marks)*

40 MARKS



ANSWER 2 QUESTIONS ONLY

QUESTION BI 1

You are requested by insurers to handle the business interruption claim for a prestigious city centre restaurant. The restaurant had only recently opened and was subject to considerable media interest. As well as having a bar and restaurant area, there is a separate area for corporate events such as meetings and conferences which in turn generate bar and restaurant sales.

Turnover generated in the main bar and restaurant area are recorded as 'Bar and Restaurant sales'. All turnover from the corporate events business is recorded as 'Corporate Events'. For the purpose of this exercise, the Rate of Gross Profit is consistent across the business.

The fire started 28 February in the kitchen effectively destroying all of the equipment contained therein and there was smoke and extinguishment water damage to the bar and dining areas. There was no structural damage to the building, but the electrical installation needed replacing and cleaning and redecoration to the interior of the building was required.

The restaurant remained closed for four months for repairs and replacement of contents and equipment.

The directors of the restaurant consider their budgets to be accurately based on their previous experience of operating restaurants and the high profile launch and media interest.

Some additional expenditure was claimed for promoting the re-opening of the business (£5,000) and for directors travelling to the premises totalling £4,000.

Some casual staff were laid off with savings totalling £13,000. Rent savings totalling £10,000 were also secured.



Policy cover is as follows:

Gross Profit Sum Insured: £900,000

Maximum Indemnity Period: 12 months

The Rate of Gross Profit has been evidenced as being 63%.

Bar & restaurant			Corporate events		
	Budget	Actual		Budget	Actual
Jan	£95,000	£13,849	Jan	£35,000	£ 7,109
Feb	£91,000	£35,000	Feb	£50,000	£24,123
Mar	£95,000	£ 0	Mar	£50,000	£ 0
Apr	£91,000	£ 0	Apr	£50,000	£ 0
May	£91,000	£ 0	May	£50,000	£ 0
Jun	£95,000	£ 0	Jun	£75,000	£ 0
Jul	£95,000	£20,690	Jul	£75,000	£15,875
Aug	£95,000	£23,358	Aug	£60,000	£ 1,619
Sep	£91,000	£19,151	Sep	£50,000	£ 6,735
Oct	£91,000	£18,793	Oct	£50,000	£ 6,835
Nov	£91,000	£24,751	Nov	£50,000	£15,500
Dec	£91,000	£30,000	Dec	£125,000	£30,491
Total	£1,112,000	£185,592	Total	£720,000	£108,287

Based on this information and the data below you are requested by insurers to:

1. Calculate a settlement figure detailing your assumptions as appropriate.
2. Discuss the problems you think you would encounter in trying to achieve a settlement and state how these issues could be addressed.
3. Calculate an appropriate Gross Profit Sum Insured for a 12 month period utilising the budget data above detailing any other assumptions you have made.
4. Explain the difference between:
 - (a) A Gross Profit Sum Insured Basis and a Declaration Linked Basis policy.
 - (b) A Contract Price Clause and an Accumulated Stocks Clause.

40 MARKS



QUESTION BI 2

Insurers have appointed you to deal with the business interruption aspect of a loss following a flood at a manufacturing business. The flood waters have affected the building, machinery & plant and stock.

The Insured attempted to mitigate the loss through subcontracting their operation to competitors with varying degrees of success. Subcontracting is not a normal feature of the business.

The following information has been presented showing historic turnover and turnover achieved following the flood. Turnover achieved in the year 06/07 totalled £1,250,000.

	Turnover achieved	Turnover achieved
	2007/8	2008/9
May	£121,000	£36,350
June	£129,000	£46,868
July	£137,000	£67,901
August	£113,000	£70,300
September	£100,000	£37,890
October	£150,000	£10,000
November	£125,000	£35,531
December	£105,000	£42,750
January	£135,000	£47,500
February	£125,000	£30,695
March	£115,000	£47,900
April	£145,000	£33,000
TOTAL	£1,500,000	£506,685



Increased expenditure was claimed as follows:

Subcontract costs net of own costs	£366,333
Hire of miscellaneous equipment	£21,324
Temporary office accommodation	£8,188
Couriers	£3,616
Telephones	£1,232
Temporary electricians	£1,000
Assessors fees	£15,000
Fork lift truck hire x 4	£12,000
Capital amount of short term loan	£50,000
Interest on short term loan	£5,000
Overtime	£48,000
TOTAL	£531,693

Savings in overheads were scheduled and agreed as follows:

Power	£25,000
Repairs & maintenance	£20,000
Transport	£43,734
Temporary staff	£10,855
TOTAL	£99,589

An extract from the most recent set of accounts shows the following:

Sales	£1,500,000
Purchases	£ 525,000
Gross Profit	£ 975,000

The policy is declaration linked with an Estimated Gross Profit of £700,000 and a Maximum Indemnity Period of 12 months. Uninsured Working Expenses are listed simply as Purchases.

