# Insurance

## Glossary of Policy Types

The following descriptions provide an overview of some typical policies a business owner may consider. Policy terms and conditions vary. It is important to work closely with your insurance provider so that the insurance choices you make minimize any risks and losses that may occur in your business.

### Professional Liability Insurance/Errors & Omissions Coverage

If your firm provides a service rather than a product, you probably have a professional liability exposure. Examples of some industries that have this exposure include medical, legal, accounting, real estate, computer software development, and engineering firms. General liability does not provide professional liability coverage. A separate policy is required, although some miscellaneous industries such as pharmacy and optometry are provided coverage under the standard general liability policy. Professional liability policies are usually written on a "claims made" form rather than an "occurrence form" as are most general liability policies. NOTE: A commercial umbrella policy does not provide excess limits over a professional liability policy.

### Commercial Umbrella

An umbrella policy provides excess limits over any underlying policies that are scheduled on the umbrella policy declarations page. An umbrella policy differs from an excess liability policy in that the umbrella overlays all of your underlying policies. An excess liability policy is designed to provide higher limits for only a specifically identified policy. Most umbrella policies are classified as "following form". This means that the umbrella follows the form of the underlying policies. Therefore, anything that is excluded in an underlying policy will be excluded in the umbrella. For example, most general liability policies exclude professional liability exposures. Therefore, the umbrella would also exclude this coverage. NOTE: Always attempt to maintain concurrent renewal dates with your umbrella and underlying insurance. A gap in coverage could occur, if these renewal dates are not synonymous.

### General Liability

Your firm needs coverage to protect itself from bodily injury and property damage claims. Standardized sets of general liability codes have been developed that most insurance carriers use to rate your general liability premium. These codes give a basic description of your operations. For example, a water and sewer main construction company would have one code while a law firm would have another. Usually, these codes are rated on payroll, sales, or square footage of your office. Keep in mind that some carriers have developed their own set of GL codes to provide themselves a competitive advantage in specific industries. There are two parts to general liability: premises and operations coverage and products and completed operations coverage. Premises claims occur on your premises (for example, a person slips and falls in your store), while an operations claim refers to an accident that occurs during the course of your work (for example, your salesman knocks an expensive vase off a customer's desk while he is attempting to setup a product demonstration). Product liability claims refer to alleged injuries that occur because your product is inherently unsafe (silicon breast implants are an example). Complete operations claims refer to accidents that occur after you have completed your work. For example, an electrician makes an error in wiring a panel. A month later, an overload occurs because of the error causing a fire. Engineering design and build firms will often find that product liability and completed operations are excluded under their general liability policy as it is sometimes difficult to distinguish between a completed operations claim and a professional liability claim.

**Workers' Compensation**

This policy provides coverage for on-the-job injuries to your employees. Your firm is protected against other litigation related to the injury with this coverage in force. Workers' compensation is rated similarly to general liability in that each class of employees is identified by a unique code that should correspond with your general liability codes. Each code has a specific rate per $100 of payroll and is subject to audit at expiration.

**Property**

Your commercial property includes among other things: buildings, office equipment, manufacturing equipment, inventory, and work in progress. Always try to get the broadest coverage possible. Many carriers no longer use "all risk" terminology as property policies have a number of exclusions such as flood and earthquake. Quite a number of carriers are now offering endorsements that offer a broad range of additional coverages. Be sure to request selling price coverage for your finished goods in inventory. In a loss, these goods would then be covered at their sales price as opposed to the manufacturing cost. Property insurance only covers property on your premises. If an employee is taking equipment off site or if you are storing inventory at a job site, these items must be covered on a separate policy.

**Business Automobile Policy**

Vehicles titled in a company name must be covered under a business auto policy. Commercial autos are rated on the basis of their use and range of operation. Many policies do not provide automatic coverage for newly acquired vehicles so be certain that you schedule all vehicles as they are acquired. Even if you don't have any company owned vehicles, it is wise to obtain a policy that provides Hired and Nonowned liability coverage. This policy offers protection to your firm in the event an employee is involved in an accident while driving his or her vehicle on company time. For example, a salesperson could be involved in an accident that could ultimately lead to a suit against your firm. The employee's coverage is primary. The business auto policy only protects the firm and does not offer any coverage for the employee's vehicle. NOTE: Schedule all trailers on your business auto policy. Otherwise, there may be no coverage should a trailer come loose from one of your units and cause an accident.

