

Business Interruption

Guideline for sum insured calculation



SINCE
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This guideline has been prepared by Safire in order to assist its policyholders in calculating the sum insured that they require for their business interruption cover. It does not replace or override any policy schedule or policy wording, or any advice provided to a policyholder by its accountant or auditor.

Client name

Policy number

Important note: A claim must first be payable under the **Fire, Buildings Combined** or **Office Contents** section of the policy before the Business Interruption section will respond. If you have selected the Loss of Profits following Mechanical Breakdown extension, the same calculation as set out below will apply. However, a different indemnity period, taking into account how long the relevant machinery will be out of commission, may need to be considered. (Note: for this purpose, Loss of Profits means the same as Business Interruption).

The following should be provided for in the sum insured, under a Business Interruption (BI) insurance section:

- **PROFIT** that would have been earned during the interruption period; and,
- **FIXED COSTS** which will be incurred by the Insured during the interruption period.

Business Interruption (BI) extensions:

Please note that there are extensions under the BI policy such as **“increased cost of working”**, which if included in the sum insured, will protect against additional and necessary costs that may be incurred during the interruption period to continue production (such as rental of additional property, additional transport costs etc.).

Please discuss **ALL** available BI policy extensions with your broker.

Please follow steps 1 to 5 detailed below in order to calculate the correct sum insured.

Step 1: Identification of the relevant 12-month period for projection of financial results (i.e. NEXT annual insurance cover period)

The objective of this step is to clarify which 12-month period needs to be projected, so as to ensure the adequacy of the BI sum insured.

In order to ensure that the BI sum insured takes into account future growth, inflation and trends you will need to project your current **audited / reviewed** financial results over the next TWO or THREE years.

A business interruption claim could occur on the last day of your current annual insurance cover period and extend into the **NEXT annual insurance cover period**. The financial projection therefore needs to extend to at least the end of your **NEXT annual insurance cover period**.

Date of your last audited / reviewed financial year-end

(a)

dd / mm / yyyy

What is your **current annual insurance cover period**

(b)

dd / mm / yyyy

to

dd / mm / yyyy

Insure for your **NEXT annual insurance cover period** *

(c)

dd / mm / yyyy

to

dd / mm / yyyy

* i.e. 12-month period after the expiry of your **current annual insurance cover period**. The intention of this guideline is to ensure that you project your turnover (and sum insured) for the correct annual period.



Step 2: Calculate the Insurable Rate of Gross Profit (IROGP) – difference basis

Calculate the IROGP, using your latest **audited / reviewed** financial statements.

The objective of this step, using audited information, is to exclude variable costs (which would not be insured in the event of a claim) from turnover.

The resultant net figure, i.e. Turnover less variable costs, will equate to profit plus fixed costs, which is the **Insurable Gross Profit**.

Latest audited Turnover		(d)	<input style="width: 95%;" type="text"/>
Plus:	Closing stock		<input style="width: 95%;" type="text"/>
Equals	Sum of Turnover and Closing stock	(e)	<input style="width: 95%;" type="text"/>
	Opening Stock		<input style="width: 95%;" type="text"/>
Plus:	Purchases (Purchases in respect of Cost of Sales)		<input style="width: 95%;" type="text"/>
Plus:	Transport		<input style="width: 95%;" type="text"/>
Plus:	Packaging		<input style="width: 95%;" type="text"/>
Plus:	Commission on Turnover		<input style="width: 95%;" type="text"/>
Plus:	Bad Debt		<input style="width: 95%;" type="text"/>
Plus:	Discounts Allowed (net of Discounts Received)		<input style="width: 95%;" type="text"/>
Plus:	Other Variable Costs, if any		<input style="width: 95%;" type="text"/>
Equals:	Sum of Opening stock and Variable costs	(f)	<input style="width: 95%;" type="text"/>
Insurable Gross Profit (IGP):	(e) minus (f) ** =	(g)	<input style="width: 95%;" type="text"/>
Insurable Rate of Gross Profit % (IROGP):	(g) divided by (d) =	(h)	<input style="width: 95%;" type="text"/>

- * **Variable costs:** 1) These costs are normally variable with Turnover, i.e. as Turnover reduces these costs will also reduce or may fall away completely. These costs are otherwise known as **uninsured costs (or uninsured working expenses)**. Please consider these carefully.
 2) These costs will **NOT** be insured in the event of a business interruption claim.

** **Insurable Gross Profit (IGP) and IROGP %:** These terms must not be confused with the strict accounting definition of 'gross profit' as the calculation is based on different inputs. IROGP is used to determine the value you should be insuring for.

WAGES

Please note that "**wages**" can be excluded from the **Insurable Gross Profit** calculation and insured separately for a shorter indemnity period. Please discuss this with your broker if it makes sense for your business.

Step 3: Calculate the projected turnover in your NEXT annual insurance cover period

Calculate the turnover in your **NEXT annual insurance cover period** by applying business growth trends.

The projected turnover must be based on the client's view of trends in their business. This trend can be flat, decreasing or increasing.

The objective of this step is to project turnover for an annual 12- month period that is expected in the **NEXT annual insurance cover period** from step 1.

Start with **latest audited / reviewed turnover** from step 2 (d)

Apply forecast assumptions for turnover:

Add: Expected growth (for one, two or three years as required) %

Amend for other assumptions that could influence future turnover (increasing or decreasing)

equals **Projected Turnover** for **NEXT annual insurance cover period** (i)

Step 4: Calculate sum insured

The objective of this step is to apply the **Insurable Rate of Gross Profit % (IROGP)** i.e. (g) calculated in step 2 (based on audited / reviewed figures) to **Projected Turnover** i.e. (h) as calculated in step 3, to arrive at the correct sum insured.

Projected Turnover NEXT annual insurance cover period (i)

Insurable Rate of Gross Profit % (IROGP) (h)

Sum Insured excl. VAT: (i) multiplied by (h)

Add: VAT @ 15%

Sum Insured incl. VAT (SI)

Step 5: Choose and apply the correct indemnity period to the Sum Insured (SI)

In this step you choose the applicable indemnity period that you want cover to apply for.

The indemnity period you choose should be based on the amount of time you expect it will take to rebuild your business in order to resume normal operations following a loss.

Indemnity period (how long to rebuild?) – 3, 6, 9, 12, **18, 24 months**

If the selected indemnity period is twelve months or less: Insure for full Sum Insured **including VAT** i.e. **(SI)** as calculated in step 4

If the selected indemnity period is **longer** than twelve months:

18 months: SI including VAT (from step 4) multiplied by **1.5**

24 months: SI including VAT (from step 4) multiplied by **2**

It is important to note that the sum insured **CANNOT** be reduced on a pro-rata basis for indemnity periods that are shorter than 12 months. If you select an indemnity period that is less than 12 months, a **lower premium rate** will be applied to the sum insured, by the insurer.

Client acknowledgement:

I / we acknowledge that this document is only a guideline and does not replace or override any of my / our sums insured or risks as set out in my/our policy schedule.

I / we understand that this guideline does not absolve me / us from having to ensure that the BI sum insured is accurate and sufficient for my/our risk profile. In this regard, I / we undertake to regularly review the BI sum insured and to communicate any changes that may be required, to my/our broker.

Signed at _____ on this _____ day of _____ 20____ .

Client

Auditor

Date

Date