

## CILA Business Interruption SIG Wording Review

Subject	Current position	What is the problem?	What are the consequences?	Potential solutions
<b>GROSS PROFIT</b>				
<b>Definition of Gross Profit</b>	Policies have a specific definition of Gross Profit	This term is already in everyday use in business, but is not clearly defined	Confusion results. Inadvertent under-insurance arises if the definition of Gross Profit used by a business is different from the measurement defined in the policy	Consider changing the term “Gross Profit” in policies in favour of – “Insurance Gross Profit”, or “Insurable Profit”
<b>Uninsured standing charges clause</b>	Most, but not all, policies have such a clause	<ul style="list-style-type: none"> <li>Archaic language</li> <li>Lack of a definition</li> <li>Difficulty in establishing what is a fixed cost and what is not</li> <li>Basis for measuring what is fixed and what is not unspecified</li> </ul>	Application of the clause is usually problematic and subjective	Consider alternative terminology; for example, fixed costs
<b>Material Damage Proviso</b>	<ul style="list-style-type: none"> <li>Most policies have a “Proviso”</li> <li>Original intention was to ensure that MD funds would be available to mitigate the BI loss</li> </ul>	<ul style="list-style-type: none"> <li>No requirement for the MD insurance to be adequate</li> <li>Degree to which the Proviso applies to BI extensions can be unclear</li> </ul>	<ul style="list-style-type: none"> <li>Original intention of the “Proviso” can be under-mined if severe inadequacy prevents effective BI mitigation</li> <li>Cover away from the Premises may be wider than intended</li> </ul>	<ul style="list-style-type: none"> <li>Dispense with the Proviso and exclude exacerbation of BI loss through lack of funds (as a result of MD being under-insured)</li> <li>Consider relating cover away from the Premises to that at the Premises more explicitly</li> </ul>
<b>Material Damage/BI overlap</b>	<ul style="list-style-type: none"> <li>Frequently, both MD and BI policies (or sections) provide cover for the same costs</li> <li>This can specifically arise in valuing stock claims or in the use of the insured’s own labour in the business recovery process</li> </ul>	<ul style="list-style-type: none"> <li>Policyholders can potentially benefit because elements of these costs are covered by both policies</li> </ul>	<ul style="list-style-type: none"> <li>The wording does not provide a facility for adjusting claims where overlap/double indemnity occurs</li> </ul>	<ul style="list-style-type: none"> <li>Wording could be amended to exclude costs already admitted under the MD section or policy</li> </ul>
<b>Rent Receivable</b>	Routinely insured by landlords or businesses who sub-let	<ul style="list-style-type: none"> <li>Description of business in policies is not always extended to include acting as a landlord</li> <li>Misunderstandings arise as to scope of insurable interest</li> <li>Rent cover may cease at point when repairs are complete</li> <li>Need for rent cover may be entirely overlooked</li> <li>Rent may not be defined</li> </ul>	<ul style="list-style-type: none"> <li>Rent may not be insured, be overlooked or under-insured, owing to the definition of the business being too narrow</li> <li>Cover may not extend to the point at which a new tenant is secured, (potentially ending when the Premises are occupiable again)</li> </ul>	<ul style="list-style-type: none"> <li>Include rent cover within GP (subject to the MIP being long enough) for sub-letters</li> <li>Ensure definition of rent includes service charges etc</li> </ul>

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<b>Rent Payable</b>	<p>Operating cost usually insured as part of Gross Profit/Revenue, but sometimes uninsured</p>	<ul style="list-style-type: none"> <li>• If insured as part of MD section, it will be payable again once re-occupancy is possible</li> <li>• Rent will be insured by both landlord and tenant (may be desirable)</li> </ul>	<ul style="list-style-type: none"> <li>• Indemnity periods that are insufficient are commonplace</li> <li>• If uninsured as a cost, it may not reduce in line with turnover</li> </ul>	<p>Best practice may be to include rent payable within the GP cover</p>
<b>Declaration linked policies</b>	<ul style="list-style-type: none"> <li>• Preferable to sum insured policies, no proportionate reduction</li> <li>• Declarations not always requested or submitted</li> </ul>	<ul style="list-style-type: none"> <li>• Insurers may not receive appropriate level of premium</li> <li>• Significant under-declaration potentially will result in policy avoidance</li> </ul>	<ul style="list-style-type: none"> <li>• Potential avoidance risk for the insured</li> <li>• Common fund is under-resourced</li> <li>• Adequately declared policyholders are subsidising those that are not</li> </ul>	<p>Consider setting a limit on the level of under-insurance and re-introduce average when this level is exceeded</p>

