
The Circle Of Safety:

**Keys to Understanding
Commercial Insurance**

RA Fraser Agency



Consumer Awareness Publications

3205 NE 78th Street, Suite 102

Vancouver, WA 98665

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Cover designed by Nancy Phillips, Formations Design.

10 9 8 7 6 5 4 3 2 1 pbk.

Published by Consumer Awareness Publications, 3205 NE 78th Street,
Suite 102, Vancouver, WA 98665.

Printed in the United States of America.

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FOREWORD

Our studies consistently show the unfortunate fact that the average consumer doesn't really understand their own insurance. Further, they're not really aware of the many different options they have for protection.

Perhaps the industry is to blame. We tend to talk in our language. Our policies are difficult to understand. And we don't spend enough time educating the consumer on this important area of their lives.

Consumers are often left with nagging doubts. Do they have enough protection? Are there gaps in their coverage? Are they paying too much? What are they really paying for? Will their claims get paid?

This book is revolutionary. The RA Fraser Agency has taken a complex subject, stripped it of the pretentiousness of our own industry – and given it back to the consumer – where it belongs.

On behalf of the Society and its mission, I congratulate the author on a magnificent accomplishment.

Michael Jans, CAE
Executive Vice President
The National Society of Agents for
Consumer Education

INTRODUCTION

It's risky to be in business these days. Business owners face fierce competition, random economic swings and strict government regulations. Besides that, unexpected disasters can hit a potentially successful business. Take these examples:

- Fire at a drycleaner. No insurance to pay for customer goods.
- A roof collapse at a toy store one month before Christmas. No insurance to re-open.
- Insurance on a fire-destroyed building. No insurance to cover pollution cleanup costs.

That's why *loss prevention* is a crucial part of insurance. Loss prevention means protecting your assets with practical safeguards. That could include:

- better door locks
- training employees on sexual harassment policies
- construction of a fire- and earthquake-proof building.

These and similar loss prevention activities can mean **reduced insurance premiums for you**. Establishing a close partnership with your insurance agent is the best way to ensure that you're fully protected .

Your agent can provide the **best and most customized protection for disaster coverage**. Know the insurance coverage options for your business. It takes time and premiums, but it's worth the **peace of mind**—even if you never file a claim.

COMMERCIAL PROPERTY INSURANCE

Chances are, your business has either a Commercial Package Policy or a Businessowners Policy. The Businessowners Policy, or BOP, is a package policy designed for businesses of a simpler nature. Let's look at what makes up package policies first.

Commercial Package Policies—The Inside Story

A *package* in insurance lingo combines types of insurance in one policy. It takes at least two coverage forms to make a package policy. A *coverage form* details your insurance protection. Individual coverage forms may have additional *conditions*, or coverage limits.

So for a business, a package policy could mean one of each of these coverages:

- property damage
- liability against lawsuits
- crime
- machinery.

Monoline (one line of coverage) insurance policies are not uncommon; of course package policy discounts don't apply to these. Today most businesses opt for the **premium savings** and **more complete coverage** of a package policy.

A **Commercial Package Policy** has a *policy jacket* that contains:

- general material common to all policies

- Declarations pages (often called “dec” pages)
- various, specific coverage forms.

Some coverage forms you might see depending on your business needs are:

- commercial property
- boiler and machinery
- commercial automobile
- general liability
- inland marine
- farm
- liquor liability
- pollution liability
- products/completed operations liability
- employment practices or employment-related practices liability.

Your agent's goal is to help you understand and accept the coverage essential for your operations.

Declarations

The Declarations pages personalize the insurance for you and your business. If any of the information on the Declarations pages is wrong, you may face disastrous consequences in the event of a loss. When you receive a new insurance policy or a renewal policy, your first priority is to review the new Declarations. Are all your business entities named correctly? Are the coverages and limits you

agreed to listed as expected? This review is not a big job, but it is an important one.

* **Tip.** Always review your Declarations pages.

Insuring Agreement

Simply, the insuring agreement limits coverage to direct loss to property.

Exclusions & Endorsements

Each coverage form in a package policy will have its own *exclusions* and perhaps one or more endorsements.

- Exclusions help set parameters on the coverage granted by the insuring agreements set out in the form.
- Exclusions are added to make a policy better fit certain insureds.
- Endorsements are additions to the policy.

You must take into account each part of the policy to understand the whole package. Just as it takes many parts to run the engine in a car, all the parts of an insurance policy must work together, too.

A Quick Review

- Package policies contain Declarations, Insuring Agreements, Exclusions, Endorsements, and Conditions. Each line of insurance has a separate form.
- The policy parts work in unison to provide coverage.

- Premiums are often discounted for package policies.

Beware, insurance terminology changes over time! Also, insurance companies add their own policy names. Why? It makes their product sound sexier. We'll stick with common terminology as much as possible.

Property Protection: Nuts & Bolts

Have you heard an agent talk about a *standard* insurance policy? That means a product of the Insurance Services Office (ISO). The ISO develops and revises the insurance policy forms most insurance companies use. Not every insurer uses ISO forms; some use modified ISO forms. Individual states may call for altered variations of ISO or special endorsement forms. Let your agent sift the industry offerings to find the coverage best for you. We'll stay with the standard ISO forms here.

Building & Personal Property Form: What It Means

The most commonly used form for property protection today is ISO's **Building and Personal Property Form** (CP 00 10).

. **Note.** It's usually combined with one or more *causes of loss* forms. These come in three flavors: **basic, broad, and special**. The first two are *named peril* forms—a grouping of perils such as fire, windstorm, and vandalism. The special is an *open peril* form—everything is covered *except* what is excluded.

* **Tip.** Look at your **entire** policy to determine your coverage.

The Building and Personal Property Form:

- Contains the Insuring Agreement. Indirect losses, like the interruption of your business, can be covered. You can imagine that an interruption of your business could be a greater loss than direct property damage (more on this later)!
- Distinguishes between buildings and business personal property. Logic is used here, not strict legal definitions. For example, building coverage can include permanently affixed items and equipment used for building maintenance. This may not seem important, but imagine you're a landlord. You'd want your snowblower or lawnmower covered in building limits.
- Calls attention to coverage for other people's property. If your business deals with the property of others—as do laundries, equipment repairs or storage—you'll want separate *bailee coverage*.

. **Note.** Some insureds will have only business personal property. Others will have only real estate. Others will have both. That's why the insurance policy has separate dollar limits of coverage. It's important to know how property is classified.

Property Not Covered

The Building and Property Form has a long list of property not covered. Is this a rip-off? No. It's just good economics – and saves you money! Most of this list reflects risks that not all insureds have and other forms of insurance can cover. So, for instance, autos held for sale are excluded. Good thing because your premiums won't be affected by losses to

this type of property. Those in auto sales can obtain insurance specifically fitted to their risks.

Curious about property not covered? Whip out your policy and check the list. Among items not covered:

- vehicles licensed for use on public roads
- animals
- money
- other items that can be covered by other forms of insurance.

We'll get to other available insurance coverage soon.

Additional Property Coverages

The Building and Personal Property form provides five additional coverages. These apply no matter which causes of loss form is used in the package. They are:

1. debris removal
2. preservation of property
3. fire department service charges
4. pollutant clean up and removal
5. increased cost of construction.

Two key facts about these additional coverages are:

- Each are designed to meet the average commercial insured's needs. Your particular business may need more dollar protection in one or more of these areas.
- Each relates to losses arising from a covered peril, not to building or personal property value.

Remember the massive cleanup of the World Trade Center? That shows the importance of debris removal and pollutant cleanup coverage. What happens when you have to remove property in the face of an insured threat or disaster and store it elsewhere? Preservation of property coverage reimburses you for that.

. **Note.** Until a few decades ago, insurance was sold only on the basis of *Actual Cash Value* (ACV) reimbursement. ACV means losses are paid at current market cost—in other words, original value less depreciation. This makes it hard on a business forced to replace property. Today you can choose between ACV and a *Replacement Cost Option* (RCO) (cost to repair or replace).

The Last Additional Coverage

With that note on recovery in mind, the increased cost of construction coverage makes sense. If you have RCO on your policy, this pays for the higher cost to rebuild (costs usually go up because of new ordinances or laws. For example, new building codes not in effect when the building was built might require sprinklers or safety glass in windows).

* **Tip.** Remember, none of these five coverages are as simple as set out here. You are urged to brush the dust off your policy! Read it. Understand it. And review it with your agent – your trusted advisor.

Coverage Extensions: A Brief Look

The Commercial Package Policy allows you to *extend* coverage to property not regularly covered under the policy. You are saying to the insurance company, I want these specific situations covered in the event of a loss. Each

coverage extension has its own details of coverage. The nuances of the extensions come into play when a loss occurs and there's no specific insurance written on the property.

The six coverage extensions are:

1. Newly acquired or constructed property. This includes both buildings and business personal property subject to maximum dollar limits each. This extension protects your business if new property is added during the policy period.

* **Tip. Always report changes** to your business or real property.

When your business personal or real property changes, always report it to your agent. If it's a change to either coverage extensions or the business organizational structure, **report it**. This includes a new partner, the change to a corporation, or a new line of operation.

. **Note. Don't assume** a change is covered by your insurance. That's dangerous.