**Business Income Policy**

This coverage acts like a disability income policy for your firm. The three most common forms of this coverage are 1) loss of rents, 2) business interruption, and 3) extra expense. Loss of rents coverage replaces the lost rental income from your damaged or destroyed property. For example, if three buildings in the apartment complex you own burn, this policy would replace your loss of rental income while the structures are being reconstructed. Business interruption replaces lost income if you are unable to produce goods for sale as your site is being reconstructed. An extended period of indemnity can be obtained to help replace income after operations have resumed as it may be difficult to immediately return to pre-accident revenue levels. Extra expense coverage provides cash to enable a firm to reestablish its operations in a more rapid fashion. For example, if you have a service business that does not require large amounts of fixed equipment to operate, with some extra money you could rent temporary space, computer equipment, and a telephone system. In a short amount of time, your firm can be up and running.

**Building Ordinance Coverage**

Building ordinance coverage is overlooked by many insureds and insurance agents. If you own your own building, this is an extremely important coverage. In the event of significant damage to your building, local governing authorities may require you to meet all current building ordinances prior to receiving a new certificate of occupancy. Simply meeting new fire codes and ADA requirements could be extremely costly.

**Employment Practices Liability Insurance**

This liability exposure is generally excluded in your general liability policy. EPL policies provide coverage for sexual harassment, wrongful termination, discrimination, violations of parts of the Americans with Disabilities Act, and related issues. Companies with multiple locations and multiple shifts should consider this coverage. Premiums have dropped significantly since the coverage first became available a few years ago.

**Boiler and Machinery**

Not too many companies have boilers, but everyone has heating and air conditioning as well as electric systems. This coverage protects you from failures in these systems. Even if you are only renting a space, you may be responsible for such items in your lease. This is an inexpensive coverage that is often overlooked.

**Inland Marine**

This is a generic term for a wide range of miscellaneous policies that cover specific circumstances. These policies are sometimes called floater policies and generally cover goods that are "floating" between locations. For example, cargo insurance is available to cover goods shipped on a common carrier. Exhibition floaters cover your demonstration equipment set up at a trade show. Salesmen's equipment can cover laptop computers used in the field by your staff.

**Directors & Officers Liability**

D&O provides coverage for claims against company directors alleging mismanagement of a firm. As a member of a board, directors and officers are personally liable for claims against the board. Firms normally indemnify board members; however, if the company is unable to fulfill its indemnification, the D&O policy will protect the members. D&O policies now offer extremely broad coverages. Employment Practice Liability can be included which protects you from suits alleging discrimination, wrongful termination, and sexual harassment. Coverage for Securities Exchange Commission (SEC) violations can be included to cover stock offerings and private placements. Retroactive coverage to the date of incorporation of the firm is often available. NOTE: D&O covers individual board members, not the actual entity firm. If you have the potential to lose a suit, it is important to discuss the allocation of the settlement beforehand. The insurance company may want to allocate as much as possible against the firm to reduce their expense. Board members will pursue the alternative course of action. There are now policies available that include entity coverage. Additionally, some jurisdictions now limit allocations against an entity.

## Frequently Asked Questions

### I'm just getting my business started. Do I need insurance right away?

Yes, because the chance that you could suffer a loss begins with the first day of business. You can't get help after the fact. If you suffer a loss and have no insurance or have improper or insufficient coverage, there is very little, if anything, your insurance agent can do to help you.

### I don't have any major business assets. Why do I need insurance?

Every business has some property. And, when you think about it, your business is your property. Just like your home and your car, your business needs to be protected from loss, damage and liability. In addition, your business **is** your source of income, so you need protection from the potential loss of that income.

### Is insurance coverage different for different businesses?

Many small businesses are now insured under package policies that cover the major property and liability exposures as well as loss of income. A common package policy used by many small businesses is called the Business Owner's Policy (BOP).

Generally, these package policies provide the small-business owner more complete coverage at a lower price than separate policies for each type of insurance needed. Your agent can help you decide which policy or policies are right for your business. Additional coverage for property, liability or perils or conditions otherwise excluded (e.g., flood protection) can be purchased as endorsements to a standard policy or as a separate, second policy called a difference-in-conditions (DIC) policy.

Because businesses vary, it is impossible to have a standard policy to cover all contingencies. Also, some businesses, regardless of their size, do not fit the profile of a standard business owner's policy. Your insurance agent can advise you of the best policy (or policies) to protect you and your business.

