



The Sri Lanka Insurance Brokers Association

Business Interruption Insurance

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Different Names



- ✚ Loss of Profits Insurance
- ✚ Consequential Loss Insurance
- ✚ Business Interruption Insurance
- ✚ Business Continuity Insurance
- ✚ Business Income Insurance

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Business Continuity Planning

- ✚ Business Continuity Management is defined as a **holistic management process** that identifies potential threats to an organization and building organizational resilience with the capability of an effective response that **safeguards the interests of its key stakeholders**, reputation, brand and value-creating activities. (Source: ISO 22301:2012)
- ✚ Planned activities intended to ensure that an organization's critical business functions will continue to operate even after a serious incident/disasters; if not, it might have an interruption or will end-up in bankruptcy
- ✚ The business continuity is part of **risk management** (risk identification, risk analysis, risk control and risk financing)
- ✚ It is often described as **common sense**. It is all about taking responsibility for your business to stay on course. It is about keeping calm and carrying on

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Benefits of Business Interruption Insurance

Business interruption insurance protects companies from **financial losses when operations are disrupted**, ensuring continuity by covering lost income, ongoing expenses, and recovery costs.

It acts as a **financial lifeline during crises** such as natural disasters, fires, or supply chain breakdowns.

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Key Benefits of BI Insurance

- 1. Income Protection**
 - ✓ Covers lost revenue during periods when the business cannot operate.
 - ✓ Helps maintain financial stability and prevents insolvency.
- 2. Coverage of Fixed Expenses**
 - ✓ Pays for ongoing costs such as rent, utilities, and loan repayments.
 - ✓ Ensures obligations are met even when income stops.
- 3. Employee Retention**
 - ✓ Provides funds to continue paying staff salaries, avoiding layoffs.
 - ✓ Helps retain skilled employees and maintain morale.
- 4. Support for Recovery Costs**
 - ✓ Covers temporary relocation expenses, equipment rentals, or outsourcing.
 - ✓ Helps businesses resume operations faster after a disruption.

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Key Benefits of BI Insurance

- 5. Protection Against Supply Chain Disruptions**
 - ✓ Extends to losses caused by supplier failures or damage to partner facilities.
 - ✓ Keeps production and delivery commitments intact.
- 6. Safeguard for Customer Relationships**
 - ✓ Ensures businesses can fulfill contracts and maintain trust.
 - ✓ Prevents reputational damage from prolonged downtime.
- 7. Business Continuity Assurance**
 - ✓ Provides a safety net that allows companies to focus on recovery rather than financial survival.
 - ✓ Strengthens resilience against unpredictable events.
- 8. Peace of Mind for Owners**
 - ✓ Reduces stress by ensuring that unforeseen events don't derail long-term plans.
 - ✓ Allows leadership to focus on strategy rather than crisis survival.

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Consequential losses

Property material damage policy would indemnify for Building, Plant, Machinery, Stocks etc. but **not** for the following

- Under insurance under the material damage
- Difference in value of property at the time of the loss and the reinstatement/replacement
- Deterioration of undamaged stocks
- Loss of records/information causing financial losses
- Fines, damages and penalties for non-performance of any contractual obligations
- Third party claims and obligations
- Cost of preparation of claims
- Litigation costs
- Losses due to work stoppage, attending to injured, police enquiries, investigations etc.
- Salaries and other fixed costs that continue to be paid
- Additional expenses incurred to achieve some turnover
- Loss of Net Profit

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Cover under Business Interruption Insurance

- Loss of **Gross Profit** due to a reduction in the turnover caused by a peril insured
- Increase in Cost of Working** for the sole purpose of reducing the loss in the turnover

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Gross Profit/Net profit (in accounting parlance)

The Gross Profit
This is calculated in the Trading Account and is the excess of sales over the cost of goods sold during the period.
(Sales less cost of making and selling goods)

The Net Profit
This is calculated in the Profit and Loss Account and is what remains after all other costs used up in the period have been deducted from the Gross Profit.
(Gross profit less other overheads)

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Gross Profit under a BI Policy

Turnover

- Gross Profit
- Specified Working Expenses
- Net Profit
- Standing Charges
- Variable Costs