2. Personal effects of people involved in your business
3. Research to restore valuable papers and records
4. Property off-premises temporarily for storage or for shows.
5. Outdoor property such as fences, signs, and plants
6. Non-owned detached trailers

. **Note.** These six categories of coverage extensions are a great deal more complex than we'll go into here. Check with your insurance agent for complete details.

HAPPINESS IS A BOP

Almost everyone knows about Homeowners and Personal Auto policies. The success with these policies spurred the development of a similar package policy: the Businessowners Policy (BOP). This policy is intended for main street businesses. The BOP combines building, personal property, and liability coverage with other attractive options. Every BOP package must have a set of Policy Conditions. We'll review those conditions later.

As mentioned before, the Insurance Services Office forms are as close to a standard or benchmark policy as there is in the United States. The ISO also standardizes the BOP, although you may have a BOP with different provisions.

Are You Eligible for a BOP?

The two keys to BOP eligibility are **type of business** and **square footage**. General examples:

- apartment buildings
- office buildings
- buildings used primarily for mercantile, service or processing purposes
- wholesalers
- contractors
- mixed use, e.g., stores in an apartment building.

Square footage guidelines can relate to overall building space or a business's rental space. Generally, the cutoff for BOP eligibility is 25,000 square feet; however, this varies between insurance companies.

One Size Package Policy Fits All?

Fitting an insurance policy to a business depends on a number of factors. This includes which insurance companies are in the market for what types of risks and restrictions. While BOPs are fine packages of coverage, you haven't missed out if your business has a Commercial Package Policy (CPP). A CPP is the right coverage for many businesses. An insurance agent can determine whether your business is eligible for, and should have a BOP.

Business Personal Property Coverage

Business personal property coverage can include:

- a building owners' business personal property in an apartment building
- office business personal property
- business personal property for merchants, wholesalers, and service or processing organizations
- commercial condo unit owners.

When you *own* a building, the same BOP must cover both the building and the business personal property. Otherwise business personal property can be insured alone in a BOP. This is good for businesses that lease or rent space.

Different BOP Forms

The CPP has different causes of loss forms that provide different levels of coverage. The ISO BOP has a named peril form (Standard) and a Special peril form.

The BOP named peril form will:

- have coverage for a dozen or so perils such as fire, lightning, windstorm and hail, sprinkler leakage, and vandalism
- usually cost less.

The Special peril form will:

- have coverage for all risks of direct physical damage except as limited in the policy
- have broader coverage than one setting forth *specific* perils.

Additional Coverages

By nature, the Special form has more coverages built in. The Standard form has approximately a dozen *additional* coverages. Among these are:

- debris removal
- counterfeit money orders and paper currency
- increased cost of construction
- forgery
- exterior glass and lettering (this includes replacement and repair of items on the outside of the building, commonly advertising-related materials)
- collapse and water damage.

Don't worry, we're not ignoring loss of business income and extra expenses from a direct insured loss. Frequently a loss from a fire or other insured peril goes beyond the direct damage caused by the fire. Even *minor* damage can close

your business for a long time. This means your business has no income to maintain salaries and other expenses. Don't ignore loss of income protection! We'll get to the issue of a break in the workflow soon.

* **Tip.** Business interruption coverage is *not* a luxury.

Coverage Extensions

Recall that extensions are an opportunity for you to have certain property covered after a loss. Extensions are controlled by:

- a limit on expendable dollar amounts
- an after-the-fact additional premium, or
- a territorial restriction.

The ISO BOPs make provisions for the following:

- newly acquired property
- personal property off-premises
- outdoor property
- personal effects (non business property)
- valuable papers and records
- collapse and water damage.

Coverage is limited in these areas. You may need specific insurance to cover one or more of these extension areas for your business.

Exclusions & Conditions

Exclusions and *conditions* are common in insurance policies. BOPs are no exception. You'll find some

exclusions and conditions from policy to policy, regardless of the type of insurance. Conditions are normally procedural matters and loss adjustments. Exclusions are matters the insurance is not designed to cover.

. **Note.** Remember an insurance policy must be read as a unit, not as independent paragraphs or sections.

A “one policy fits all” attitude will not work any more than one prescription for glasses works for every person. Our insurance needs are all different. Everyone has a different type of property, amount of property, location, ownership, and so on. Your prescription for insurance should closely reflect your risk of loss. That way you’re not paying more premiums than necessary.

PROPERTY INSURANCE TRICKS

You may think, “At last, here are the secrets the insurance industry hides from us!” No, but you *will* find a number of tricks to make insurance work better. You’ll learn how to make the right choices when you buy your insurance

Boundaries On Loss Payments

How do you determine value? For example, my old refrigerator just gets noisier and noisier. Now if there’s an electrical fire, will the insurance company pay me for the cost of a new one? Or will I be paid what the old clunker was worth at the time of loss?

The standard recovery is *Actual Cash Value* or ACV. The law defines ACV in several ways. One ACV is current fair market value; another is replacement cost less depreciation. An insurance policy may qualify ACV giving the insurer the contractual right to replace or repair an item if this is economical.

Let’s say my refrigerator was only a year old when my place had a fire. The actual cash value of my used refrigerator is much less than a brand new one will cost. The loss payment is less than the cost of a new fridge. I’ve been let down by the insurance process. Policy options to the rescue!

I can save myself this problem if I buy **replacement cost coverage** on personal and real property. This is known as “new for old.” Of course there are controls on a loss recovery. This is designed to make it fair to me *and* the insurance company. Another tool for a fair recovery is **inflation protection**. This offers an automatic rise in

insured property values so inflation won't mean low recovery at the time of a loss.

Valued Policy, Valued Policy Law, Agreed Value Policy and similar names indicate policies with a special settlement provision. These policies have set amounts you must pay at the time of a total loss. Most common are collector vehicle policies. The amount to be paid for vehicle theft or destruction is set in the Declarations. In other words, this is a *pre-adjusted loss*.

* **Tip.** Don't rely on the terminology for these insurance policies! It is seriously misused. Know your policy. Ask questions about things you don't understand. Your agent is there to give you answers.

Some states have *value laws*. These require the insured value to be paid in a total loss. These laws stop insurance agents and companies from selling high dollar coverage that would never be paid under an ACV policy.

* **Tip.** Review your insured property values each year. Values change.

Why Do Deductibles Exist?

Sometimes it makes no sense to insure a small loss. Why? It could easily be paid out of pocket and deducted from your taxes. Besides, it can end up costing more than your recovery. Policy writing and claim adjustment costs make insuring small losses uneconomical for both sides. Deductibles eliminate small losses and save premium dollars.

Deductibles also reduce the chance that dishonest people would create losses if there was no cost to them. No one likes a deductible during a loss. But that deductible may save you *more* premium dollars than the amount of the

deductible. Probably the first one that comes to mind is for a car. Those deductibles of a set number of dollars are called *straight deductibles*.

There are three other types of deductibles:

1. **Aggregate.** Adds all losses up to a certain dollar amount. After that, other losses for the policy year are paid in full. That way a business knows its maximum dollar loss for the year.
2. **Franchise.** Below a certain dollar amount, you pay for a loss. Above a certain dollar amount, the insurance company pays. These deductibles are common in ocean marine insurance where small losses from dampness, pilferage, and similar perils are common.
3. **Disappearing.** Lives up to its name. When a loss is large enough, there is no deductible.

* **Tip.** Save money! Increase your Deductibles!

More Deductibles?

The few remarks here concern insurance tools that are like deductibles or otherwise control loss payments. Two deductible-like tools are found frequently in health insurance:

1. **Elimination** or **waiting** period. Holds loss payments until a certain point is reached. You carry the losses up to that point.
2. **Percentage participation requirement** (also called co-pay or, incorrectly, coinsurance - see below). Holds you to a set percentage of the payment in a loss.

Provisions

What happens if you have two insurance policies covering the same property? Insurance policies commonly have provisions for this situation. Even though they are not deductibles these provisions also serve to reduce moral hazard.

Policy provisions to multiple insurance policies covering the same property:

1. call for the policies to split a loss prorata (no sense in buying more than one policy)
2. make one policy primary and the other excess
3. bar any contribution to a loss, and
4. with no provisions, both pay as in life insurance.

Coinsurance & Its Friends

Never tell an insurance agent that coinsurance is a type of deductible. Chances are, you will be considered wrong. A coinsurance provision in a property insurance policy means an insured shares in a loss. Isn't this the act of a deductible?

Insurance rates are determined on a number of assumptions. A major one is projected losses. Another is that every insured will take enough insurance dollar-wise to cover the full value of an insured property. However, some insureds will figure that most losses are small and rarely a total loss. So those insureds will insure for less than the value of the property. In turn the premiums received by the insurance company are less than expected.

The insurance company reasons that if you want to insure for less than full value, you'll have to share in the losses. The insurance policy will set a coinsurance percentage,

frequently 10%. That percentage will be the basis for loss sharing. **If the insured maintains insurance to the required percent, there is no loss sharing.** For example, a \$100,000 building, a 10% coinsurance requirement, and \$90,000 of insurance equals full recovery. Meeting the required coinsurance percentage means no loss sharing.

Coinsurance penalties are established at the time of a loss. If your property has increased in value, surprise! Your loss recovery is reduced by a penalty.