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<b>DAMAGE</b>				
<b>Definition of Damage</b>	Damage is imprecisely defined (e.g., as damage or loss); it is also used both as a defined term and an undefined term in the same policy	<ul style="list-style-type: none"> <li>Confusion over the scope of cover available can arise from the incorporation of defined and undefined uses of the term, damage</li> <li>Market practice and the legal definition can vary</li> </ul>	<ul style="list-style-type: none"> <li>Impairment of use (this is often temporary) is a significant modern issue, examples are flooding and peaceful protests</li> <li>Impairment of use may not be considered as Damage by the courts</li> </ul>	<ul style="list-style-type: none"> <li>A more precise definition of Damage would be helpful</li> <li>Such a definition to be used consistently in the extensions to cover</li> <li>Explicit inclusion or exclusion of temporary impairment of use would help to clarify cover</li> </ul>
<b>Wide Area Damage (WAD)</b>	Policies cover damage at the premises. WAD is not covered either at law (e.g., Orient Express Hotels) or in practice (CILA 2007 flood note)	Policyholders are frequently disappointed if there is a WAD deduction, albeit insurers need to be able to scope BI cover and risk to effectively assess premium	<ul style="list-style-type: none"> <li>Exclusion of WAD can produce anomalies (e.g., the impact of WAD being so great as to exclude the loss flowing from damage at the premises)</li> <li>The intention of insurance cover may be undermined</li> </ul>	<ul style="list-style-type: none"> <li>If the implication of significant losses at the premises being excluded by WAD is undesirable, it might be more appropriate to exclude “exacerbation of loss”</li> <li>Alternatively, the wording could explicitly state that WAD BI losses are excluded</li> </ul>
<b>Premises</b>	Premises is invariably not defined in the policy or the list in the schedule is referred to	<ul style="list-style-type: none"> <li>It is unclear whether Premises means Buildings of the demised site (for the whole or part of an address, in the case of shopping centres or multi tenanted office blocks)</li> <li>Is a website part of the Premises?</li> </ul>	<ul style="list-style-type: none"> <li>Uncertainty can arise as to whether warranties have been complied with</li> <li>Cover relating to extensions can be unclear</li> </ul>	Clearer definition of the Premises would assist; for example, the wording could specify whether Premises is restricted (or not) to that part of the building in tenants sole occupation
<b>Suppliers and customers</b>	Most policies have limited cover, often for unspecified customers & suppliers; on package policies there is often a limit of 10% of Sum Insured	The definition of a customer or supplier can be imprecise	<ul style="list-style-type: none"> <li>There can be confusion as to whether the cover applies only to the business with whom the insured transacts or if it extends to the whole supply chain</li> <li>It can be difficult to identify the Supplier in the former instance e.g., if product is delivered by an outsourced manufacturer but billed directly</li> </ul>	<ul style="list-style-type: none"> <li>A better definition as to whether the supply chain generally is covered would be desirable</li> <li>Additionally, the Supplier definition could deal with web hosts, ISP’s and data warehouses</li> </ul>