1. Calculate settlement of the loss given the information above.
2. What factors should be taken into account when considering whether a cost ranks for inclusion as an increased cost of working?
3. How do Additional Increased Costs of Working differ from Increased Costs of Working?
4. In considering a claim for Increased Costs of Working for overtime, what would you take into account in trying to calculate the increased cost?



5. What do you understand by the terms 'Indemnity Period' and 'Maximum Indemnity Period'? **40 MARKS**

QUESTION BI 3

You have been appointed by insurers to adjust a business interruption claim for a commercial laundry following a serious fire at their premises. The company has activated its business continuity plan and has been able to find other laundries willing to work on a subcontract basis for the insured. The loss occurred 1 January 2009. Severe damage was caused to building, machinery & plant and stock.

By virtue of the subcontracting, impressive turnover levels were achieved in the eight months following the fire totalling £450,000, but at the cost of significant sums expended as Increased Costs of Working. The remaining turnover was generated via prompt replacement of some machinery and overtime working.

Detailed below are the most recent set of accounts for the business and an historic analysis of turnover achieved:

	2005 £	2006 £	2007 £	2008 £	2009 £
January	15,350	26,040	39,562	69,256	48,445
February	14,999	28,896	47,274	65,907	69,835
March	21,650	30,078	61,619	77,883	86,674
April	25,653	30,327	64,781	78,760	71,760
May	30,567	37,851	66,215	78,765	75,929
June	30,239	39,168	68,491	79,753	86,990
July	30,161	39,396	73,172	99,520	82,153
August	33,394	38,446	64,330	83,868	82,039
September	31,957	40,487	66,341	89,220	88,300
October	32,059	41,591	71,221	81,292	71,221
November	27,825	40,010	74,025	73,486	74,025
December	29,488	40,748	85,665	85,921	85,665
	£323,342	£433,038	£782,696	£963,631	£923,036

Sales		£	963,631	£
Opening stock		29,400		
Linen purchases		122,845		
Detergent purchases		27,500		
Closing stock		-35,200		
Cost of Sales				144,545



Gross Profit		<u>819,086</u>
Wages	253,767	
Carriage	57,817	
Rent	36,000	
Rates	12,000	
Insurance	12,500	
Lease costs	40,000	
Electricity	96,000	
Heat and light	27,998	
Repairs to machinery	36,750	
Repairs to building	4,532	
Motor expenses	7,630	
Telephones	2,653	
Printing, postage and stationery	6,530	
Bank charges	2,550	
Invoice discounting charges	19,272	
Directors remuneration	40,000	
Depreciation	40,000	
Overheads		<u>695,999</u>
Net Profit		<u>123,087</u>

Additional expenditure was claimed as follows:

Subcontracting	415,640
Temporary premises rent	45,000
Temporary premises rates	10,000
Utility costs at temporary premises	25,000
Vehicle hire	10,000
Overtime	16,532
Agency staff	14,977
Assessors fees	96,732
Directors bonus	50,000
Total	683,881

Policy cover is Estimated Gross Profit £650,000. The Maximum Indemnity Period is 12 months. The Uninsured Working Expenses are defined as Purchases (accounting for stock movement) and Carriage.

Based on the above information calculate:

1. The Rate of Gross Profit.
2. A proposal for settlement of the Gross Profit loss.



3. A proposal for settlement of the Increased Cost of Working claim with an explanation of the reasons for their inclusion or exclusion.
4. A proposal for what categories of cost could constitute savings and your explanations as to the reasoning behind their inclusion as a savings item.
5. Had the insured consulted you in October 2008, what figure would you have recommended that the insured declare as their Estimated Gross Profit for the twelve months to 31 December 2009?
6. (a) A contract that had been awarded and signed the day before the fire was postponed until August allegedly due to the incident.

(b) In addition, the insured submitted a claim for a contract they had tendered for (due to commence in June 2009) and were confident of winning, but which was awarded to a competitor.

What enquiries would you undertake to establish whether they should be included within the adjustment?

40 MARKS