Coinsurance is more complex in detail, but those are the basics. What looks like a rip-off at the time of a loss settlement actually translates into premium savings over the years. Want to avoid coinsurance problems? Then don't avoid this tip!

* **Tip.** Dodge coinsurance penalties with avoidance tools. Review this with your agent!

Ask about an *agreed value provision*. This allows you and your agent to set the amount of insurance you carry. If this agreed amount is carried, then a coinsurance provision is waived. Other avoidance tools are *Replacement Cost Coverage* and *Inflation Guard Protection*. These prevent your coverage from falling below the required coinsurance percentage, forcing you to share a loss.

Reporting Forms

Business inventories can fluctuate widely over time. Perhaps the inventory is high because a special sale is scheduled. Or maybe Christmas season inventory is higher than normal. Goods may be moved from location to location for special sales or other reasons. Therefore, inventory can vary at multiple locations. Say that the business owner paid premiums based on the highest inventory period of the year.

The result would be over insurance. Reporting forms allow you to pay the correct premium for the inventory despite varying inventory.

At the beginning of a year, you pay a provisional premium. Current inventory values are reported on a daily, weekly, monthly, quarterly, or policy year basis. At the end of the insurance policy year, you either pay additional premium or the provisional premium is returned.

* **Tip. NEVER** accept a reporting provision unless you can provide timely, accurate reports. There are penalties for failing to report properly.

Improvements & Betterments—Or, Insuring Something You Don't Own

You rent a new facility and installed permanent partitions, fancy lights and a large boiler. With a 15-year lease, it looks like you're set until retirement. After a year of happiness, the building burns to the ground. You can't collect for the loss of the permanent items you installed. Why? Because they legally became the landlord's property. Where will you find the funds for a new location? The value of improvements to the real estate of others can be very expensive.

A person investing in improvements and betterments (alterations) to rented property can insure the *use value* of the changes. Permanently installed items or items that devalue the property if removed generally become the landlord's property.

You can insure against the loss value of your changes. This begins at cost. But as the years go by, since you have had the use of your improvements, it is less. Conversely, the landlord can insure the value of your improvements. The

term *improvements and betterments* is an old one intended to convey any type of improvement.

Another term, *trade fixtures*, is an important one because it conveys items like counters that can be removed legally even though permanently attached to the rented space. This is by custom but usually a lease will cover trade fixture ownership.

H Example. Let's say I rent your space from you and I do not like the lights. I tear your lights out and install my own of much better quality. I better save your lights because when I leave, the space has to be made usable. In other words it needs lights. The time to set ownership of property installed in a landlord's building is at the time of leasing.

* **Tip.** A proper lease takes into account questions like who owns what and who will insure what. That's the key to protecting both the lessee and the lessor.

The "Vacant & Unoccupied" Trap

Properties that are vacant or unoccupied present a higher risk of loss than property in use. Vagrants can use vacant buildings for shelter. And fires can occur with no one to send out an alarm. Insurance companies will insure vacant and occupied buildings but they want to know it.

Provisions are often found in property insurance policies eliminating or reducing coverage for a building that becomes vacant or unoccupied. These provisions may become effective after so many days, 60 days is common. Coverage may not be cut for all perils, but only those likely to occur as vandalism and glass breakage.

Unoccupied means usual activities or operations have been suspended; however business personal property has not

been removed. Vacant means empty. This *trap* should not catch you—just keep your insurance agent apprised of any periods of vacancy.

* **Tip.** The material in this chapter will make you a better insurance consumer and reduce surprises at the time of a loss.

THE LOSS OF BUSINESS INCOME TRAGEDY

Suddenly, your business is destroyed and your income stream crashes to a halt. It will be months before you can hope to be operating again. Your property insurance will provide funds to rebuild, but where will your personal expenses, e.g., your home mortgage, come from? Will your valued employees drift off if there are no funds for payroll? Will your customers return when you reopen? What if your business can't stop and you must fund a temporary location?

H Example. A dairy owner can't tell cows, "We're not going to milk for a month or so." A number of businesses must keep operating, such as newspapers and banks. There are, of course, other examples. Closed businesses can't maintain customers or fulfill important contracts.

Business Interruption Coverage— Protect Yourself Before It's Too Late

Many businesses know they need to cover their property with insurance to replace physical property. But most fail to see the significance of business stoppage. Fortunately, insurance is available to answer the need for income funds. Business Interruption, Business Income, Time Element, and Extra Expense are all terms used for insurable non-physical losses.

What Does Loss Of Business Income Insurance Mean For You?

Business income insurance covers business earnings in the event of an interruptive loss. The ISO forms state that:

coverage is provided for net income (net profit or loss before income taxes) earned or incurred. Coverage is also provided to continue normal operating expenses incurred, including payroll

Think Profit and Loss statement.

* **Tip.** Use a worksheet to determine coverage.

A business income worksheet establishes coverage amounts of business interruption insurance. This establishes dollar amounts of coverage with no uncertainty. Involve your accountant in preparing a worksheet.

Do You Need Extra Expense Dollars?

There are two major reasons for extra expense insurance: competition (for instance, small businesses) and public demand (newspapers, banks).

Extra expense insurance is bought with business income insurance. It provides extra operating money while the business income coverage provides earnings. The extra expense funds cover continuing operating costs. This might mean temporary operating quarters until the permanent quarters are repaired or rebuilt.

Important Info: Additional Time Element

If you have suffered a business income loss or an extra expense problem, you are required to pursue normal operation quickly. This requirement protects the insurance

company. That way recovery isn't prolonged because the business is enjoying an income stream.

What if business doesn't return to normal volume right away? After the disaster of being forced to close, nothing is more discouraging than opening the door to a slow start. There is special insurance for this situation. It's called *Extended Loss After Operations Resume*.

Sometimes one business depends seriously on another business. Perhaps there's a fire at a computer chip factory and they can't supply the computer manufacturer. Or the anchor department store in a business's shopping center burns and shopping traffic disappears. *Dependent Property* coverage, formerly called Contingent Business Interruption Coverage, provides protection.

Many options exist in Business Interruption insurance. For example, the loss of rental from damaged property can be covered. So can the loss of tuition by organizations that receive their income at a given time of the year.

The specifics of business income coverage depend on the perils covered by the policy. The perils closely mirror those in the property policies we have looked at previously.

Coinsurance

If you liked the idea of waiving coinsurance in a property policy, you'll like these four optional coverages that stop coinsurance from applying to a loss:

1. Maximum Period of Indemnity
2. Monthly Limit of Indemnity
3. Business Income Agreed Value
4. Extended Limit of Indemnity

* **Tip.** Every business should consider some form of loss of income insurance. Discuss this with your agent! It may be the most overlooked form of protection that you can't afford to ignore.

LIABILITY

If you injure or damage a person or their property, you are liable to that person for damages. That's a basic premise of our legal system. This premise came out of the English Common Law system as adopted by America. Some types of liability include contractual, product, and professional. The most familiar liability is negligence, or failing to avoid injury to others or their property.

Negligence is based on taking reasonable care to avoid bodily injury or property damage to others. We guard against the cost of our negligence with liability insurance. The same act may make you both criminally and civilly liable to others. However, liability insurance only protects against civil responsibility.

Auto Liability: Why?

You're most familiar with automobile liability insurance. Business liability is just as dangerous as the auto liability. Let's look at a number of liability insurance policies including general, auto, pollution and employee.

Despite the criticism surrounding auto liability insurance, jury awards and lawyers, we retain the negligence system. Why? Simply because no one's ever come up with a more satisfactory system. When another person causes injury to you, your family, or your property, you want compensation from that person. Someone must take responsibility for the damage or injury.

No-fault coverage has been around for years. But it's not a very popular idea to buy insurance for others' mistakes.

Should the person who ran the red light and caused you serious injury claim no responsibility?

Unfortunately, we have to buy insurance to protect our family, our property, and ourselves. The reason is that many people don't purchase liability insurance to answer for their faulty actions. That's why we have uninsured, underinsured motorist, and no-fault plans. We'll look at Workers Compensation in relation to no-fault coverage later.

Liability Policies: Ins & Outs

Liability insurance policies are easier to understand than property insurance policies. That's because liability policies have numerous things in common, even among different types.

Here's an overview of liability insurance:

- covers acts anywhere within the policy territory.
- provides various dollar limits, or "maximums" that a policy pays for a claim. The costs to defend a liability claim may be in addition to the policy's limit of liability. Or they may be included within the liability limit.

Different limits can exist for different events, and there can be *single* or *split* limits. Your personal auto policy may have a single limit of \$300,000, or a split limit of \$100,000/300,000. This split limit covers up to \$100,000 for bodily injury to one person in an accident, and a maximum of \$300,000 for all bodily injuries. Often there is a separate amount for property damage; these limits could be expressed 100/300/50.

- may contain a Medical Payments provision. Injured persons are paid simply on bodily injury, not liability. Kind of a good Samaritan coverage.

. **Note.** Employees are often not covered for medical payments. They should be covered by Workers Comp. We'll review that later.

- have *named, additional, and other* insureds. These can be complex and can depend on various factors. Check with your agent. And review your policy carefully.

* **Tip.** Always know who is an insured before an accident. Otherwise, you could face a liability claim without an insurance company's pocket to pay a settlement or judgment.

If your son or daughter helps out at work one day, are they covered for negligence under your business's Commercial General Liability Policy? If your cousin Will came to visit and wanted to borrow your company car, is he covered for a negligence claim?