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Business Expenses

FIXED EXPENSES <i>Charges that are fixed irrespective of the level of turnover</i>	VARIABLE EXPENSES <i>Charges that vary with the level of production or turnover</i>
<ul style="list-style-type: none"> Salaries/Wages Insurance costs Directors Fees Bank Loans instalments Interest and Finance/Lease instalments Rates and Rent Marketing & Advertising Royalties/Franchise Depreciation 	<ul style="list-style-type: none"> Purchases of Raw Materials Duty and Freight Packing Cost and Materials Repairs and Maintenance Wages on casual labour Commissions to Sales Transport and Traveling Overtime Telephone/Electricity?

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Calculation of Gross Profit

TRADING ACCOUNT XYZ Manufacturing PLC				PROFIT AND LOSS ACCOUNT XYZ Manufacturing PLC			
Dr.	Rs.'000	Cr.	Rs.'000	Dr.	Rs.'000	Cr.	Rs.'000
Opening Stocks as at 01.01.19	1,000	Sales	30,000	Rent and Rates	1,500	Gross Profit	15,500
Purchases	10,000	Closing Stocks as at 31.12.19	1,500	Salaries	1,500		
Wages	5,000			Director's Fees	2,000		
Gross Profit	15,500			Traveling Expenses	1,000		
	31,500		31,500	Advertising	500		
				Repairs and Maintenance	1,000		
				Net Profit	8,000		
					15,500		15,500

Accounting GP = Sales less Expenses
30,000 - less (10,000 + 5,000) = 15,000

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Calculation of Gross Profit Method 1

Gross Profit: ADDITIONS BASIS

The sum produced by adding to the Net Profit the amount of the Insured Standing Charges, or if there be no Net Profit the amount of the Insured Standing Charges less such a proportion of any net trading loss as the amount of the Insured Standing Charges bears to all the standing charges of the Business.

Net Profit (or Net Loss) + All the Fixed Costs

Standing charges

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Calculation of Gross Profit Method 1: Addition Basis

TRADING ACCOUNT				PROFIT AND LOSS ACCOUNT			
XYZ Manufacturing PLC				XYZ Manufacturing PLC			
Dr.	Rs.'000	Cr.	Rs.'000	Dr.	Rs.'000	Cr.	Rs.'000
Opening Stocks as at 01.01.19	1,000	Sales	30,000	Rent and Rates	1,500	Gross Profit	15,500
		Closing Stocks as at 31.12.19	1,500	Salaries	1,500		
Purchases	10,000			Director's Fees	2,000		
Wages	5,000			Traveling Expenses	1,000		
Gross Profit	15,500			Advertising	500		
	31,500		31,500	Repairs and Maintenance	1,000		
				Net Profit	8,000		
					15,500		15,500

Net Profit (or Net Loss) + All the Fixed Costs
 $8,000 + (1,000 + 500 + 1,000 + 2,000 + 1,500 + 1,500 + 5,000) = 20,500$

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Calculation of Gross Profit Method 2

Gross Profit: DIFFERENCE BASIS

The amount by which;

- the sum of the amount of the Turnover and the amounts of the closing stock and work in progress shall exceed
- the sum of the amounts of the opening stock and work in progress and the amount of the Uninsured Working Expenses.

(Turnover + Closing Stocks + Work in Progress) less (Opening Stocks + WIP + Variable Costs)

Uninsured working expenses

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Calculation of Gross Profit Method 2: Difference Basis

TRADING ACCOUNT				PROFIT AND LOSS ACCOUNT			
XYZ Manufacturing PLC				XYZ Manufacturing PLC			
Dr.	Rs.'000	Cr.	Rs.'000	Dr.	Rs.'000	Cr.	Rs.'000
Opening Stocks as at 01.01.19	1,000	Sales	30,000	Rent and Rates	1,500	Gross Profit	15,500
(+) Purchases	10,000	Closing Stocks as at 31.12.19	1,500	Salaries	1,500		
Wages	5,000			Director's Fees	2,000		
Gross Profit	15,500			Traveling Expenses	1,000		
	31,500		31,500	Advertising	500		
				Repairs and Maintenance	1,000		
				Net Profit	8,000		
					15,500		15,500