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<b>INCREASED COSTS</b>				
<b>Expenditure beyond Maximum Indemnity Period (MIP)</b>	<ul style="list-style-type: none"> <li>Cover is provided for loss over a defined period</li> <li>The policy wording requires that the Gross Profit loss being mitigated be within the MIP rather than the costs to be incurred falling within the MIP</li> </ul>	<ul style="list-style-type: none"> <li>Some costs to mitigate BI loss are paid after the MIP has ended</li> <li>Increased costs do not necessarily fall outside the scope of cover because of that</li> <li>Apportionment of the benefit of the costs incurred between insured GP and uninsured GP (either after the MIP or in a time excluded period) can be problematic</li> </ul>	An inconsistency in approach can arise because the policy wording is not explicit	The ICW definition could be clarified to make it clearer that the timing of GP losses is the relevant issue (i.e., are they within the MIP or not); rather than the timing of ICW payments
<b>Outsourcing and Blundell Spence</b>	Outsourcing and globalisation has given rise to many administrative only locations and suppliers	<ul style="list-style-type: none"> <li>Increased costs relating to admin-only sites can be difficult to justify economically</li> <li>The Blundell Spence agreement historically dealt with this but it is not part of the policy wording</li> </ul>	Inconsistency can arise; the reliance on a historic agreement (of which the insured will be unaware) is unsatisfactory	Consider including an explicit clause encompassing the Blundell Spence agreement; this could be subject to a limit (as with Suppliers/Customers extensions)
<b>Fines and Penalties</b>	Contractual fines and penalties will not meet the definition of an ICW; as such costs must be 'solely' to avoid a GP loss	<ul style="list-style-type: none"> <li>Non-contractual payments to retain a customer may be covered</li> <li>There can be the perception that fines and penalties are covered as part of AICW item, albeit there would be no apparent need for fines and penalties cover if this were the case</li> </ul>	<ul style="list-style-type: none"> <li>The distinction between contractual/non-contractual payments may be seen as semantic</li> <li>Expectation issues can arise</li> <li>Insurers may not receive the appropriate premium if there is an intention to cover fines and penalties as part of a general AICW item</li> </ul>	Consider explicitly stating that ICW cover does not include fines and penalties, but allow a buyback with a limit

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<b>PROCEDURAL</b>				
<b>Declaration Linked Policies - Fundamentals</b>	Declarations are required at the start and end of the MIP, but these are not routinely provided or requested	<ul style="list-style-type: none"> <li>It can be unclear who has responsibility for ensuring the declaration is made</li> <li>The basis period for the declaration can be unclear (12 months pre policy period, period most co-terminous with it, etc)</li> </ul>	<ul style="list-style-type: none"> <li>Declarations are made that often are too low</li> <li>Insufficient premium is being received by insurers</li> <li>Common fund is under-resourced</li> </ul>	<ul style="list-style-type: none"> <li>Require all Declarations to be the equivalent annual GP (insurers to then adjust to the length of the MIP)</li> <li>Consider using a more explicit wording that clearly defines where onus rests for making/requesting the declaration</li> </ul>
<b>Declaration Linked Policies – Two Declarations</b>	Declarations are required at the start and end of the MIP	Often, end of period declarations are not provided.	Insufficient premium may be paid	<ul style="list-style-type: none"> <li>Alternative mechanisms could be considered to ensure end of period declarations are received</li> <li>The end of period declaration could be dispensed with and pricing models could be altered to reflect this</li> </ul>
<b>Declaration Linked Policies – Base Periods</b>	Different policies use different basis periods for declarations (some retrospective, some looking forward)	Confusion arises, especially if there is a change of insurer	Any confusion is likely to exacerbate the already significant under declaration issue	Clearer terminology that describes the basis period to be used and the basis of claim settlement might reduce this issue
<b>Declaration Linked Policies – Periods longer than 12 months</b>	For periods of more than 12 months the annual GP must be proportionately increased; for periods below 12 months, it is not reduced	Often the policyholder is confused / does not appreciate the need to increase the annual amount	Inadequate declarations may be (inadvertently) made	Consider requiring a 12 month declaration, with insurers adjusting them in line with the length of the MIP
<b>Increased Costs</b>	<ul style="list-style-type: none"> <li>Cover generally has an economic limit applying to it</li> <li>Insurers are not required to confirm cover at the decision point</li> <li>Policyholders are not required to tell insurers that ICW are being incurred</li> </ul>	<ul style="list-style-type: none"> <li>Costs can exceed expectation leading to ICW exceeding the economic limit</li> <li>Significant ICW may be brought to the insurers/adjusters' attention late in the claim process, producing delay and complication</li> </ul>	<ul style="list-style-type: none"> <li>Surprises can be received by either the policyholder or the insurer</li> <li>Retrospective application of the economic limit can be seen as inequitable</li> </ul>	Consider removing the facility for a retrospective application of the economic limit in return for a supported business case at the decision point

