

# Come On Baby, Light My Fire

## (so I can collect on my insurance policy)



Until recently, I had very little knowledge, experience or even interest in property and casualty insurance. I, like many business owners, simply trust my insurance agent to do their job by providing me with adequate insurance coverage against a potential loss. My whole attitude changed when a client's music store burned to the ground due to arson caused by a burglar. Since then, our accounting firm has been thrust into the arduous task of calculating loss damages for three of our clients. All three were retailers, all three had a complete property loss from their fire, and all three were living nightmares for their owners.

Accordingly, I thought I'd share some of the things I learned the hard way about business insurance and the agents and insurance companies you're led to believe are your friends. If you think there's a sarcastic tone at the end of that last sentence, you're absolutely right. If you think there are various Doors / Jim Morrison references in this article,

you are again correct. And if you think The Doors and property casualty insurance have a lot in common, well—I guess they do now.

### Hello I Love You, Let Me Sell You Insurance

Life is full of surprises: some good, some bad. A tornado may drop a bag of money in your store's parking lot, but it's probably more likely to drop a tree on your roof. These unexpected and unpleasant events—like structural damage from an earthquake, medical expenses for a work-related injury to an employee or water damage from flooding—are the typical risks we often choose to insure ourselves against.

By paying an insurance premium, we avoid most of the economic impact (known as a "loss" in the insurance industry) from such unfortunate events. When you cut through the mumbo jumbo of any insurance policy, you basically have this: In exchange for premium payments, the insurance company

promises to pay you, the insured, a specified sum of money upon the happening of a covered economic loss.

Every business owner must weigh the cost of insuring against a variety of risks against the economic impact of an uninsured loss. Unfortunately, insurance premiums can make a substantial dent in any business budget. So let's discuss why insurance is important, what types of insurance you need, how much insurance you need and the things you can do to minimize your risk of loss and related insurance premium cost.

### Break on Through to My Checkbook

Many business owners view insurance as a luxury they really can't afford. Given the constant pressures of shrinking margins, increasing payroll and other drains on cash flow, many retailers feel compelled to cut back or eliminate insurance from their budget. They go forward thinking, "If I get robbed or my water pipes burst, I'll deal with it then. I'd rather spend money on what I know will happen, rather than something that probably won't happen."

To some degree they're right. Cash flow is easily impaired by paying big insurance premiums to insulate against property losses that'll probably never happen. But there are other potential losses that have a greater likelihood of happening, like product liability damage that arises in the form of a lawsuit. In any event, if you understand the importance of insurance to your business, you can then better determine the type of insurance you need and how much. But don't forget that a large, uninsured loss could threaten both the continued operation of the business as well as the owner's financial well-being.

## Insurance Riders on the Storm

Clearly, the most common form of business insurance is the business owner's general liability policy. Like a comprehensive home owner's policy, a business owner's general liability policy protects against economic losses caused by (a) damage to the owner's property and (b) legal liability to others for bodily injury and property damage involving the business.

But there's additional coverage, or "riders," that you can (and probably should) add to your business owner's policy. For an additional premium cost, you can add coverage for (1) income lost as a result of a loss to business property (like from a fire) and (2) litigation losses stemming from product liability. Lost income coverage is important as it provides funds to pay key operating expenses while the business is non-operational. This, in turn, allows you to keep your employees gainfully employed while the store is rebuilt after a catastrophic event, for example. Product liability coverage is also important, as a music retailer can be sued if a customer is injured using the product they were sold. This can happen even though the retailer had nothing to do with the product design or manufacture.

A business owner's general liability policy is often the most economical way to protect against a broad range of risks that may befall your business. This type of policy is available for many specified types of lower-risk small businesses (such as retail shops and professional offices). However, if for some reason your store does not qualify for a business owner's policy, you'll need a commercial policy, which is usually way more expensive. Since obtaining adequate coverage in a commercial policy depends on identifying and insuring against specific risks, your selection of an insurance agent becomes much more important. Therefore, it's vital that your agent is familiar with your type of business, as well as knowledgeable about the commercial

policies available.

## Love Me Two Times & Charge Me Twice Today

Once you have determined the type of insurance you need, you must then accurately assess how much insurance you need. Too little insurance can leave you vulnerable. On the other hand, paying \$500 a year for theft insurance on a company vehicle with a book value of only \$1,000 will drain cash from your business and get you very little protection in return. Accordingly, here's some general guidelines in determining how much insurance you need for both property and liability:

**Know your lender's limits.** If you've borrowed money from a bank or other commercial lender, you usually must maintain a certain level of insurance in accordance with the loan agreement. Failure to do so will give the lender the right to seize your property, or purchase its own insurance on the property and charge you a ridiculous price for it.

**Know the value of your property.** There are really two "values" to a piece of property. The first is what you paid for it. The second value is what it would cost to replace the property if it was lost to fire, theft or other unfortunate circumstances. If your business can't operate without the property in question, you probably need to insure the property for its replacement value. This will often cost more than insuring the property for its actual value, so think twice before you start insuring everything at replacement value.

**Know the legal minimums.** Ask your insurance agent whether there are any minimum insurance levels set by law. You must purchase at least this amount of insurance, although it's usually not enough.

**Know your business form.** Look at the structure of your business. If your business is incorporated or is a limited liability company, you can probably get away with buying insurance with lower limits. In the event you're sued and lose,

only the assets of the company may be seized to satisfy a judgment. On the other hand, if you're a sole proprietorship or general partnership, you'll generally need more liability insurance, as you can be held personally responsible for any judgments against your business.