### What types of property do I need to insure?

Your business may not possess all the following types of property, but you can use this list to make sure that you have considered all the property categories and any insurance coverage that may be warranted:

- Furniture, equipment and supplies
- Inventory
- Money and securities
- Records of accounts receivable
- Improvements you made to the premises
- Machinery
- Boilers
- Data processing equipment
- Valuable papers, books and documents
- Mobile property such as automobiles, trucks and construction equipment
- Satellite dishes
- Signs, fences, and other outdoor property not attached to a building
- Intangible property (good will, trademarks, etc.)
- Leased equipment

**What types of property insurance should I consider buying?**

The best thing to do is to take a complete inventory of all your business property, determine their value and decide if each is worth insuring. Then check to see that the items on the inventory list are included in the basic business property policy and covered for the correct amount. If not, ask your agent about the cost of purchasing additional coverage to meet your needs.

**How much property insurance do I need to buy?**

There is no one answer to this because each business is different. You can consult with your agent on the monetary limits needed to cover your potential for loss. Obviously, a one-person accounting firm will need to purchase less insurance than a store with a substantial inventory. But each will need to make sure that all necessary business property is covered, that the limits of liability are sufficient to protect the owner and the employees, and that loss of income is protected.

In addition, each business has unique needs and situations that must be handled. If the store happens to be located on a flood-prone area, the owner should invest in flood insurance. The accountant may wish to purchase reconstruction-of-accounts-receivable insurance to cover the loss of accounting records. The costs of reconstructing those records, money borrowed because of delayed payments due to the records being lost, and lost payments from those clients whose records cannot be reconstructed are all covered.

Liability protection also will vary from business to business. A retail business is more at risk for potential suits than a business that is not open to the public. Also, in some states, courts tend to respond more positively to lawsuits, increasing both the likelihood of successful lawsuits and the amount of damages awarded. In today's lawsuit-conscious society, higher liability limits are extremely important and relatively inexpensive. Your agent can help you decide how much coverage is needed for your particular business.

**Who decides how much my business property is worth?**

Property insurance can be purchased on the basis of the property's actual value, on its replacement cost, or on an agreed amount. The differences between the three are:

**Actual Cash Value**
The replacement cost of the item minus depreciation. For example, a new desk may cost $500. If your 7-year-old desk gets damaged in a fire, it might have depreciated 50 percent. Therefore, you would be paid $250 for it.

**Replacement Coverage**
The cost of replacing an item without deducting for depreciation. So today's cost for a desk of a size and construction similar to the 7-year-old one damaged by fire would determine the amount of compensation. If it costs $500 today, that would be the replacement coverage.

**Agreed Amount**
Art objects, antiques and other unique items are usually insured at an amount agreed upon when the policy is being written. An appraiser values the goods to be insured and the business owner and the insurer agree upon an amount that the insurer will pay if the goods are destroyed due to a covered peril.

Check your policy. If you prefer replacement coverage and do not already have it, this coverage can be added to your policy. Inflation-guard coverage, which automatically increases your insurance amount a certain percentage, protects against rising construction costs. Your agent can advise you of the costs involved.

**Everybody seems to be suing everybody else these days. What if someone sues my business?**

No business can afford to be unprepared for a lawsuit. Liability insurance protects your business assets when the business is sued for something the business did (or failed to do) that contributed to injury or property damage to someone else. Liability coverage extends not only to paying damages but also to the attorneys' fees and other costs involved in defending against the lawsuit - whether valid or not.

The standard business owner’s policy provides liability coverage, as does a separate policy known as a commercial general liability (CGL) insurance policy. Generally, commercial liability insurance, whether purchased in a separate policy or as part of a standard business owner’s policy, will cover bodily injury, property damage, personal injury or advertising injury. The medical expenses of a person or persons (other than employees) injured at the business or as a direct result of the operations of the business are also covered.

**I work out of my home. Will my homeowners insurance cover my business?**

Yes, but on a very limited basis. Loss of business property is usually reimbursed up to $2,500 in the house and up to $250 for business property damaged or lost away from the premises. Even if your business is a sideline such as a craft studio, these limits may be too low to cover all the equipment and materials you have accumulated. It's also important to know that no business liability coverage is included in a standard homeowner's policy. Your insurance agent can help you ascertain what, if any, additional coverage you need. This additional coverage may be added to your homeowner's policy or found in a separate commercial policy.

