

Seven costly insurance traps

While the vast majority of small businesses believe they have adequate insurance cover, many may be in for a rude shock at claims time.

While 17 in 20 small businesses believe they are adequately insured, many have gaping holes in their coverage. According to a recent Cameron Research report, these gaps range from no public liability insurance (7 per cent) to no cover for fire (13 per cent), burglary (20 per cent) or Directors & Officers (87 per cent).¹ What's more, only one in three small companies has business interruption insurance to bankroll their overheads in the aftermath of a fire or other serious insured event.¹

Tony Maher, Head of Regional Australia for Zurich, says the credit crunch has made it more important than ever for businesses to have appropriate insurance protection. "Any shortfall following a loss can impact business liquidity and personal cash flow, given many small business owners personally guarantee their company loans and leases," says Maher.

Here are seven common underinsurance traps business owners need to be mindful of.

1 Not seeking advice

Few business owners would dream of doing their own tax or presuming themselves to be experts on the finer points of contract law. So why risk a do-it-yourself insurance assessment?

Maher says seeking professional advice from an insurance broker provides peace of mind. "A broker will ensure your insurance program covers all bases both in terms of types and levels of cover," says Maher. "Subtle differences in insurance wordings can lead to very different outcomes in the event of a claim.

"For example, Zurich's business pack and ISR policies offer flood cover to the full limit of the sum insured. Whereas some insurers impose sub-limits for this peril, capping the amount they will pay in the event of a flood claim. Say the sub-limit is \$500,000, then that's the maximum they'll pay for a flood claim irrespective of the damage bill."

To find a licensed broker in your area, visit www.needabroker.com.au.

2 Inadequate sums insured

Zurich recently took a look at its Business Insurance data and discovered that just one in four policyholders had increased their sums insured on renewal that year.

"If your business suffers a partial property loss and the claims assessor determines that it was significantly underinsured, then the Underinsurance Clause can come into play and only a proportion of your claim will be paid," says Maher. "Say your property was insured for \$1 million and you lodge a claim for \$500,000 after a storm. And the assessor determines your property's value at policy inception was \$1.5 million - 50 per cent more than what you insured it for. The claim payout would be reduced to \$416,000."

3 She'll be right, mate

We'd all prefer to think disaster won't strike us. And while your business would be unlucky to suffer a major loss (e.g. burn down or be sued by someone who injured themselves on your premises), ignore these risks at your own peril.

Insurance is based upon the principle of pooling risk (i.e. the premiums of many policyholders paying for the claims of the few). And the Australian insurance industry paid out \$18.2 billion in claims last year.²

Maher says that insurance is good value when you consider the average small business pays about a \$2000 in tax-deductible premiums per annum to cover a myriad of risks that could otherwise cost them hundreds of thousands following a peril.

4 No business interruption cover

Your property insurance will pay the cost of rebuilding your premises and/or replacing your contents following a peril. But if there's no income coming in, will your business have enough cash flow to pay its loans, leases, wages etc. while you rebuild?

Business Interruption insurance protects your income and pays fixed expenses following a major loss. "Without Business Interruption insurance, I'd estimate only one in 10 companies will stage a full recovery after a major loss," says Maher.

5 Uninsurable contracts

Never sign a property lease or a contract to do work for a third party without first seeking legal advice and consulting your insurance broker. Many leases or contracts impose onerous liabilities upon you or your business that could put your assets at risk.

"In some cases, an insurance policy won't provide cover for all the indemnities or 'hold harmless' conditions that can be specified in a contract," says Maher.

6 No PI insurance

Most people are aware that professionals (e.g. doctors, accountants etc.) can be sued by a client for poor advice. But did you know that incorrect advice provided by other occupations can also result in legal action against the individual and their business?

At-risk occupations can include anyone from a motor mechanic to an IT consultant. If your business provides advice to clients, be sure to tell your insurance broker, who'll let you know if you need professional indemnity (PI) insurance to cover this risk.

7 Not disclosing material facts

Before entering into an insurance contract, you are required by law to advise the underwriter about any facts that may be considered relevant to their acceptance of your policy risk. This disclosure requirement applies on renewal also. If you do not comply, your insurer may cancel your policy and refuse to pay or only part-pay a claim.

Material events that have occurred during the period of insurance can range from a significant speeding charge for a motor policy to a new tenancy that changes a property's usage for fire insurance.

1 "The Australian Small Business Market for Financial Services: 2008: Insurance", Cameron Research Group 2008.

2 Quarterly General Insurance Performance December 2008, APRA.