FAQs on Business Interruption Insurance

What is Business Interruption (BI) Insurance?

Business interruption coverage is generally part of a commercial (business) property and casualty insurance policy that protects policyholders against covered events that may disrupt their businesses. Typically, BI coverage is not sold on a standalone basis; instead, it is added to a property insurance policy or included in a package policy. All insurance policies, including BI insurance policies, require that coverage of a specific risk is purchased before a loss occurs. This allows for the appropriate level of premium to be collected prior to a covered event.

What does BI insurance cover?

Business interruption insurance compensates businesses for lost income resulting from property damage caused by covered events specified in the policy. These covered events usually include fire, hurricanes, or tornadoes. Business interruption insurance typically covers the business's lost revenue as determined by an analysis of financial records. The policy also covers operating expenses, like payroll and utilities, that continue even though business activities have temporarily ceased.

Why do BI policies typically exclude coverage for pandemics?

Business insurance policies, including BI insurance, generally provide coverage only where there is a covered cause of loss, i.e. an accidental direct physical loss to covered property. Viruses, bacteria, and pandemics are not typically a covered cause of loss and are typically excluded from policies. Due to the widespread nature of the risk, these events are fundamentally uninsurable. Additionally, viral spread is not generally considered an accidental direct physical loss to covered property. In a recent letter to Congress, the NAIC said it best: "Insurance works well and remains affordable when a relatively small number of claims are spread across a broader group, and therefore it is not typically well suited for a global pandemic where virtually every policyholder suffers significant losses at the same time for an extended period."

Insurers charge policyholders premiums based on an actuarial assessment of risk in order to cover the risk of loss. Insurers then reserve and hold capital against losses. As with all insurance products, the premium collected has to cover the estimated amount of claims payments. With the likelihood of near universal claims, BI coverage for pandemics would be unaffordable and no longer useful as a risk pooling mechanism.

Why not retroactively mandate coverage of pandemic-related BI losses?

In addition to governmental efforts already underway, some stakeholders have suggested insurers should be required to support businesses impacted by COVID-19 by paying out business interruption claims for pandemic-related losses, regardless of whether the policy language covers such losses. While the devastation caused by COVID-19 urgently demands a

response, a retroactive mandate would violate fundamental legal principles and cause serious unintended consequences.

Insurance is a legally binding contractual relationship between two parties who both agree to perform specific obligations. In the case of BI coverage, this means the policyholder agrees to pay the insurance company a premium, and the insurance company agrees to pay the policyholder if certain covered events interfere with the business's operation. The amount owed by the policyholder is actuarially determined so that the insurance company collects enough money to cover potential losses. Events like pandemics, which are typically excluded from BI coverage, are not priced into the contract—meaning the policyholder has not agreed to pay for pandemic-related BI coverage, and the insurer has not agreed to cover those potential losses. Insurers stand ready to pay all claims related to specified events covered by a policy. It's imperative that consumers and insurers can rely on contract terms that have been agreed to, approved by regulators, and repeatedly tested in courts.

Retroactively mandating coverage for a known risk for which an insurer did not underwrite or collect premiums would have a devastating effect on the industry and the economy. It has been estimated that small business losses caused by COVID-19 are between $255-$431 billion per month. This would exhaust industry surpluses designated to pay all property/casualty claims (including homeowners and auto policies) in just two months. This doesn't mean insurers aren’t well capitalized—it simply highlights that the industry isn’t in the financial position to pay for significant and widespread losses that aren’t insured. To further display the extreme magnitude of the crisis, the 2005 hurricane season resulted in the industry processing the most claims ever handled in one year—three million. Small businesses that suffered coronavirus-related losses could produce as many as 30 million claims—ten times the standing record.

A stable federal government is the only entity capable of handling the fallout from a pandemic crisis like the one we're all living through. Mandating insurance coverage sets a concerning legal precedent that undermines the nature of contracts while jeopardizing the industry's solvency.

What is the government doing to help small businesses?

Families across the country are suffering devastating losses because of COVID-19 related closures. The numbers are staggering. In addition to $300 billion in direct relief for individuals, the federal government established the $350 billion Paycheck Protection Program (PPP) via the CARES Act to provide small businesses with low-interest loans that convert to grants when used for certain purposes such as payroll. With the PPP expected to quickly need at least an additional $250 billion in funding to meet the needs of small businesses, this disaster has made clear that the federal government is the only entity equipped to respond to a pandemic-induced crisis.