(Turnover + Closing Stocks + WIP) less (Opening Stocks + WIP + Variable Costs)
 $(30,000 + 1,500) - (10,000 + 1,000) = 20,500$

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Indemnity Period defined

The period beginning with the occurrence of the damage and ending not later than the maximum indemnity period thereafter during which the **results of the business shall be affected in consequence of the damage**

- Until the turnover returns to normal
- Up to the maximum indemnity period selected
- Period of Indemnity could be 3, 6, 12, 18, 24, 36, 48 or 60 months)

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Factors affecting the indemnity period

- Site Clearance
- Planning and approvals from local authorities
- Contract negotiations and actual rebuilding
- Extended replacement time for foreign made plant & machinery
- Availability of raw materials and components
- Replacement and training of staff
- Nature of business
- Nature of damage
- Ability to attract customers
- Nature of the suppliers
- Any other inherent factors

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Gross Profit Projection

Financial Year (Audited) : 01.04.2019 - 31.03.2020
Proposed insurance period : 31.03.2020 - 31.03.2021
Indemnity Period : 24 months
Projected Growth : 10% for the year 2020/21
15% per annum thereafter

Gross Profit for the audited Financial year : Rs. 500,000
for the insurance year (2020/21) +10% : Rs. 550,000
for indemnity period (+15%); year 1 : Rs. 632,500
for indemnity period (+15%); year 2 : Rs. 727,375
Sum Insured for 24 months indemnity : Rs. 1,359,875

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Gross Profit Projection

Financial Year (Audited): 1.4.19 - 31.3.20
 Gross Profit: Rs. 500,000/-
 Proposed insurance period: 31.3.20 - 31.3.21
 Indemnity Period: 24 months
 Projected Growth: 10% for the year 2020/21
 15% per annum thereafter

Gross Profit Rs. 500,000- **Gross Profit** Rs. 550,000- **Gross Profit** Rs. 632,500- **Gross Profit** Rs. 727,375-
 +10% growth in T/O +15% growth in T/O +15% growth in T/O

31/3/2020 31/3/2021 31/3/2022 31/3/2023
 Indemnity Period 24 months
 Loss of Gross Profit Rs. 1,182,500- (550,000 + 632,500)
 Indemnity Period 24 months
 Loss of Gross Profit Rs. 1,359,875- (632,500 + 727,375)

Incorrect GP Calculations
 500,000 x 2 = 1,000,000
 550,000 x 2 = 1,100,000
 632,500 x 2 = 1,265,000

Loss on the last day of insurance

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Preamble Clause

"..... Business be destroyed or damaged by and the business carried on **by the Insured at the premises** be in consequence thereof **interrupted or interfered** with, then the Company will pay to the insured in accordance with the provisions contained in the specification, provided at the time of happening of the damage there **shall be in force an insurance** covering the interest of the insured in the property at the premises against such damage and the **payment shall have been made or liability admitted** therefor under such insurance"

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Preamble Clause Simplified

- ✚ The premises should be damaged
- ✚ There must be a material damage policy
- ✚ Material damage policy must be liable for the loss
- ✚ Due to the damage, the business must be interrupted
- ✚ Both policies (MD and BI) must cover the loss/peril
- ✚ Both policies must be in force

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Definitions

Turnover: Money paid or payable to the insured for goods sold and delivered and services rendered in course of the business at the premises
Annual Turnover: The turnover during the 12 months immediately before the date of the damage
Standard Turnover: The Turnover during that period corresponding with the indemnity period in the **12 months immediately** before the date of the damage appropriately adjusted if the period of indemnity exceeds 12 months
Shortage in Turnover: The amount by which the Turnover during the indemnity period fall short of the Standard Turnover


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Definitions

Date of loss 1.1.25 30.9.25 Date of loss 1.1.26 Date of resumption 30.9.26
 Annual Turnover Period of Interruption
 Standard Turnover Turnover

Turnover: Money paid or payable to the insured for goods sold and delivered and services rendered in course of the business at the premises
Annual Turnover: The turnover during the 12 months immediately before the date of the damage
Shortage in Turnover: The amount by which the Turnover during the indemnity period fall short of the Standard Turnover (Standard TO – TO in interruption period)
Standard Turnover: The Turnover during that period corresponding with the indemnity period in the 12 months immediately before the date of the damage appropriately adjusted if the period of indemnity exceeds 12 months