We'll look next at the Commercial General Liability Policy (CGL) and the Business Auto Policy (BAP).

PUBLIC LIABILITY/CGL

Your business should start with a general, or *public* liability policy. Your premises and other areas your business is responsible for are protected by this.

Perhaps your business also needs an auto policy and even several other liability insurance policies we'll get to later. We'll use ISO's Commercial General Liability program (CGL) to talk about public liability.

CGL: In Two Tastes

Two CGLs are available:

1. An **Occurrence** policy. (the most common) A claim is paid if it *happens* during the policy period.
2. A **Claims Made** policy. A claim is paid if *made* during the policy year.

This creates problems when you switch between types. In addition to these CGL divisions, there are coverage forms A, B, and C. Two others also exist:

1. **Owners and Contractors Protective Liability.** Protects you from liability for acts of independent contractors.
2. **Products-Completed Operations Liability.** Protects against claims on product failure. This could be anything from a building to a jar of spaghetti sauce.

Obviously, putting together a solid CGL policy is a tough but crucial chore.

Other tools can also fit a CGL to various business situations. Among these are pollution and employment-related matters. More on those later.

Who Is An “Insured?”

This is a complex question. We'll keep it pretty basic here.

The primary insureds are the named insureds set out in the *policy declarations*. This could include you and your spouse, a partnership, joint venture, limited liability corporation, or other organization. Members of these organizations—executive officers, directors, and stockholders—are insureds only for incidents related to their business duties. Employees, including leased workers and volunteers, are insureds for actions related to business. Temporary workers are *not* insureds; they will not be defended by a CGL. Your firm will be defended regardless.

. **Note.** The first named insured has particular responsibilities related to communication with the insurance company.

What Is Territorial Coverage?

The CGL offers coverage in the USA, its territories and possessions, Puerto Rico, and Canada. Travel and transportation between these areas are covered, too.

Goods and services are covered if:

- the goods or services were made or sold in the covered territory, or
- problems result from an insured based in covered territory, but is elsewhere on business for a short time.

Worldwide coverage for personal and advertising injury is included automatically in CGL. Coverage for all Internet activity can also be added.

To make a CGL claim, you must bring a lawsuit in the policy territory. Or the insurance company must make a voluntary settlement. Worldwide territorial coverage may also be added to a CGL.

. **Note.** you'll see how close the Business Auto coverage territory is to CGL. Remember, when you understand one liability policy, others will be similar.

Three CGL Terms You Must Know

Occurrence. Lots of time and effort has been spent deciding what incidents liability policies would routinely cover. The old word was *Accident*, but it was too narrow and implied only sudden incidents. Today the word *occurrence* is commonly found in liability policies. The CGL reads:

“*Occurrence* means an accident, including continuous or repeated exposure to substantially the same general harmful conditions.”

Insured contract. CGL does offer some coverage for a few contractual liabilities. These agreements include:

- sidetrack
- easement or license
- elevator maintenance.

H Example. Let's say a railroad contracts to run a track along your warehouse property. Plus, the railroad holds you responsible for injury or damage from the sidetrack. That's a sidetrack agreement.

Impaired property. This is tangible property that can be restored.

H Example. Some of your work is incorporated into another's work or product. It causes that work or product to be impaired. Under CGL, you have coverage. That coverage is not for your work, but for correcting the impaired property.

Realize liability insurance does not correct your poor workmanship; it just compensates others for your negligence.

CGL Coverage A

Coverage A covers bodily injuries and property damage common in any business. It also spells out the insurance company's obligation to provide a defense to claims. You are insured for an occurrence unless it's excluded. The major exclusions are categorized:

- responsibilities to employees
- damage to your work or product
- aircraft, auto and watercraft.

Other exclusions include liquor liability, pollution, intended injury and war. Unless the federal government establishes some form of support for private insurance, war coverage will most likely *not* cover terrorist acts.

. **Note.** Most of these exclusions can be picked up with an additional CGL coverage form or separate insurance.

Fire damage to property you rent or occupy can be covered; however, a separate dollar limit applies. Liability for fire to another's property in your care is excluded under basic CGL coverage. This is because liability policies don't

generally cover property in your care, custody, or control. Such property is considered to be a property risk rather than a liability risk.

* **Tip.** Party time? Keep in mind CGL exclusions for liquor and aircraft and watercraft. If you're not in the liquor business, there is coverage when providing drinks at a business or employee function. If you plan to use someone else's watercraft or plane for a party, check your policy first. CGL is not always an answer.

CGL Coverage B

Coverage B gives personal and advertising injury liability coverage. A broad range of offenses is covered which are not bodily injury or damage to physical property. Again, a specific dollar limit applies. This coverage is not for those firms in advertising, publishing, TV or Radio.

Personal injury includes libel and slander. The liability covers advertising business goods, services, and products. Exclusions include:

- intentional acts
- wrong prices or quality
- copyright, trademark, trade secret, or patent violation.

Coverage B can be an important addition to the protection provided by Coverage A.

CGL Coverage C

This medical payments provision isn't triggered by a charge of negligence. The insurer will pay up to the Declaration page dollar limits for medical services at the time of the

accident. Later medical services, including ambulance and hospital are covered, too.

Of course, territory restrictions apply. Also, the injured must submit to a medical examination.

There are three advantages to purchasing Coverage C:

1. It may give an injured person second thoughts about suing.
2. You'll have peace of mind if someone was injured on your premises or in your operations. Their medical expenses will be paid.
3. The insurer gets a medical exam of the injured. This protects you if they decide to sue later.

Volunteers are the only workers that can receive medical payments. Workers Compensation generally covers employees.

. **Note.** Athletic activities are *not* covered by C. Sponsorship of athletic activities, including auto racing, involves risks not anticipated by routine business insurance. Exclusions include intentional injuries.

What If I Need To Add A Business?

Your firm is rocking along well. The opportunity arises to add another business. You can do this by forming a corporation or buying another firm out. Will you have coverage under CGL? Yes, under certain circumstances. These are:

- First, you (your policy's named insured) must own or have the majority interest in the newly acquired business.

- Second, the coverage only applies for 90 days or, if earlier, to the end of the policy period. This automatic coverage does not apply to partnerships or joint ventures.

H Example. Hey Joe, that Brown job is a big one. Why don't we work it together? This is a joint venture, so no automatic CGL coverage. Your best operating rule is report to your insurance agent all upcoming changes to your business!

Supplement Payments & Conditions

Supplemental payments are what an insurance company pays in addition to various CGL policy limits on coverages A, B, C. These payments include:

- provisions covering the cost of bail bonds, but not their acquisition.
- your expenses and earnings up to \$250 for helping with claims and lawsuits.
- costs taxed to you; prejudgment and judgment interest.

CGL conditions deal with procedural matters in the event of a claim notice or receiving lawsuit papers. Also covered:

- when you have the right to sue your insurance company.
- what happens when other insurance covers the same loss.

The Pollution Danger – A Serious Threat

The risk of causing pollution that legally damages others, their property, or triggers action by government has become a serious threat to all types of businesses. The list of what is considered to be a pollutant has grown to the point where there are jokes about everything being a pollutant. Some items have gained a pollutant status after years of common use. Think of asbestos for example.

As the risk of pollution was expanding, insurance companies began to develop special pollution policies and began to restrict coverage under the CGL. Insurance operates based on what prior experience indicates losses will be in the future. No one knew how big the pollution risk was going to be and, of course, the premium structure for the CGL did not take into account what insured would have to pay for pollution coverage. Thus began the restriction of pollution coverage in existing liability policies.

Pollution Exclusion: It's Black & White

The CGL pollution exclusion is nearly absolute. As the pollution risk grew through court action, this exclusion developed. The old versions of the exclusions were expanded to cover new pollution forms and policies. CGL has two Pollution Liability coverage forms. It also has a special form for underground storage tanks.

The current edition of the ISO CGL has pollution coverage narrowed down to a few covered occurrences. These may include:

- certain off-premises exposures

- certain product-completed operations
- smoke, fumes, soot, vapors from your heating equipment or from a fire in your building
- gas or fumes from materials you bring into a work site.

One CGL pollution situation left by the exclusion is liability coverage for fuels, lubricants, and other fluids used to operate mobile equipment. We'll see this protection again in the business auto coverage.

What are the solutions to the pollution insurance question? A specific CGL form or a separate Pollution Liability Policy. We'll look next at Business Auto Coverage and its Pollution position. Pollution insurance follows that.

TWO TRICKY TRAPS OF YOUR CGL

Logic would tell us to follow the CGL chapter with one on the Business Auto Policy (BAP). However, before that, we need to look at the dangerous confusion between these two insurance policies. We must determine which policy covers loading and unloading, and mobile equipment.

How To Deal With Loading & Unloading

Your employees are loading your truck. A box is carelessly tossed at the truck. It strikes a passerby and injures them. Covered by your CGL or your BAP? What if it is my truck and driver? Your CGL or my BAP? Where does the BAP end and the CGL take over? Once a delivery item is set on the ground, off the truck, or at its destination?

Numerous questions like these have caused many lawsuits. They have also led to many rewrites of the CGL and the BAP.

