NEEDS ANALYSIS,

THE BASICS

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INTRODUCTION

When analyzing your customer’s needs, there are a few simple steps that you may want to start with over and above the information on the application. A simple way to start would be by using the information below, remembering that this is just a starting point in building your client’s profile to determine your client’s financial problems or deficiencies so that the prospect begins to recognize the actual need/deficiencies as well.

A simple discussion to start the process should contain some, if not all of the following topics:

- **Cash Management** – is more than merely balancing a checkbook, cash management includes preparing and following a budget, using credit wisely and keeping the income tax burden to the lowest level possible
- **Risk Management** – There is risk of loss of both life and property. Life insurance can be used to protect a family against the risk of premature death. Disability insurance can protect against the loss of a person’s ability to earn a living. Property and casualty insurance can protect our worldly goods against accident and such perils as fire, flood, earthquake and theft. Health insurance can help pay the cost of needed medical care.
- **Accumulation Goals** – We all need to save money for some reason. Educating our children is one very common goal. Buying a home and building an investment portfolio are two other typical accumulation goals.
- **Retirement** – Taking action in the present to insure the future.

Rules of thumb or simple tests

- Quick tests are less specific than in-depth analysis
- Best used when time and premium are limited
- Quick tests are simple to understand

Types of Simple Needs Analysis

- Annual income times number of years protection desired
- Five Step Basic Security Test. Asks 5 questions:
  - Do you have a minimum of 5 times income protection?
  - Is your mortgage protected?
  - Do you have at least one year of income protected in case of disability?
  - Do you have 3 to 6 months of take-home pay in a liquid account?
  - Do you have a medical reimbursement policy?

After answering, plug in the numbers to meet basic security test.
Americans are among poorest savers in the world.

- Most families do not have 3 months of liquid savings.
- Average credit card debt per household exceeds $9,000.
- Interest rate on credit card debt is exorbitant.

Needs analysis can address a strategy to assist better habits.

Human Life Value Approach

- Determines what a person is worth economically over his lifetime.
- Factors to consider would be:
  - Future income
  - Years of earning potential
  - Taxes
  - Education and its impact on earnings
  - Training and professional development
  - Inflation

Simplified approach would be present gross earnings x number of years to retirement.

Example: Male age 37, retirement at 67, 30 years of work at present gross earnings of $50,000 = $1,500,000 (Assumes no raises, no factoring of inflation)

Having stated the above, which is a good place to begin, in the world of insurance, client's must decide when to insure, what to insure and how much to cover and pay. As an agent, it is your job to analyze these needs and be an advocate or problem solver to make sure the requested risk has been transferred. A client views policies in terms of obtaining reduced uncertainty. In most cases, your customers can only hope that the policy they purchase is appropriate. That is why agents are vital players in solving client needs.

Detailed Needs Analysis

- Cash Needs at Death
  - Final Expenses
  - Probate/Administration Expense
  - Federal/State Taxes
  - Last Medical Expenses
  - Funeral Expenses ($6,000-$12,000)

- Debt
  - Mortgage
  - All other debt
• Emergency Fund
  • 3 to 6 Months of survivor’s budget needs
  • Should be separate from income needs
  • Should be in a liquid account

• Income for surviving spouse should include 3 periods
  • Dependent children at home
  • Blackout period
  • Retirement
  • Social Security can be factored in if desired

• Education Funding
  • Can use the current cost or factor in inflation
  • Current cost of 1 year x number of years desired x number of children
    \((\text{Number of years is not necessarily 4})\)

• Add ALL cash needed to determine total
  • List all cash assets to offset cash needs
  • Life Insurance – both personal and group
  • Cash Savings
  • Liquidated value
  • Pension benefits of the deceased if immediately available at death
  • IRAs and other qualified programs if taken as a benefit to the survivor
  • Social Security, if qualified
  • Any other assets convertible to cash

• Total all amounts available at death then subtract the total cash available from
  the total amount required

• If the amount required is greater, life insurance could be part of the solution.

• After the amount of the life insurance is agreed upon, the next step is to
determine the type to use.

• Factors in determining type (whole life, universal life, term) could be:
  • Premium Cost
  • Client’s philosophy regarding term versus permanent
  • Client’s history of saving (permanent can encourage)
  • Client’s sophistication about investments/insurance
  • Savings and investments currently in place
  • Time frames for which coverage is needed
  • Client’s health

• Single Need Approach
  • Child-rearing years
  • Mortgage
• Outstanding Loans
• Survivor Income
• College
• Special Needs
• Handicapped family member
• Long-term Care
• Retirement needs in event of premature death

Capital Liquidation versus Capital Conservation

• How will the money be utilized at death and how long?