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Policy Cover


Item No.1 : Gross Profit

- (a) in respect of reduction in turnover
- (b) in respect of increase in cost of working

Item No.2 : On Auditor's Charges

Limited to the reasonable charges payable for producing any particulars as may be required by the insurers in terms of the policy and not for preparing the claim

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Policy Cover *contd...*

Item No.1 : Gross Profit
(a) in respect of reduction in turnover


The sum produced by applying the RATE OF GROSS PROFIT (%) to the Shortage in Turnover

$$\text{Rate of Gross Profit} = \frac{\text{Gross Profit}}{\text{Turnover}} \times 100$$

During the Financial Year immediately before the date of the damage

The amount by which the Turnover during the indemnity period fall short of the Standard Turnover

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Policy Cover *contd...*

Item No.1 : Gross Profit
(b) in respect of increase in cost of working

- The additional expenditure necessarily and reasonably incurred during the indemnity period for the sole purpose of avoiding or reducing the consequence of damage
- Limited by applying the RoGP to the amount of the turnover achieved during the period
- Less any sum saved during the Indemnity Period

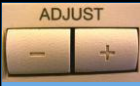
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Examples of Increase in Cost of Working

- Purchasing raw materials from different source at a higher price (Supplier's Extension)
- Processing raw materials or WIP in another factory
- Leasing-out a factory to complete the orders or to retain customers/shelf space
- Leasing/hiring emergency equipment/machinery
- Renting out an additional store/warehouse/facility
- Allocating guests to another hotel or patients to another hospital
- Alternate accommodation

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Adjustment

... to which adjustments shall be made as may be necessary to provide for the trend in the business and for variations in or special circumstances affecting the business either before or after the damage or which would have affected the business had the damage not occurred, so that figures thus adjusted shall represent as nearly as may be reasonably practicable the results that would have been obtained during the relative period after the damage.

Examples:

- Change of life styles and habits, customs, times, lobby groups, seasonal
- Change of laws, taxation, political and social situation
- Trade and economic agreements

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Condition of Average (Underinsurance)

Sum Insured (Gross Profit) < Sum produced by applying the RoGP to the Annual Turnover (or proportionately increased if the indemnity period is more than 12 months)

$$\frac{\text{Sum Insured}}{\text{RoGP} \times \text{Annual Turnover}} \times \text{Loss}$$

The turnover during the 12 months immediately before the date of the damage

Loss of Gross Profit plus Increase in Cost of Working less Savings

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Additional Clauses

- ✓ **Alternative Trading Clause:** Goods sold or services rendered elsewhere for the benefit of the insured ... the money paid or payable in respect of such sales/services shall be brought into account in arriving at the turnover during the indemnity period
- ✓ **Return of Premium Clause:** If the Gross profit earned during the accounting period most nearly concurrent with any period of insurance being less than the sum insured, a pro rata return of premium not exceeding% of the premium paid
- ✓ **Uninsured Standing Charges (applicable for Addition Basis):** If any standing charges are not insured, then in computing the amount recoverable under increase in Cost of Working only such proportion of the additional expenditure shall be brought into account

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Additional Clauses *contd...*

Departmental Clause: if business has separate sections or departments each earning different rate of gross profit. Separate RoGP is taken for the calculation of the loss, provided it has been declared to the insurers prior to the policy.

Method 1: if separate GP can be allocated to each dept.