Let's see how the policies handle this problem. CGL doesn't cover injury or damage from the transportation of property by truck. When loading or unloading a truck, CGL gives coverage if you load with a forklift or other mechanical device. However, when an insured trucker is loading by hand or with a hand truck, coverage is under a BAP. The BAP is meshed with the CGL coverage.

The BAP excludes loading or unloading by mechanical device *unless* the device is attached to the vehicle. Combined with the CGL, this makes a device attached to the truck a problem for the BAP. But a device not attached

to the truck is a CGL problem. Further, the BAP covers the entire transport process of property.

So one truck delivery or pickup could result in a BAP covered claim *and* a CGL covered claim. Without *both* a BAP and a CGL, you can't properly cover loading and unloading.

* **Tip.** It is good to have both your CGL and your BAP with the same insurance company. If there is a question of loading or unloading, there is no question about which insurance company covers it. There is only one.

What's Mobile Equipment—And What's Not?

Both the CGL and the BAP have identical lists of what is and isn't mobile equipment. These lists help determine which policy to use for what equipment.

First let's look at what is not mobile equipment. This will belong on your BAP. The first category is classified as autos. This includes:

- self-propelled vehicles with permanently attached equipment, if designed primarily for snow removal, street cleaning, or road maintenance other than construction or resurfacing.
- cherry pickers and similar devices mounted on an auto or a truck chassis.
- air compressors, pumps, generators, welding units, building cleaning units and other similar items.

Now what's included as mobile equipment in the CGL? Here's a sampling:

- bulldozers, forklifts and other equipment designed primarily for use off public roads, including vehicles on crawler treads.
- vehicles used primarily to give mobility to loaders, diggers, air compressors, and similar equipment.
- vehicles that are self-propelled or not self-propelled. Not self-propelled could be a trailer.

Obviously businesses can easily get into a non-covered situation. Vehicles *maintained for use solely on or next to the premises you own or rent* can be classified as mobile equipment. So you could have a pickup truck for on-premises use only. It would be cheap to insure and probably would not have to be licensed. But then employee Joe Not Too Bright decides he can make a fast trip off premises with that pickup. Accident? No coverage.

Why the big deal about how to classify what? It all comes down to coverage and premium cost. Your agent is interested in seeing your equipment is correctly insured. Clearly regular road driving is a very different risk from the use of mobile equipment.

THE BUSINESS AUTO POLICY, AKA THE COMMERCIAL AUTO PROGRAM

Warning! Warning! A plain vanilla Business Auto Policy (BAP) does **not** serve as a substitute for a Personal Auto Policy (PAP). Unless you're in a company car on business, the BAP doesn't cover liability and medical payments. This is not a cruel trick; it protects your company from liability for non-business accidents. So you borrow my car to pick up your child at soccer. No coverage.

If you insure your auto under a PAP, you and your family have liability coverage and medical payments for non-business accidents.

Can the BAP be endorsed to function like a PAP? Yes, there are two *drive other car (DOC)* endorsements to effect this change. One is for corporations and the other is for unincorporated businesses. Your agent can arrange the proper endorsement for your needs. However, don't avoid a PAP just to save premiums or for tax reasons.

Generally, a PAP can suffice for a sole proprietor with private, passenger-type vehicles only. A private passenger vehicle owned or leased by a corporation, partnership or other business organization is a different story. You must use a BAP.

Business Auto Coverage Forms

Most businesses carry the ISO Commercial Auto Program liability coverage along with a CGL. The auto policy and the CGL may be packaged together; however, they remain separate policies. The auto risk and the premises risk are not

combined into one policy. The Business Auto Policy (BAP) has three close relatives:

- the Truckers policy
- the Garage policy
- the Motor Carrier form.

These policies are very similar to the BAP. They are altered to meet the differing needs of those in a garage business and those in a trucking business.

A **Garage** policy is used for service stations, public parking facilities, trailer dealers and others involved with auto activities.

The **Truckers** policy is for those who offer for-hire trucking.

The **Motor Carrier** form is used for organizations that haul their own goods and the goods of others. This form also covers the interchange of semi-trailers. The federal act regulating motor carriers can make certain insurance coverages and limits mandatory. We'll look at basic business auto coverage.

. **Note.** *Auto* here is used to mean a land motor vehicle, trailer, or semi-trailer designed for travel on public roads.

* **Tip.** It's not simple to insure business autos. Be sure to give your agent all the details of your business vehicle use. **IMPORTANT:** Don't forget to report any changes that occur.

Symbols & The BAP

No longer are we dealing with *special*, *standard*, and the like. The Business Auto Policy uses symbols 1 through 8 to

indicate vehicle coverage for claims. **Symbol 1** gives any auto coverage. The insured is covered for owned, rented, borrowed autos and an auto just used by the insured. This is the most common coverage.

Symbol 7, the other most common symbol, covers only specifically described autos. Newly acquired ones, under 7, are given coverage only if the insurer insures *all* owned autos. Symbol 7 also covers a new vehicle that replaces a covered one. This feature only works *if* the acquired auto is identified to the insurance company within 30 days.

Symbol 8 covers only hired, leased, rented or borrowed autos and *not* owned autos. That's good for a business that doesn't own an auto.

Symbols may be combined to serve certain coverage needs. Now, if the coverage symbol insures the auto, is the driver insured?

Who Is Insured Under A BAP?

You or the firm, as the named insured, is an insured for any *covered auto*. Anyone else using a covered auto you own, hire, or borrow with your permission is an insured.

Exceptions? Of course.

- the owner or anyone else from whom you hire or borrow an auto
- an employee if the covered auto is owned by that employee or his family
- persons working in an auto business that is not yours
- a partner if he or she owns the auto.

These exclusions appear complex. In reality, they confirm that your policy doesn't cover other auto owners; in other words, get your own insurance for your own car or coverage for your garage business. WAIT, you and your business are still covered!

Employees as a category are covered as insureds by a BAP; however, they may *not* collect as claimants from the policy *if*:

- they are entitled to Workers Compensation benefits, or
- they are covered by Employer's Liability Insurance.

This prevents double recovery and keeps Workers Comp the exclusive means of compensating an injured employee. As mentioned, we'll cover more later on Workers Compensation. Leased employees, but not temporary employees, are covered as drivers of a covered auto.

Some Answers For "When & Where Covered"

The coverage territory includes:

- the United States, its territories and possessions
- Puerto Rico
- Canada, and
- transportation between those places.

Special coverage exists for the growing business with Mexico. For you travelers, the BAP gives coverage anywhere in the world. This covers private passenger type autos leased, hired, rented, or borrowed without a driver. The time constraints on this are 30 days or less.

. **Note.** The policy only pays if a lawsuit is held in the basic policy coverage territory.

One other territorial factor is covered by the BAP. This is the variation in auto insurance required by the 50 states and the other territory covered. The BAP automatically adapts to the financial requirements beyond the borders of your home state. United we stand—until it comes to drivers licenses, license tags and financial responsibility laws.

BAP Exclusions

Expect to see three exclusions when you deal with commercial autos:

- intentional acts
- racing
- war.

Insurance excludes intentional acts almost universally. Insurance is not for helping people who have intentionally caused others bodily injury or property damage. Racing insurance coverage is available from what we call *specialty markets*. These markets specialize in providing insurance for unusual risks.

War acts are too great a risk for private insurance companies. After the World Trade Center disaster in 2001, insurance companies attempted to exclude terrorist acts. Why? Because they realized one event could be too costly for any insurance company. To insure these acts would require premiums to drastically increase. Some states have allowed a terrorist exclusion. Others have not. Perhaps the federal government will create a reinsurance pool to support private insurance companies. Maybe then insurance can offer you coverage for terrorist acts.

Coverage: One For You, One For Them

Two matters of coverage may surprise you. One regards property in your care, custody, and control. This property is *not* covered. Liability insurance pays for damages to *others'* property, not property you control. Items in your hands are rightfully a *property*, not a liability risk. Your property, bailee's and transportation insurance cover items in your care, custody, or control.

A person making a liability claim against you may be surprised to find out they cannot collect on "diminishing value."

H Example. Say your truck negligently hits my brand new Belchfire 8, a car I just love. I claim that even though the car can be repaired, it will never be worth what it was before the accident. A number of jurisdictions do not allow diminishing value damages. This subjective loss of value does not affect the use value of the car.

A Little Pollution Coverage

As we saw, the CGL strictly limits pollution coverage. This is true with the BAP, too. Awareness of pollution problems has led to a dramatic rise in claims against polluters. The insurance industry was not prepared to support these claims. No premium had been collected and the extent of the losses was unknown. Thus, separate pollution coverage was developed. This meets the need of firms involved with polluting materials.

What pollution coverage does the BAP offer us?

H Example. There's an accident on a road and gas or other vehicle fluids leak out. You are covered for cleanup charges

required by government. This doesn't include claims arising from the spill of cargo or trash.

H Example. Your truck is on the property of another to collect pollutants. It hits a pollutant container, spilling its contents. You are covered by the BAP. No coverage for pollutants on or in the truck. A little confused? When in doubt, get pollution coverage.

Supplementary Payments & Your Duties

Supplemental payments are what the insurance company will spend. They don't reduce the limits you use to pay claims. The insurer will pay the following:

- all of the court costs
- some money for taking time off of work to help, and
- the cost of a bail bond related to an accident covered by the policy. The limit on bail bonds is \$2,000. The insurance company won't acquire the bond for you.

