

Insure Wisely When Expanding or Relocating

By Thomas McMahon, CPCU,
Managing Director of Commercial Sales; Cook, Hall & Hyde, Inc.

THERE ARE SEVERAL events that may require an adjustment to your property coverage. Most business owners know they need to update their coverage when moving to a new location or acquiring an additional location. Many fail, however, to recognize other circumstances that should prompt them to update their insurance. For example, they may fail to change their coverage when they replace old equipment or add additional production capacity. Understanding these other needs and updating coverage accordingly is critical for any changing business.

Property coverage is one of the most important parts of any manufacturer's insurance program. This coverage protects the assets used to generate their income. An inadequately insured loss to their buildings or means of production can place the company's future in jeopardy.

The key to any property insurance program is the accurate valuation of the real and personal property as well as the business income. Maintaining appropriate insurance to value is essential to assuring that there will be adequate funds available in the event of a loss, in order to replace damaged property or lost income. It is additionally important to understand that the increased value of the new equipment can create a gap between a business' current coverage limits and the actual coverage needed. The result can be a penalty applied in the event of a partial loss, or inadequate coverage to replace all the damaged property in the event of a total loss.

Most insurance policies cover property on a replacement cost basis. This form replaces old property with new without applying any depreciation. While this valuation will provide adequate funds to replace older property with new, the insurance coverage must be set at a level that reflects this higher replacement cost. If the property limit instead reflects the depreciated value carried on the corporate balance sheet, the insurance will not be sufficient to replace the damaged building or equipment.

Another factor to be considered is what is known as "demand surge." This is the increase in prices that occurs

after a catastrophic loss — a hurricane, for example — where there can be widespread demand and resulting shortages in building materials. A good property program should make allowance for this as well.

Business income is an often overlooked and undervalued coverage. It provides for replacement of lost earnings during the period in which operations are shut down (or continued at a reduced level) due to an insured loss to real and/or personal property. Without adequate business income coverage, the company may not have the funds to pay the increased costs necessary to continue operations during the period of repairs. Even worse, the company may be left with inadequate capital to resume operations after the premises are repaired. To assure that adequate business income coverage is maintained, a business income worksheet should be completed annually. This worksheet will point out exposures that need to be considered in establishing the needed level of business income coverage. With manufacturers, it is critical to determine how long operations will be interrupted or reduced if equipment is damaged or destroyed. Often, this is dependent on how long it will take to get new machinery, particularly if it involves specialized equipment or machinery made overseas.

Maintaining adequate insurance coverage takes some work, but it is time well spent in the event of a loss to your manufacturing facility.

Thomas McMahon, CPCU is managing director of commercial sales for Cook, Hall & Hyde, Inc., a diversified insurance and risk management organization with offices in New York and New Jersey. He can be reached at (631) 390-9716 or tgmcmahon@chhins.com.