GP on Dress Department : Rs.
 GP on Stationery Department : Rs.
 GP on Footwear Department : Rs. So on and so forth

Method 2: if its not practical to allocate separate sums to each department, then independent trading results of each department is considered and RoGP is applied

New Business Clause: as there would not be readily available data, the RoGP would be the GP earned on the turnover from the commencement of the business up to the date of the loss

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Payroll Cover

- ✓ Payroll refers to remuneration (salaries and wages) paid to employees.
- ✓ If the employer intends to retain all or most of the staff throughout the period of interruption, payroll should be included in full as part of GP
- ✓ **Dual Basis:** if high proportion of employees would be declared redundant, either the whole payroll or wages only should be excluded from the GP and insured separately.
- ✓ Under Dual Basis:
 - ✓ 100% cover for the initial period ofweeks following damage to cover insured's obligations
 - ✓ A % to apply during the remainder of the indemnity period to cover those employees who are to be retained throughout the interruption
- ✓ Two options,
 - 1) Remuneration saved during initial period can be carried forward to the remainder
 - 2) For short interruptions, the remainder can be converted to provide an increased number of weeks at 100% cover

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Working of a Claim

Month	Pre Fire Year T/O	T/O during Indemnity Period	Shortfall in T/O
Jan	70,000	10,000	60,000
Feb	80,000	20,000	60,000
Mar	60,000	30,000	30,000
Apr	90,000	60,000	30,000
May	80,000	70,000	10,000
Jun	90,000	80,000	10,000
Jul	100,000	90,000	10,000
Aug	110,000	95,000	15,000
Sep	100,000	95,000	5,000
Oct (p.y)	70,000	70,000	230,000
Nov (p.y)	80,000	80,000	
Dec (p.y)	70,000	70,000	
	1,000,000		

Assumptions:

- Fire damage in January
- Sum Insured: GP = Rs. 120,000-
- Rate of Gross Profit for the previous Financial Year : 15%
- Increase in cost of working 15,000 which achieved a 80,000 turnover
- Annual Turnover: Rs. 1,000,000-

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Working of a Claim *Contd...*

Reduction in the Turnover during interruption period: Rs. 230,000-

Rate of Gross Profit as per audited previous financial year: 15%

Loss of Gross Profit: Rs. 230,000- x 15% = Rs. 34,500- (a)

Increase in Cost of Working: Rs. 15,000-

Turnover achieved by the increased expenses: Rs. 80,000-

Reasonableness: Rs. 80,000- x 15% = 12,000- (b)

Amount Payable (a) + (b) = Rs. 46,500

Underinsurance:

Sum Insured on GP: Rs. 120,000-

Correct GP: Rate of GP x annual turnover: 15% x Rs. 1,000,000- = Rs. 150,000-

Application of underinsurance: Loss x sum insured → Rs. 46,500- x Rs. 120,000- / Correct GP Rs. 150,000-

Final Amount payable = Rs. 37,200-

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Exclusions



- Basic Fire or Material Damage Exclusions
- Deductibles (Time/Monetary/percentage) under Fire material damage and/or Business Interruption Policy
- Underinsurance in Material Damage Policy
- Underinsurance in Business Interruption Policy
- Uncovered Fixed Costs (Standing Charges)

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Extensions

- ⚡ All the additional Perils under the Fire Policy
- ⚡ Denial of Access/loss of attraction
- ⚡ Infectious Disease
- ⚡ Public Utilities (Electricity, Water and Gas)
- ⚡ Named Suppliers
- ⚡ Other/Un-named Suppliers (limited to, say, 5% of the T/O)
- ⚡ Specified sub-contractors
- ⚡ Named Customers (% of the Turnover for each selected customer)


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ELEMENTS of BI Policy

- 🌐 Retention of markets/clients/shelf space
- 🌐 Continuity of the business
- 🌐 Retention of important staff/key employees
- 🌐 Pays for fixed costs/standing charges
- 🌐 Loans and leases serviced during interruption
- 🌐 Contribution towards net profit
- 🌐 Safeguards stakeholders
- 🌐 As part of good corporate governance


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Types of BI Covers

- 🌐 **Legal Firms/Offices/Banks**
 - Alternate accommodation for logistics/airline offices
- 🌐 **Hotels/Hospitals**
 - Conventional BI with denial of access, loss of attraction
- 🌐 **Trading/Retail and Factories**
 - Conventional BI with specified suppliers/customers if any
- 🌐 **ICT Firms**
 - Alternate accommodation for offices, BI through Electronic insurance and Reinstatement of data
- 🌐 **Plantation/Estates**
 - Alternate accommodation for broking offices
 - Other trading/manufacturing/processing – conventional BI with specified suppliers/customers if there are such

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End of Presentation



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End of Presentation

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