Your Duties Under The BAP

Give prompt notice of accidents that fall under BAP. Include whatever details you can about other people and property involved. Don't assume responsibility for an accident. Be sure you cooperate fully with the insurer. Part of this cooperation is forwarding legal papers from the other side immediately to the insurer. Another part is notifying the police of stolen property.

* **Tip.** Never admit liability to anyone. You may lose your coverage. Fault is a legal decision for the courts.

Medical Payments Coverage

Contrary to your PAP's Medical Payments section, BAP Medical Payments is an endorsement. This is because few businesses take medical coverage. Workers Comp usually takes care of that. It can be a good idea in these cases:

- if you are an individual named insured
- if your firm carries passengers
- if your business allows customers to drive your autos.

How Do I Cover Vehicle Damage?

The BAP includes coverage for damage to your property, not just liability. Therefore it's not a *monoline* policy. The physical damage coverage is referred to as *first party* coverage. The liability coverage is referred to as *third party* coverage. The third party claimant is not a party to the insurance policy. So it's logical.

The physical damage coverage for your autos and their equipment is available. With this, you've got a choice of collision/overturn and comprehensive coverage for six named perils. The *Specific Causes of Loss* coverage includes:

1. Fire, lightning, or explosion
2. Theft
3. Windstorm, hail or earthquake
4. Flood

5. Mischief or vandalism
6. Sinking, burning collision, or derailment of any conveyance transporting a covered auto.

Comprehensive coverage costs more but covers many more situations, like glass breakage and hitting an animal. If you want to save premium, take the six perils above. Or purchase a few of them.

The physical damage coverage has its own restrictions and conditions. One is the exclusion of tapes and records, speed measuring equipment, and other electronic equipment not used solely for the reproduction of sound.

* **Tip.** In this day of loads of electronic equipment in vehicles, consider carefully and specifically what items need insurance.

After Auto Damage: What Now?

As you stand looking at your wrecked vehicle you may say, “Give me the cash.” But that is not your choice. The insurer has the option under the policy of paying, repairing, or replacing the damaged property. You can’t abandon your damaged property to the insurance company. Does the insurer normally pay in cash? Sure, but unusual circumstances may call for a different settlement.

Subrogation is a common law doctrine. It says if someone pays for damage to your property, that person has the right to seek recovery from the other party. So if your insurance company pays for your damage caused by a third party, it has the right to have your help in going against them.

How To Choose BAP Endorsements

Boy, are there plenty of BAP endorsements. Remember also, there are the Garage form and the Trucker forms. The endorsements are designed to fit common situations. Here are some endorsement examples:

- Limited Mexico Coverage
- Rolling Stores
- Employee Hired Autos
- Auto loan/lease gap.

Check with your agent for proper BAP insurance.

A FEW MORE LIABILITY RISKS

Businesses can face a number of liability areas beyond those covered by the basic CGL and the basic BAP. We'll look at those risks and insurance for those risks in this chapter.

* **Tip.** Don't be surprised if your agent suggests liability coverage not mentioned here. Dozens of liability policies exist for special operations.

Risks related to employment—Workers Compensation, Employers Liability and Employment Related Liability—will come later.

Pollution Liability

A number of markets offer various pollution insurance products. ISO has a form that can be added to your CGL. Some coverage is available in *admitted* markets. Other coverage is available through the *surplus lines* market. Surplus lines refer to insurance sold by insurance companies not admitted to your state.

. **Note.** If you use a surplus lines market, your state's insurance regulators won't protect you. This doesn't mean a surplus lines market isn't a good source of insurance coverage; it's just something to keep in mind.

What if there's an exclusion in an insurance policy and you want coverage for the excluded area? If you select that, you are *buying back* coverage. Let's say you want to buy back the CGL pollution exclusion with ISO's Pollution Liability Coverage Form. What points are most important to consider?

Actually there are two ISO coverage forms. They are quite similar. But the limited coverage form excludes government mandated cleanup costs.

Are you wondering about a BAP pollution form? No such thing. The auto policy exclusions tie in to the CGL pollution forms. These CGL forms are “claims made” forms. Claims are covered only if reported during the policy period or an *extended reporting period*.

Elements Of Pollution Coverage

You'll find a number of these provisions familiar. The coverage is for bodily injury and property damage. There is a supplemental payments provision. Who is injured will be covered in detail.

Punitive damages—those additional damages based on severity and assessed by a court—are generally excluded. Deliberate failure to obey an environmental regulation may also be excluded. A maximum dollar limit for claims during a period of time or combination of events is common.

Your business's pollution exposure requires careful analysis to match you to the proper coverage. CGL pollution forms fit most businesses. There are specialty policies for:

- underground tank pollution
- real estate owner asbestos abatement
- pollution cleanup
- and many other liability risks.

What Is Bailee Liability Insurance?

A *bailment* is a change of possession without a change of title. You are involved in bailments on a daily basis.

H Example. You leave clothes at a cleaners or you leave your car for service. You still own the clothes or the car, but they're bailed to the cleaners or the garage.

Possibly your business is a regular holder of others' goods—a *bailee*. Are you covered by your liability insurance? Maybe, maybe not. Your liability insurance could exclude others' property with a care, custody, and control exclusion. Your property insurance may only cover a small amount of others' property.

Bailee liability insurance can be the answer to protecting others' property. Bailee liability insurance only pays if you are negligent. A bailee's obligation to the owners in a bailment for profit is just reasonable care.

* **Tip.** Try bailee's customer coverage.

You may or may not be legally liable to your customers whose property has been damaged or destroyed. Either way they'll expect compensation. If they're not compensated, they're not likely to support your business. Bailee's customer insurance will pay losses if your business is liable or not. It's another type of goodwill insurance.

Professional Liability Insurance

Don't be thrown off by the term professional *liability*. That covers a broad range of services by people with specialized knowledge and training. You may think of a doctor and a lawyer as the only professionals. Actually the term encompasses occupations like web site designers, travel agents, and insurance agents.

Some will argue about who is a professional. For insurance purposes, it's someone that provides specialized services that not everyone can provide. Thus insurance is available for a wide range of services. Bodily injury or property damage is unnecessary for damage to the recipient of a professional's service. If an escrow agent fails to perform properly there may be no property damage or bodily injury; however the parties will suffer at least a delay.

Why don't general liability insurance policies cover professionals? The professional risk differs from the general liability risks we all have in our personal and business lives. By separating general and professional, you don't pay extra general liability premiums to cover the professionals' risks.

Check with your insurance agent to see if your business needs professional liability coverage. The list of businesses that do includes:

- paramedics
- sports agents
- medical imaging centers
- tour operators
- mortgage brokers
- interior designers.

In the construction field, design/build firms and project managers also need professional liability insurance.

The term *errors and omissions*, or *E & O* can be used as a distinction from professional liability insurance. This applies to:

- medical related occupations
- real estate agents

- accountants
- insurance agents.

The latter group refers to its coverage as E & O.

Directors & Officers Liability

Directors and Officers liability insurance (D & O) is like professional liability insurance. It covers managerial decisions, not accidents. These D & O policies are not standardized, but they do have things in common.

Typically the policies have two parts. One gives the directors and officers direct coverage for their acts. The other covers the corporation for its obligation to reimburse directors and officers.

Important Info: What Kind Of D & O Claims Are There?

Claims that are brought against directors and officers vary.

H Example. One claim might be that the stock value was lowered because of decisions, errors, or omissions of the board.

H Example. Another claim might come from employees, the public and other businesses harmed by board actions.

Since acts by the insureds are based on personal liability, a claim outlives a director or officer. For that reason, the coverage usually extends to heirs, estates and legal representatives. There may be a spousal extension as well. This covers situations where assets have been transferred to

a spouse to hide them from a judgment. (Enron executives may be interested in this last point.)

Defense costs are treated differently than CGL. There the insurer has a right and duty to defend the insureds. In D & O, the individual insureds may have responsibility, within limits, for their own defense. This includes hiring their own lawyers.

Cyberspace (Internet) Liability

Welcome to a newly developing insurance coverage.

As Internet commerce grows, so does the need for new forms of insurance protection. We saw that CGL gives advertising and personal injury coverage. Miscellaneous E & O policies cover problems related to third party service. And specialized Media liability policies offer some peril and defense coverage. Insurance companies are starting to combine those three areas into one cyberspace policy. This offers more thorough protection to businesses communicating on the Internet.

What About Those High Judgments?

You read in the paper where the makers of a product are sued for millions or a company truck causes a 16-car accident. Does any firm carry enough liability insurance for today's claims? How can you better protect your company against an extremely high judgment?

Umbrella liability and excess liability policies can answer those questions. An excess policy simply raises the monetary amount of coverage over an underlying policy.

H Example. My auto policy has a single limit of \$300,000. I could buy an excess policy that would add an additional million or more dollars.

An umbrella policy raises the limits over *all* your other liability policies, not just one policy. It can even broaden out to pick coverage for liability risks where there's no underlying coverage.

Umbrella and excess policies tend not to follow a standard type policy. Don't let the names fool you; some insurance companies come up with colorful names for these products.

* **Tip.** Protect your business better with an umbrella liability policy or excess liability policies.