**Can I do anything to lower my insurance premiums?**

Remember that all insurance premiums are based on the risks involved. The insurance company evaluates the situation to determine the risks - or potential for losses - and bases its rates on the results. Therefore, deliberate steps you take to lower your risks not only can help safeguard your business but also may make you eligible for lower insurance rates. Consider these steps:

- Maintain adequate lighting throughout your business premises.
- Keep electrical wiring, stairways, carpeting, flooring, elevators, and escalators in good repair.
- Install a sprinkler system, smoke and fire alarms, and adequate security devices.
- Keep only a small amount of cash in the cash register.
- Keep good records of inventory, accounts receivable, equipment purchases, etc. Consider keeping a second set of records off-site, such as with your accountant, insurance agent or at home.
- Make sure your employees have good driving records.
- Make sure your employees know how to lift properly and use all necessary safety equipment, such as goggles, gloves, and respirators.
- Consider using the services of a risk manager. Such an outside consultant can advise you of any safety or environmental regulations and talk to your employees about safety practices.
- You may also wish to raise your deductible where appropriate to lower your insurance premiums. How high to raise the deductible should be governed by how much you can afford to pay out of pocket. Be careful not to raise it so high that you cannot cover it should a loss occur.
- Finally, make sure your agent is familiar with your business and the risks inherent in it. He or she should be able to advise you on risk management techniques and their benefits to both you and the insurer.

**What should I look for in an agent?**

Agents are there to help you. At the most basic level, any agent should be able to answer all of your questions about insurance, provide you a thorough assessment of your insurance needs, and offer you a choice of insurance products to meet those needs. Also, any insurance agency should provide you with prompt, quality service in the case of a claim.

Just as important is the level of professional confidence and personal comfort you feel with the agent.  Many people stick with the same insurance agent for decades, even generations. It helps to find an agent you can get to know and trust.

An important, but sometimes overlooked, factor to keep in mind is that there are two kinds of insurance agents: those who represent only one insurance company and those who represent more than one insurance company.  Agents offering through their agencies only the policies of one insurance company often are referred to as "captive agents," because the company they represent does not allow them to offer their customers competitive alternatives.  By contrast, agents offering through their agencies the policies of more than one insurance company are called "independent agents," because they can shop around for their customers for the best insurance values among a variety of competing companies.  A nationwide survey in 1994 showed that Americans prefer to work with independent insurance agents by a 2-to-1 margin over captive agents.

# Health Insurance

## Introduction

If, by becoming self-employed you lose your employer-sponsored health insurance coverage, you have other alternatives. You can buy an individual health plan from a private insurance company. In Pennsylvania, as in most other states, you have limited guaranteed access to individual health insurance. Whether you can buy an individual health plan may depend on your health status, the kind of coverage you want to buy, and other circumstances. Also, there are some alternatives to individual health insurance coverage such as COBRA or conversion policies.

Replacing health insurance for yourself and your family can be expensive and should be calculated into your start-up and operating expenses. If you are self-employed and buy your own health insurance, you are eligible to deduct an increasing percentage of the cost of your premium from your federal income tax. This deduction is 60% for 2000 and 2001, 70% for 2002, and 100% in 2003 and thereafter.

## Insurance Providers

The following information was taken from "A Consumer's Guide to Health Insurance," Pennsylvania Insurance Department, www.ins.state.pa.us/ins

*Individual insurance* includes health insurance coverage you can purchase on your own directly through an insurance company. Many health insurance companies offer individual health coverage to people who either are self-employed or work for a business that does not offer health insurance.

All Pennsylvania residents can buy individual health insurance through the Blue Cross and Blue Shield plans on a guaranteed issue basis. However, your choice of health plans may be limited and you may face a pre-existing condition exclusion period.

Other insurers that offer individual health insurance coverage can medically underwrite applicants and do not have to offer coverage to everyone who applies. You have limited guaranteed access to individual health insurance in most other states.

*Franchise insurance* is individual insurance. This type of insurance coverage is optional and the insurance policy is issued to the employee of an employer or a member of an association where the employer or association agrees to collect the policy premiums on behalf of the employee or member and pay them to the insurer. For employees, this option may allow them to purchase coverage through payroll deduction.