**Know your people.** This includes knowing both your employees and yourself. Is your business staffed with highly skilled professionals with years of experience or with high school kids? Are you, or any of your employees, accident prone? Consider these factors when you decide how much liability insurance to buy.

Following these steps should help limit your insurance coverage to what you need. However, if the quotes from your agent still seem too high, or if you've been told that certain aspects of your business are uninsurable, you may wish to explore some alternatives to insurance.

## People Are Strange

These days, as everyone seems to be suing everyone else, insurance premiums continue to soar. Fearing the exposure of litigation, some insurance companies actually refuse to make certain types of insurance available to businesses. So in most cases you have insurance you can barely afford, and in some cases you need insurance you can't get. What do you do?

One solution is to "self-insure," which is simply to start saving a pile of money to protect you in the event of a loss or catastrophe. But bear in mind that some types of insurance are required as a matter of law (i.e. auto insurance), and other types may be so important that you shouldn't be conducting business if you can't afford it or can't get it.

Perhaps a better solution to soaring insurance premiums is to simply reduce risks. Let me explain.

## Roadhouse Blues

The following are just a few things you can do to minimize risks, there-

by lowering the amount of insurance needed back at the roadhouse:

**Burglary Protection.** Protecting your office and store equipment as well as your employees' property from vandals and thieves can lower your risk of burglary. The use of door and window locks, key control, lighting, timers and alarm systems are just a few of the many ways to safeguard your business property.

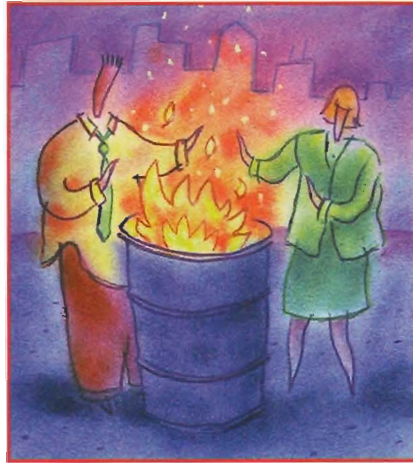
**Theft Protection.** Embezzlement happens every day to small business owners, especially those who don't take precautions to prevent it. The best ways to combat embezzlement are to recognize the warning signs (like increases in sales returns, bad-debt write-offs, bounced checks and inventory shrinkage) as well as establish good internal controls (like screening applicants before they're hired, having two people sign checks and dividing financial responsibilities).

**Bonding Employees.** Even if you have internal controls that make embezzlement difficult, the danger of collusion still exists. Consequently, some companies protect themselves from employee dishonesty by bonding their employees. Bonding can cover losses from larceny, theft, embezzlement, forgery, misappropriation and many other fraudulent or dishonest acts committed by an employee, alone or in collusion with others.

**Create a Safe Workplace.** Workplace accidents can destroy your business. Thousands of Americans are killed each year in on-the-job accidents, and many more suffer from work-related disabilities or occupational illnesses. Besides the incalculable cost of pain and grief, there are high monetary costs attached to workplace accidents. These costs can include the wages paid to sick and disabled workers, wages paid to substitute employees, workers' compensation claims and increased insurance premiums, to name a few. Accordingly, keep your workplace clean and organized. Don't

stack inventory in piles that can topple, and don't create a jungle of cables and power cords that people can trip over.

**Have a Backup Plan.** Assume for the moment that your store is completely destroyed. Consider the items that would be important to your business and those that



would have to be recreated from scratch in order to continue. Typically, the most critical items are business records; so backup your computer data daily. Consider keeping backup disks off-site or in a secure place, such as a bank vault.

### The Lizard Kings (an Editorial)

Earlier in this article I made a snide remark about the "friendly" nature of insurance agents and insurance companies. While it appears to me that some insurance agents are your best friends when writing a policy and your worst enemies when processing a claim, it would be unfair of me to stereotype these individuals as used car salespeople. The insurance companies, on the other hand, are the true lizard kings. I have an extreme distaste for the three insurance carriers I had to deal with as a result of the fire losses sustained by all three of our aforementioned clients. The grief they received from their respective insurance carriers at the most traumatic time in their lives was unconscionable.

While I can appreciate the increasing tide of insurance fraud,

especially from arson, it seems grossly unfair to treat insureds as "guilty until proven innocent." Although these are strictly my opinions based on my experiences, I feel it important to alert you, the policyholders, of practices by some insurance companies to reduce claims payouts.

So, what can you do? Two simple, but important, things: (1) Make sure you completely understand your insurance policy, what you're covered for and what you're not, and (2) keep detailed accounting records, financial statements and tax returns that support the cost of assets lost in catastrophic events.

Don't assume anything in your business insurance policy. I once saw "inventory" defined in an insurance policy to include store fixtures, office equipment and leasehold improvements! So when our client initially thought he was getting paid the policy maximum of \$500,000 for just the inventory lost in his fire, he in fact received nothing for the store's fixed assets. To make matters worse, they didn't receive the insurance proceeds promised in their policy for seasonal increases in inventory. Why? Because they couldn't support their claim with adequate accounting records.

### This Is the End

The stories can go on and on. Don't be one of them. Make your insurance agent explain all the provisions of your policy and make sure you both understand them. Otherwise you might have to touch me on some strange days waiting for the sun on a ship of fools (as a true Doors fan, I especially like the "touch me" part).



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