WORKERS COMPENSATION AND ITS FRIEND, EMPLOYERS LIABILITY: THE GREAT NO FAULT CHANGE

The dawn of the industrial age brought a wave of job-related accidents to workers. Workers had a right to sue their employer for on-the-job injuries. The employer had three common law defenses to a worker's claim for compensation. These defenses—contributory negligence, assumption of risk, and fellow servant doctrine—effectively blocked an employee from successfully recovering medical expenses and related damages.

The early 1900s saw interest grow in a system that would compensate injured employees without question of fault. The employee would be compensated and the family would gather the death and disablement benefits. Rather than a federal system for all workers, individual states created their own separate systems. The federal government also developed a separate system for certain classes of workers.

The idea was for Workers Compensation to be an exclusive, no-fault system. However, employers still found themselves involved in litigation with employees. Today an employer is generally mandated to carry the following:

- Workers Compensation coverage
- Employers Liability coverage
- in most cases, Employment Practices Liability (EPLI).

EPLI is part two of the Workers Compensation policy. It covers situations where an injured employee can sue the employer in spite of Comp benefit eligibility. EPLI is for wrongful termination and mishandling of employee relationships, as we will see in the next chapter.

How Does Workers Comp Work?

Since each state has its own Comp system, programs differ. A few states require Comp be bought from the state. Other states sell Comp in competition with private insurance companies. Benefit amounts can vary widely from state to state.

A state may have a provision to exclude an employer with three or fewer employees from the Workers Compensation system. Other common exclusions from Comp are domestic, agricultural and casual employees.

Employees not requiring coverage under Workers Comp can be covered under a Voluntary Compensation Endorsement. This applies in many states. Care must be used in seeing that leased employees are properly covered because of their unique work relationship.

One idea lately has been to merge Comp with health and disability insurance programs. This hasn't been too popular. But if accepted, it would give 24/7 worker coverage. Another idea is for employers to opt out of the Comp system, yet maintain responsibility in some way for workers compensation.

The Policy: In Detail

A workers compensation policy includes insured statements, defense provisions, other insurance provisions, and similar insurance policy items.

One unusual feature is the policy language. This is what ties the insurance company's payment responsibility to state law. Part one of the policy agrees to pay the mandatory benefits required by law. This policy part has no limit on the amount the insurer will pay in Comp benefits. Comp benefits are unlimited.

Comp coverage is extended to bodily injury by accident and bodily injury by disease. The latter coverage has been an important factor in occupational diseases like black lung and more recently, carpal tunnel syndrome. The injury or disease must result from being on-the-job. Over the years, people have disagreed as to what constitutes on the job. Certainly a truck driver making deliveries is on the job. But how about the employee picking up a tool on his way to work in his own car?

Who is insured presents some problems. The named insured may be a corporation, partnership, sole proprietorship or other form of business organization. Being a named insured does *not* mean one is entitled to collect Comp benefits. Depending on the state, executive officers of a corporation may be covered for Comp benefits or they may elect out of eligibility. Generally, partners and sole proprietors are not covered for Comp benefits, but may elect to be covered.

* **Tip.** If you personally have a choice, carefully consider the potential benefits of choosing Comp coverage.

Worker's Comp: Benefits

What are the benefits for employees who suffer an occupational injury or disease? The five main types of benefits are:

1. Unlimited medical care
2. Disability income

3. Death benefit
4. Income benefits for survivors
5. Rehabilitation services.

Coverage Territory Or Item 3.A

On the information page of the Workers Compensation policy is the notorious item 3.A. (The Information page serves the same purposes of a Declarations page in other policies.) ONLY states listed in 3.A have Comp coverage. Claims filed in other states will not be covered. Be certain that all the states where you operate are listed. Notify your agent immediately when a new location is added.

What happens when an employee is hurt while attending a seminar in a state that is not listed or while crossing through a non-listed state? That employee may want the higher benefits paid in the other state and file for benefits there.

Here is the solution: Other states' insurance is now part three of the Comp policy and can be taken to provide Comp coverage. Other states' coverage is ONLY for incidental risks, not for states where the insured has operations.

A Few Other Comp Matters

Comp claims from illegally employed persons can affect the coverage of the Workers Compensation and Employers liability policy. Avoid employment of minors and undocumented aliens or you can lose your coverage. The rules vary from state to state. Verify that persons you hire are qualified to work in the way you intend.

H Example. In some states, minors are restricted from operating power-driven machinery. What's the age of a minor in your state? Check it out or ask your agent.

If your company has an operation in one of the monopolistic states (currently North Dakota, Ohio, Washington, West Virginia, and Wyoming) it must buy Comp insurance from the state. This will NOT include Employers Liability part two coverage. The way around this is to buy Stop Gap coverage. It does not provide Comp. It only covers those claims that arise under Employers Liability Claims. We'll see that in a minute.

Foreign Compensation is an important Comp policy addition. It provides Comp-like coverage for employees traveling on business or working outside the country. It can also provide coverage for endemic disease (one particular to a foreign country) and repatriation (the expensive return of a sick employee to the U.S.)

The federal government has a number of Workers Compensation and Employers Liability laws concerned with special groups or occupations. If your business is involved with coal mines, agricultural workers, or those working around navigable waters or on ships, you have special Comp coverage problems.

Holes In The No-Fault Concept

The idea of workers compensation as an exclusive, no-fault way for an injured employee to be compensated has been to the benefit of thousands of employees and their families. However, Comp did not remove all sources of employee liability claims for the employer. The majority of such claims would not find coverage under a CGL policy because of employee exclusions. Employers Liability, Part two of the Workers Compensation Policy, to the rescue!

Part two offers protection against all claims not excluded. In addition, it sets out specific coverage for these four common types of employer liability claims:

- Consequential bodily injury claims
- Dual capacity claims
- Loss of consortium claims
- Third-party-over claims

Consequential bodily injury claims are when a family member becomes ill because the employee was injured, as in a spouse having a nervous breakdown caused by the employee-spouse being totally disabled.

Dual capacity is the idea of bringing a claim against the employer, not as the employer, but possibly as the building owner where the work site is located. In other words, the employer was negligent as the building owner, not as the employer.

Loss of consortium is losing the services of a spouse or parent.

Third-party-over claims concern an injured employee suing a third party, who in turn sues the worker's employer.

H Example. Say a third party's delivery person injures your employee. That employee sues the delivery company. Then the delivery company sues you, saying your delivery platform was the cause of the accident. That's third-party-over.

An employer may also be sued when there is no workers compensation available to the injured employee. Perhaps the employee is an uncovered farm laborer or domestic worker. Another common employers liability claim is when the employer has too few employees to require Comp coverage.

Employers Liability: More Limits

Employers Liability coverage does not allow for an employee to recover twice for the same injury or occupational disease. It may appear, for example, an employee can collect damages from a third party and also collect Comp under his employer's policy. Not so, as a provision is made to correct a double recovery situation.

Employers Liability protection is limited to injuries or occupational disease during employment just like Comp. The CGL and other liability policies must complete the jigsaw puzzle of liability insurance coverage for an employer.

* **Tip.** Workers compensation is one insurance coverage where an ounce of prevention can save many premium dollars.

How To Reduce Comp Costs

Risk Management is about reducing the potential for your business to be hit with unexpected financial losses. It goes beyond just using insurance to guard against unexpected claims and losses. We could say Risk Management is a specialized form of management. You don't have to be a specialist or even trained in Risk Management to apply it to your firm.

Tool Kit: Risk Management

Two important tools risk managers use are *loss prevention* and *loss reduction*. Both these tools work exceedingly well in the workers comp arena. As an illustration, take the requirement of the Workers Compensation policy that you

must pay certain charges in excess of the regular comp benefits. These penalty amounts occur when your firm:

- is guilty of serious and willful misconduct
- employs a worker in violation of law
- fails to comply with health or safety regulations
- discharges, coerces, or discriminates against a worker in violation of comp law.

Any of these can be reduced through loss prevention. All management and supervisors should be trained to avoid these mistakes. There should be systems for handling comp cases correctly.

Loss reduction is a plan to handle on-the-job injuries. There are a variety of reduction measures including:

- providing first aid training for employees
- keeping on hand special medical equipment
- having arrangements with a local emergency medical facility to handle employee injuries.

Experts today talk of creating a *safety culture* in a business. The thought is to make every employee safety conscious. There are literally thousands of video tapes, posters, books and speakers that offer safety information.

* **Tip.** Effective safety efforts reduce problems for employees and their families. AND they can reduce your business premiums for Comp insurance. Don't overlook them.

Safety Reflects Premiums

Workers Compensation is one line of insurance where a good loss ratio can pay off in reduced premiums. It would

not be surprising if your comp premiums are subject to some form of *experience rating*. Experience rating is where premiums are adjusted at the start of a policy period by comparing past losses with the coming year's expected losses.

Retrospective rating is where the premium is adjusted at the end of a policy period. You get this by comparing expected losses with what happened during the policy period. So you receive the immediate benefits of an improved safety record.

EPLI: THE NEW KID ON THE BLOCK

The 1990s saw a great Internet boom. There was also an explosion in employment-related claims and lawsuits. Remember the Anita Hill-Clarence Thomas harassment case?