*Association sponsored insurance* includes health insurance coverage that may be offered to you or a member of your family through a fraternal or professional association. Association sponsored insurance usually costs less than individual insurance because, similar to employer sponsored insurance, you may be able to purchase health insurance at a group rate.

*Government Sponsored insurance* includes health insurance coverage that provides medical benefits to senior citizens, disabled persons, and the economically disadvantaged. Examples include Medicare and Medicaid. Government sponsored insurance also may be available to those with conditions related to military service.

In the southwestern Pennsylvania region, policies for **self-employed individuals** or **small business employers** are available from several sources, including but not limited to:

- Private insurance providers, such as Highmark
- Local Organizations, like Chambers of Commerce, SMC of Pittsburgh, Pittsburgh Technology Council
- National Professional/Business Organizations relevant to your trade or business
- Various national insurance carriers found through independent insurance agents

# Bonding

**What is a bond?**

A bond guarantees the fulfillment of a legal obligation. It's a three-party agreement or promise where a third party (surety company) guarantees to a second party (obligee or owner) the payment or successful performance of the first party (principal). A bond is not an insurance policy calculated to cover losses. Rather, a bond is an extension of credit with the assumption that there will be no loss. The bond premium paid to the surety covers only the underwriting expenses of the surety company. When losses occur, they have a significant impact on the surety company's financial results.

**Types of Bonds**

Bonds cover numerous aspects of operating a business. Typical bonds are surety and fidelity.

**Benefits of Surety Bonds**

Surety bonds are a risk transfer mechanism. The risk of doing business with the principal is shifted from the obligee to the surety company. Federal, state and local governments often require surety bonds to guarantee that business owners and individuals will comply with various laws protecting public funds. For example, license bonds protect the public from business misconduct. Contract bonds protect taxpayers by guaranteeing that projects are completed properly, on time and without liens.

**Types of Surety Bonds**

Different surety needs are met by different classes of surety bonds:

- Contract Bond guarantees that an entity awarded a contract will meet its obligations under that contract.
- License & Permit Bonds guarantee that individuals granted a license or permit to operate a business or to exercise a privilege will meet the obligations under that license or permit.
- Miscellaneous Bonds guarantee a variety of non-classifiable obligations. These include utility, lost securities, workers compensation premium payments, and sales tax payments.

**Types of Fidelity Bonds**

Companies are vulnerable to a wide variety of commercial crimes, including employee theft or dishonesty; forgery; loss of money, securities and other property on premises; computer fraud; disappearance or destruction of property; robbery and burglary. Different security needs are met by different classes of fidelity bonds:

- Pension Trust (ERISA) Bonds are designed to protect the investors and the money in these funds.
- Blanket & Schedule Bonds provide protection against employee theft. These bonds cover the loss of money, merchandise or other property owned by the insured when such a loss is due to employee dishonesty.
- Janitorial Services bonds are specifically designed to provide protection for customers since they have access to customers' assets, equipment, supplies and personal belongings.

**Underwriting Process**

A surety company must determine the probability of a loss should the principal be unable to complete their obligations under the bond. Since a bond is an extension of credit, the surety company must analyze the principal's financial standing and business aptitude to determine if the principal has the financial strength and business knowledge to support the bonded obligation. This is called the underwriting process. Surety company underwriters evaluate risks in ways similar to banks evaluating loan applications. Underwriters consider business and personal financial statements, credit reports, credit references and other factors.

**Collateral**

A surety company may request collateral to reduce the risk of the bond. Forms of collateral include cashiers checks, certificates of deposit or irrevocable letters of credit. In addition, collateral reduces the risk a surety company assumes when issuing a bond. After all obligations of the bond have been met, collateral is returned to the principal and the obligee releases the surety company from their obligation under the bond.

**Choosing a surety**

Surety companies handle a wide range of surety products, and sell different products at many different rates. When selecting a surety company, make sure the company is listed with the U.S. Department of the Treasury. The Treasury Department lists all surety companies that are qualified to write bonds for federal contracts. To be an acceptable, the company must qualify financially under the regulations of the U.S. Department of the Treasury.

Check on the rating of the company. An acceptable surety company is rated "excellent" or better by the A.M. Best Company, an insurance rating service. You can get a copy of its annual Best Rating Report from the surety company.

Make sure the surety company is licensed to do business in your state by calling the state's Department of Insurance. The lowest rate does not always guarantee you are getting the best deal. Check out the surety company before you decide to place your business with them.

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