• Capital Liquidation (Utilization)
  • Uses both principal and interest
  • Logical for immediate disbursement of funds
  • Used to fund income over a period of years; problem for lifetime income
  • Disadvantage is it could erode fund prematurely
  • Advantage is it takes a smaller amount of money.

• Capital Conservation (Retention)
  • Uses interest only
  • Can produce income indefinitely and never uses the principal sum
  • Assumption of a reasonable interest rate critical
  • Advantage: Lifetime income more assured than Liquidation Method
  • Leftover corpus can be left to others.

The preceding has been an introduction to determining needs. The following is more in-depth in explain how to determine the required information.

Suitability When Determining Client Needs

Beyond being, the most responsible agent you can be, you should size-up your client and anticipate his needs when he cannot. How can this be accomplished?

Aside from determining current and future risks that you know about, you need to expect those that have not happened. For instance, you should know that a 50-year-old baby boomer client is a far more complex individual than his parents before him. His insurance needs are also more complex: higher life limits to cover college and entrepreneurial pursuits; medical coverages, long-term care and more retirement needs for a longer life span; higher primary and umbrella coverages to protect against lawsuits.

To really uncover as many of these client needs as possible, you must know more about your clients. Of course, a client profile is the best way to accomplish this. Customer profiles can provide a lot more information than you would gleam from an application. You must also ask clients what about their needs.
Three important questions might be:

- Have I given you all the information you need to make a decision?
- Does this information or policy make sense?
- Is there something else I can answer for you to assure you that this is the right solution based on your needs and objectives?

In addition, you should do research about their needs as a group so you can better anticipate insurance needs. Every additional bit of information you learn about your client helps you get closer to knowing their goals, needs and wants.

In some cases, your clients will not know the answers to your questions themselves – you may need to interpret for them. But, by all means NEVER do this without involving them in the process. And, of course, once you have asked all the questions you must be sure that you implement or meet their needs to the best of your ability.

Needs-Based Analysis

Beyond the issue of risk, traditional industry thinking tells us that suitability should be based on needs. Needs analysis is a procedure to help prospective insurance clients plan for their future.

Needs-based analysis has been around since the early days but it was refined in the late 1960s by Thomas J. Wolff, a tenacious and studious insurance agent, who is today an industry legend. As a young agent, Wolff struggled to make it in the business.

While other agents and teachers dazzled their audiences with tales of sales wizardry and artful cherry picking among the rich and famous, Tom Wolff told a much different tale. Instead of trying to achieve his place by showing everyone how good he was, he taught his students how effective they could be as agents through capital needs analysis and financial needs analysis. Thus, began the beginning of the suitability approach to selling insurance.

The purpose of a needs-driven sales system is to analyze a client’s needs and determine how insurance can best meet those needs. It is not meant to generate the sale based upon the obvious points of the product or the need of the salesperson to produce. It uncovers a prospect’s general financial problems or deficiencies so that the prospect begins to recognize the need.

The problem is personalized to arouse interest in a possible solution. Like any system, needs analysis works effectively only when it is used as it is designed. The system builds upon itself in terms of both content and data and is most effective when used from start to finish. Shortcuts undermine the effectiveness of the process. An agent following this system from start to finish should never be accused of less than professional point-of sale practices.

Needs-based analysis goes into great detail in analyzing needs and creating recommendations that are based upon airtight logic and conclusions. Needs-based selling involves the client, allowing him or her to use his or her own ideas and
assumptions. It is a process that allows the prospect to participate in creating his or her own solutions to needs based upon what he or she considers important. Analyses must represent and respect the client’s opinions. The goals are those of the prospect, not the agent. If the goals are not the goals of the prospect, the prospect is not likely to go along with the agent’s recommendations in the end.

A COMPLETE SYSTEM

Needs-based selling is a complete system for obtaining the appointment, opening the interview and gathering factual data for all types of prospects. At the end of the fact-finding process, a joint decision is made between the prospect and the agent as to which of three cornerstones of financial security is top priority:

- **Accumulation** (developing a sound plan to assist in paying for education and for other financial objectives),
- **Retirement** (planning to provide the additional income needed to supplement Social Security, pension plans, existing savings and investments) or
- **Protection** (planning to assure that obligations are met in the event of death, disability or loss of property).

Let's assume a life analysis was being conducted for a baby boomer client. Your fact finding will likely reveal that most boomers are underinsured and require more capital in the event of death than other segments because they have large loans, college-bound teens, business income replacement, partner buyouts, spouse retirement needs, etc. Seniors, on the other hand, are “winding down” their lives with fewer protection needs. However, for those who have not planned as well, an in-force policy that can be sold as a life settlement to pay long-term care costs or small burial plan can be a real comfort.