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<b>Payments on Account</b>	Most policies do not explicitly confirm an entitlement to payments on account; the BI policy insures GP not cashflow	Whilst the current absence of such a clause is testament to the pragmatism of the UK industry, it also appears anachronistic	Under-funding post incident hinders loss mitigation	Consider a clause confirming POA entitlement, that requires a cashflow projection/business justification
<b>Claims Condition – Notification of claim</b>	Currently, BI claims must be submitted no later than 30 days after the end of the IP. (Potential) incidents must be notified as soon as they are known.	Notification procedures can be inadvertently overlooked	<ul style="list-style-type: none"> <li>• Some claims may not be paid</li> <li>• Insurers may not have an acceptable quantification of an exposure until many months after the initial notification</li> </ul>	<ul style="list-style-type: none"> <li>• Consider requiring notification within a reasonable time rather than immediately</li> <li>• Require quantification by the insured (as noted above under POA), but regardless of payment requests</li> </ul>
<b>Claims Condition – Information Disclosure</b>	Insurers are only entitled to documentation/quantification as above or when a payment on account is requested	As part of an inter-active process, a right for insurers to have documented updates would seem to be reasonable	Significant reserve increases can arise when withheld documentation shows higher levels of loss than intimated	Consider a clause entitling insurers to the timely production of reasonably requested information and documentation

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<b>SUNDRY</b>				
<b>Auditors and Accountants Charges</b>	Most policies cover costs incurred by auditors/accountants providing information that is requested in writing by insurers	<ul style="list-style-type: none"> <li>Confusion arises as to what is a claims cost and what may be covered by such a clause</li> <li>Many firms no longer have an audit, whereas the wording may anticipate otherwise</li> </ul>	<ul style="list-style-type: none"> <li>There may be a reluctance to mine for data if the cost is not covered, causing delay</li> <li>Expectation issues could arise in these circumstances</li> </ul>	<ul style="list-style-type: none"> <li>The accountants fees clause could more explicitly exclude costs of claim calculation/presentation</li> <li>If claims presentation costs are included as part of a separate clause, it may be advisable to define acceptable rates in advance of a claim</li> </ul>
<b>Time Deductibles</b>	Typical of Engineering BI covers, these often span 24 or 48 hours	It can be unclear if these are chronological, (from the point of the loss) or represent the stated number of hours in which loss accrues	<ul style="list-style-type: none"> <li>Inconsistency can arise</li> <li>Confusion arises over the treatment of ICW (incurred in an excluded period to avoid GP loss in the insured period &amp; vice versa)</li> </ul>	<ul style="list-style-type: none"> <li>Clarity as to whether the time excess is chronological from the point of damage (or not) would assist</li> <li>Clearer definition as to the timing of the GP loss is key rather than the timing of the ICW</li> </ul>
<b>Definition of Maximum Indemnity Period (MIP)</b>	Currently defined as the period during which the results are affected	Policyholders assume it is the period during which results are depressed	Consideration of "clawback" can be a surprise and expectation issues arise as a result	Consider emphasising that <u>improved</u> as well as <u>depressed</u> performance will dictate the length of the IP
<b>Depreciation Savings</b>	Policies allow for savings paid or payable to be deducted from settlements	Whether depreciation is paid or payable has been debated for years without consensus being reached	There is no consistency of approach on this issue; the insured cannot predict how depreciation will be handled	Notwithstanding the Synergy Healthcare case (which is being appealed), it seems appropriate that the Savings Clause explicitly include or exclude depreciation
<b>Alteration Condition</b>	Most policies allow for termination of cover if a business enters administration/receivership etc	<ul style="list-style-type: none"> <li>Confusion arises as to whether this is a condition precedent</li> <li>The terminology in these clauses does not always reflect the modern business options re insolvency</li> </ul>	<ul style="list-style-type: none"> <li>Surprises may be experienced by insurers or policyholders in individual cases</li> <li>In extreme cases, policies may be regarded as voidable meaning no recovery will be achieved post incident</li> </ul>	<ul style="list-style-type: none"> <li>It could be underlined that this is a condition precedent and does not apply to situations that arise post incident</li> <li>Some clauses need to be updated to reflect modern business options</li> </ul>