The Next Level of Business Income Coverage

A critical provision of most business income and extra expense forms is that, for coverage to apply, the proximate cause of income loss must be due to direct damage at scheduled premises.

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While this concept may seem intuitive, consider the following example for which coverage would be expected.

Claims Scenario

A large office building suffers damage during a late summer hurricane. Although the damage to the building is minimal, the tenants cannot occupy the building following the loss. The building takes 30 days to restore, during which time the owner suffers a loss of rental income. The area surrounding the building also suffers significant damage, and local authorities prohibit access to the building (and the surrounding area) for 60 days following the storm. The building owner submits a claim to recover the lost rental income lost for all 60 days.

After evaluating the claim, the insurer states that, because damage to the surrounding area is not an "insured premises," there would not be coverage for this lost income under the policy, presumably for days 31 through 60. Somewhat discouraged, the owner is nonetheless hopeful that at least the loss of income from the first 30 days when his building was under repair would be paid.

However, the insurer goes on to assert that, regardless of the damage to the building, tenants would still not have had access to the building, and the income loss would have been the same whether the building was damaged or not. The insurer further explains that a property policy is designed to make the insured whole (citing the principle of indemnity). By paying for *any* of the lost income, the building owner would be better off because the damage to the surrounding area would still exist even if the damage to the building had never occurred. The insurer then denies the entire business income claim.

While policy provisions may dictate whether the insurer can make such an assertion, it is nonetheless a conceivable scenario. So, what can be done to ensure that the building owner has sufficient coverage if such a loss occurs?

Civil Authority Introduction

When civil authority coverage is included within business income/extra expense insurance forms, income losses arising as a direct result from actions of local police, fire, etc., may be covered. Orders made by civil authority *must* be the cause of the lack of access to insured premises (or the reason that normal operations cannot continue) due to damage caused by a peril covered under your policy. There must be an act of civil authority for coverage to apply; blocked access to a location alone is insufficient to trigger coverage. (See section on ingress/egress below.)

The initial solution to the claims scenario above may now appear obvious. Civil authority coverage (or endorsement) is provided under most insurer business income and extra expense cover forms, and the insured would be properly covered. However, the terms of civil authority coverage may be too restrictive to grant an acceptable amount of coverage for all policyholders. Four limiting provisions under standard Insurance Services Office, Inc. (ISO), civil authority coverage should be completely understood and potentially amended for your specific situation.

1. The proximity requirement stipulating that the civil authority actions must occur within one mile of the "insured premises"
2. The maximum period that can be collected is limited to 30 days (after a 3–day deductible).
3. Courts have held that access to the premises must be completely prohibited and not just impaired/limited in order for coverage to apply.
4. There must be damage to property by a covered peril.

Potential Enhancements

Not every business owner has a compelling need to expand beyond the standard coverage, but actions of civil authority can nonetheless have a dramatic impact on income following a catastrophic loss. If, after evaluating the potential for loss, there is a higher than normal civil authority exposure, adding ISO form CP 15 32 "Civil Authority Changes" (or similar) should be considered. This endorsement allows an insured to expand the mileage radius away from its premises for which civil authority action will trigger coverage and allows an increased period for which coverage will apply beyond the standard 30 days. Some insurers will also provide a strict dollar limit of civil authority coverage that is not subject to a specific time limit.

Another important consideration to the standard civil authority coverage is to amend language so that coverage will apply when access to the insured premises is simply "impaired" and not "denied" or "prohibited" by actions of civil authority. "Impaired" policy language considers the broader impact of a civil authority's action in the surrounding area and does not restrict coverage if access to the premises is impossible. Typically, this improved language is available on larger manuscript policies.

Finally, civil authority will only apply if it was caused by a loss that is otherwise covered under the property policy. Following the terrorist attacks of September 11, 2001, there were numerous examples of claims filed by businesses that were dependent on airports being operational. After the federal government suspended air travel for an extended period, many of these businesses filed business income claims due to the act of civil authority. However, these actions, while certainly the result of the threat of further terrorist attacks, did not follow a covered loss to the surrounding area (the airport). Therefore, these claims were denied. This condition emphasizes the need to not only ensure that catastrophic loss to windstorm, flood, and earthquake losses are covered but also that civil authority coverage is included when these perils are added to a standard form via endorsement. Sometimes insurers will specifically exclude civil authority coverage when adding certain catastrophic perils.

Ingress/Egress Coverage

Some insurer forms also separately provide protection for loss of income due to a lack of ingress and egress to/from insured premises. Like civil authority coverage, ingress/egress coverage is designed to pay for the loss of income triggered by physical loss or damage caused by a covered peril to third-party property that prevents or hinders ingress to or egress from the insured's business. However, an act of civil authority is not needed to trigger ingress/egress coverage. Any evaluation of the terms and conditions of civil authority coverage should be accompanied by a similar review of ingress/egress coverage as well.

Conclusion

When evaluating potential property and business income loss scenarios, it is important to consider situations in which an off-premises event causes direct financial harm to your business. Having proper coverage for civil authority and ingress/egress can help lessen the potential for portions of a property claim going uncovered.