Performing Needs Analysis

The needs analysis system breaks the sales process down into carefully engineered parts:

**The Pre-approach**

This step is designed to get an appointment under favorable conditions for a face-to-face meeting.

**The Approach**

The objective of the approach is to obtain the appointment. During the approach, no detailed data-taking or selling takes place.
The Initial Interview

The agent’s objective during this initial interview is to gather information and uncover the dominant needs of a prospect. Information such as name, birth date, spouse’s and children’s names and birth dates, address and telephone numbers, property owned and basic obligations are gathered at this time.

Other information to obtain at this time is occupation, spouse’s occupation and whether or not the prospect is a smoker, works at home or engages in a high-risk occupation or hobby. A questionnaire is usually filled out at this point, rating his or her feelings, concerns and goals in a variety of areas.

Next, the prospect’s financial situation must be assessed. This part of the questionnaire covers such areas as annual income, total life insurance, total assets and total liabilities, the value and the mortgage of the residence, and present investments (such as savings and CDs, money markets, mutual funds, real estate other than the residence, stocks and bonds, U.S. government bonds, IRAs, 401(k)s or other salary savings plans, and pension or profit sharing plans).

The questionnaire then assesses the prospect’s financial risk profile. For example, what kind of financial risk is he willing or able to take: Considerable risk, almost none? Is he willing to take average risks in order to improve the rate of return? Is he or she willing to take substantial risks in order to maximize the rate of return? In the next part of the questionnaire, the prospect is asked to make expectations and predictions about his future. For example, will he be changing jobs, starting a business, selling a business, receiving a promotion or retiring, buying a new home or car? Will he be buying a larger or smaller home, making improvements to a home, caring for a parent/spouse or changing marital status? Does he anticipate getting a raise, getting a bonus, inheriting assets, borrowing money, paying off a loan or purchasing property?

This initial interview begins the process of building trust. The initial interview and questionnaire allow the agent to screen the prospect and then determine whether to eliminate him or her based on the data gathered or to proceed with the selling process. The data gathering phase of needs analysis is designed to help understand people. It is often said that people don’t buy because they are made to understand; rather they buy when they feel they are understood. The more time that is spent in the effective gathering of both facts and feelings, the less time that will be needed to be spent on the close. Being sincerely interested in people will permit them to be openly interested in the full presentation.

The Review

After the prospect completes the questionnaire, the agent reviews it quickly and looks for areas of importance. The agent may discover, for example, that the prospect is not satisfied with his current premiums, the percentage of income he
or she is saving, that he or she does not have an understanding of trusts or that he or she does not participate in a pension or profit-sharing plan.

The relationship should be terminated if the prospect is uncooperative, if his or her needs do not meet the agent’s minimum requirements, area of knowledge or if insurability does not permit the agent to offer help.

The interview should be continued if the prospect agrees that this is an appropriate time to engage in further discussion, or another appointment should be scheduled. An appropriate prelude to further discussion might be advising the prospect that the 15 minutes are up, and that the agent is prepared to leave as promised. The agent may suggest that, based on the information shared, he or she can be of assistance to the prospect in the areas where the prospect’s goals are not being met. The purpose of this interview is to screen the prospect and uncover his or her needs. Naturally, some cases are more involved than others, and the agent may experience a situation where he or she feels overwhelmed and in over his or her head.

At this time, it is wise to make the decision to involve a manager, trainer or a fellow agent with expertise in the advanced market areas. Even if this means splitting a commission, the agent will benefit by learning more, earning more and developing a loyal client, not just a policyholder.

**Matching Client Needs with Product**

When you are comfortable that you know your client needs and have asked the client himself, it's time to match these needs with an appropriate product. Much has been written on the perils of matching the wrong product to a perceived client need. This is an area where agents need to exercise extra due care for the client's sake and their own financial well-being.

Questionable market conduct in the 1980s and 1990s created new demands for today’s agent. Past agent abuses have centered around twisting, wholesale replacement, deceptive advertising, misleading illustrations and other unethical acts.

Regulators have responded with replacement policy forms, insurer fines, agent reprimands, and in some cases, revocation of licenses. To compound the problem, the industry's image has been occasionally tarnished by solvency problems. Further, stiffer competition, declining interest rates and thinner profit margins have impacted how insurers and agents work together - less support in marketing and support materials.

The bottom line in either case is that agents are forced to work harder and smarter. In lieu of sitting back and waiting for the market to improve, industry forecasters say that agents must accept new roles to survive.