As the claims increased, so did efforts to find coverage for employment-related claims under existing policies. This included CGL. These efforts were not very successful. The insurance industry's answer was to develop employment practices liability insurance (EPLI). New insurance coverage often encourages more claims. In contrast, EPLI has *reduced* the number of charges made against employers. This is due to an awareness of employment-related problems and the efforts to control them.

Insurance companies have tried combination policies before. Insurers joined EPLI to Directors and Officers Liability policies. But this did not become the common approach to employers practices insurance. The trend went to separate policies. This included Employment-Related Practices Liability coverage from ISO. This can be used with your firm's Comprehensive General Liability policy. Endorsements have been offered to add EPLI to certain Business Owners Policies.

If there is a coverage trend today, it leans towards a *management liability* policy. This includes:

- Directors and officers coverage
- professional liability
- merger & acquisition coverage
- EPLI.

Today you'll either have the ISO coverage form or a separate EPLI policy.

Just What Are Employment-Related Practices?

EPLI covers the following:

- acts of wrongful termination
- demotion
- negative evaluation
- discrimination based on factors such as sex, race, and religion.

These risks are usually preventable through management risk control efforts. Insurance companies offer risk management help. They can train management and employees to prevent poor employment practices.

* **Tip.** Compare EPLI policies for inclusion of the employment practices you want covered by insurance. In today's market the available EPLI policies vary widely in the covered practices

An EPLI policy probably will exclude:

- civil or criminal fines
- fraud
- malicious acts or omissions
- Workers Compensation situations, and
- Americans with Disability Act problems (often).

If ADA problems are covered, the costs of creating proper conditions for the disabled *won't* be covered.

Unusual Features Of EPLI

Defense costs may or may not be covered by EPLI. The ISO coverage form provides for a Co-Payment feature. This requires the insured to pay a percentage share of defense costs. You can find this feature on the Declaration page. In some policies, the defense costs are included in the policy dollar limits. This reduces the dollars available for claim payments.

* **Tip.** Defense costs can accumulate quickly. Consider how your policy covers them.

A deductible is a common EPLI feature. Deductibles, co-payments and similar devices encourage employers to work on loss prevention.

Another area of concern is “who is insured.” The firm’s covered, no question. But the stockholders or the general run of employees? Not as likely. The Directors and Officers policy *may* cover stockholders. Non-supervisor or manager types are on their own if sued. However, it is possible to cover stockholders and general employees. How? Use an endorsement.

You already know that EPLI policies are “claims made” policies. So pay careful attention to the extended reporting period allowed for reporting claims. A short period can be built in an EPLI policy. You also have the opportunity to buy a longer time period for reporting.

Reduce Those Losses—For Good

We tend to think of insurance in relationship to ourselves and our risk problems. However, insurance also has an

The Circle of Safety:
How to Protect Yourself and Your Business with Today's Insurance

impact on society. EPLI has played a significant role in encouraging employers to apply loss prevention to employer practices. These efforts have created an awareness of poor practices. In turn, this has helped reduce claims.

Employment practices' training is available from insurance companies. Don't overlook them! Better employment practices create a better work environment.

CRIME, FIDELITY & A LITTLE SURETY

Crime is a simple word for a multitude of dishonest acts. Crimes range from a simple street robbery to a safe burglary to a kidnapping. These definitions may help our look at crime insurance:

- **Burglary**—entering and leaving a premises with no legal right
- **Robbery**—taking property from a person by threat of physical or mental harm
- **Theft**—a catch-all category including the terms above
- **Extortion**—surrender of property by threat to of physical or mental harm to a person or related third party
- **Embezzlement**—theft of others’ property in your care

Before you buy crime insurance, review the coverage in your existing property insurance policies. Is your property insurance policy on a name peril basis? Or is it on an “everything is covered *except*” basis? It makes a difference! If it’s a name peril, your need for separate crime insurance is likely to be important.

Crime insurance covers a broad range of activity:

- robbery
- burglary
- theft
- disappearance and destruction

- fraud
- forgery
- embezzlement.

The available insurance coverage is divided into a number of areas. These cover only specific types of crimes. Make sure you and your agent consider your particular exposures to crime. Some businesses need coverage for outside sign theft. Other businesses require coverage for safe burglary. Others require only employee honesty coverage.

Some crime coverage may be available in other insurance policies. For example, kidnapping can be part of a Directors and Officers policy.

What Are Fidelity & Surety?

Fidelity protects against loss from the dishonest or fraudulent acts of employees. Surety refers to the activity of bonding a person or persons. A surety bond provides for monetary compensation if the bonded person or organization fails to perform in a correct manner. Bonds are very common. Regular bonding is required of some firms such as contractors. There are fiduciary bonds, license bonds, permit bonds among others.

* **Tip.** The most trusted employee may turn to crime. How? Under the pressure of family money draining illness or serious money problems. Crime may not pay, but insurance does.

ISO and the Surety Association of America (SAA) both offer fidelity protection against employee criminal acts. We'll use ISO's crime program as a basis here.

Do I Need A Separate Crime Policy?

Your business needs crime insurance if:

- its property insurance doesn't offer crime coverage.
- if a significant amount of money or securities passes through its hands.
- if any employees have the opportunity to steal large amounts of money or valuable property.

Crime Insurance: Forms

Remember “claims made” policies? Crime insurance has a similar *discovery* form. A *loss sustained* form accompanies this.

Why two forms? Because employee-related crimes are *silent* crimes. Silent crimes are ones that may take place over a long period of time. They're often difficult to discover. The discovery form covers you for undiscovered employee crimes, even if they occurred before the policy began.

The ISO program allows crime coverage to be a separate crime policy. Or it can be a coverage part to join your other property coverage. Seven types of crime coverage are offered. You may take one, several, or all seven. The seven are:

1. Employee Theft
2. Forgery or Alteration
3. Inside the Premises - Theft of Money & Securities
4. Inside the Premises - Robbery or Safe Burglary of Other Property
5. Outside the Premises

6. Computer Fraud

7. Money Orders and Counterfeit Paper Currency

Employee Theft covers loss or damage to money, securities and other property. You're covered whether an employee acted alone or with others.

Forgery or Alteration covers checks, drafts, promissory notes and similar items regarding the payment of a sum of money. The insurer pays your defense costs in *addition* to the dollar limits of your coverage.

Inside the Premises - Theft of Money & Securities covers theft, disappearance and destruction. Damage to the premises caused by an actual or attempted theft is covered. So is loss or damage to a locked safe, vault, cash register, cash box or cash drawer. Vandalism, if not related to a theft attempt, is excluded.

Inside the Premises - Robbery or Safe Burglary of Other Property. Damage is covered here as in the above coverage. The key to coverage here is *other property*. Nearly any tangible property is covered. This includes a piece of jewelry, a gun, a computer part, etc. This coverage meshes tangible property with the intangible property (above).

Outside the Premises protects money and securities in the hands of a messenger or an armored car service. The perils are theft, disappearance, or destruction. Property other than money and securities is covered only if the loss or damage results from an actual theft or attempted robbery.

Computer Fraud coverage fits money and securities coverage to the new financial world. Losses are paid when a computer is used to fraudulently transfer money, securities, and other property from your premises to a person or place

outside your premises. This is NOT computer insurance; it is fraud insurance.

Money Orders and Counterfeit Paper Currency protects your acceptance of such items in good faith *in exchange* for merchandise or services.

These explanations of the seven crime coverages are short and simple. In truth, they are subject to many conditions, exclusions, definitions, etc.

* **Tip.** Pick through the seven for the ones most fitting for your business. Discuss with your agent how they will work for your firm's protection.

Who Is An Employee?

An *employee*, under Crime coverage, must be a natural person. A business organization is not an employee. Generally the right to control and to direct a person makes a person an employee.

For our purposes, an "employee" may also be a former employee who commits a wrongful act immediately after being let go. Managers are employees acting within the scope of their employment. Temporary workers are considered employees. Leased employees are not. Executive officers may or may not be employees for coverage purposes.

There are three ways to place employees under a Crime policy: as individuals, by position, or as groups of employees under blanket coverage. These are referred to as a name schedule, a position schedule, or a blanket schedule. Which schedule you would use depends on the employees you want covered.

The Circle of Safety:
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Crime insurance has a wealth of endorsements used to modify the basic coverage. It takes a great deal of study on an insurance agent's part to set Crime coverage up properly.

POSTSCRIPT

A well thought out insurance program for your business boils down to a knowledgeable agent. This is a person who will take the time to understand your company and its insurance needs. No one vehicle meets the needs of every driver and no one set of insurance policies fits every operation. You are unique.

An agent develops insurance knowledge in a number of ways. It may come through experience, college studies, self-study, industry programs, or designation programs. An agent may hold designations such as the traditional CIC, CPCU, and CLU. There are also a number of other designations available. Some agents hold over a dozen insurance and financial designations.

Designations are a fine sign that an agent has devoted time and effort to learning more about the insurance field. To us it's more important that you have an agent you trust and have confidence in. Membership in organizations like the National Society of Agents for Consumer Education (NSACE) indicates an agent who is not in the business just for the bucks. Those agents see themselves as serving you and your firm.

Going for the cheapest quote when there is a choice between two insurance companies may sound like the best deal. Watch out—it may be a poor choice! Don't take for granted that the insurance company is solid financially and gives good service on claims and other matters. Insurance agencies have the resources and contact to aid in checking on an insurer.

A rewarding relationship can come from working with a competent agent.