Repeat business, referrals and long-term rewards must center more around client needs, rather than the products agents wish to sell. The trend toward
"agent as counselor" is the most obvious path. Putting oneself out to be knowledgeable in many financial matters, however, will come with a price tag as you will see in this chapter.

Both regulators and clients will hold insurance professionals to ever higher standards. Agent due care and sales conduct will be more important than at any time in our industry's history. This will involve a commitment by agents to polish skills and acquire a systematic approach to filling client needs. Following are some basic due care discussions which may help the agent get started. Of course, every situation will vary and require constant refinement.

**CHOOSING THE CORRECT PRODUCT**

If an agent is truly using due care in selecting the right policy, before selling, he should:

- Obtain specific information on the client's current and anticipated risk exposure and review all existing policies
- Review a "specimen" policy and policy amendments for every insurance contract he is marketing
- Make sure that the client clearly understands the type and limit of coverage being purchased; the responsibilities of each party, the insured and the insurance company; and the services that will be provided by the agent
- Monitor policy needs on a continuing basis.

The need for responsible planning in today’s market is key to your client’s future financial needs. Most of your clients can expect to face financial issues during their life.

Some of those issues may include:

- **Cash Management** – is more than merely balancing a checkbook, cash management includes preparing (and following) a budget, using credit wisely and keeping the income tax burden to the lowest level possible.
- **Risk Management** – There is risk of loss of both life and property.
  - Life insurance can be used to protect a family against the risk of premature death.
  - Disability insurance can protect against the loss of a person’s ability to earn a living.
  - Property and casualty insurance can protect our worldly goods against accident and such perils as fire, flood, earthquake and theft.
  - Health insurance can help pay the cost of needed medical care.
- **Accumulation goals** – we all need to save money for some reason. Educating our children is one very common goal, buying a home and building an investment portfolio are two other typical accumulation goals.
- **Retirement** – it is important to emphasis the significance of taking action today to ensure that the later years are as comfortable and worry-free as possible.
• Estate planning – recognizing that death is inevitable and planning for the ultimate transfer of our assets to our heirs

**LIFE INSURANCE**

Life insurance is a unique asset that can be used to solve some of life’s perplexing financial problems. Some of the death benefit uses for life insurance are:

• Create an estate: Where time or other circumstances have kept the estate owner from accumulating sufficient assets to care for his or her loved ones, life insurance can create and instant estate.
• Pay death taxes and other estate settlement costs:
  • These costs can vary from a low of 3% to 4% to over 40% of the estate.
  • Federal Estate Taxes are due 9 months after death.
• Fund a business transfer: Business owners often agree to buy a deceased owner’s share from his or her estate after death. Life insurance provides the ready cash to finance the transaction.
• Pay off a home mortgage: Many people would like to pass the family residence to their spouse or children free of any mortgage. Often a decreasing term policy is used, which decreases in face amount as the mortgage balance is paid down.
• Protect a business from the loss of a key employee: Key employees are difficult to attract and retain. Their untimely death may cause a severe financial strain on the business.
• Replace a charitable gift: Gifts of appreciated assets to a charitable remainder trust can provide income and estate tax benefits. Life insurance can be used to replace the value of the donated assets. Proceeds from life insurance policies can also be paid directly to a charity.
• Pay off loans: Personal or business loans can be paid off with insurance proceeds.
• Equalize inheritances: When the family business passes to children who are active in it, life insurance can give an equal amount to the other children.
• Accelerated death benefits: Federal Tax Law allows a “terminally ill” individual to receive the death benefits of a life insurance policy on his or her life income tax free. Such “living benefits”, received prior to death, can allow a person to pay medical bills or other expenses and maintain his or her dignity by not dying destitute. If certain conditions are met, a “chronically ill” person may also receive accelerated death benefits free of federal tax.

*(Note: The text here concerns Federal Tax Law; state or local tax law may vary.)*

Existing life insurance policies should be reviewed to verify that policy provisions allow for payment of such “accelerated death” benefits.
While life insurance products are primarily used for death benefit protection, they are also used for long-term accumulation goals.

- College fund for children or grandchildren: Cash value increases in a policy on a minor’s life (or the parent’s life) can be used to fund college expenses.
- Supplemental retirement funds: Current insurance products provide competitive returns and are a prudent way of accumulating additional funds for retirement.

Available cash values may also serve as an “emergency reserve,” if needed, or a source of loans, since life policies frequently include features permitting borrowing against these cash values.

Note: A policy loan or withdrawal will generally reduce cash values and death benefits. If a policy lapses or is surrendered with a loan outstanding, the loan will be treated as taxable income in the current year, to the extent of gain in the policy. Policies considered to be modified endowment contracts (MECs) are subject to special rules.

Before determining the amount of life insurance needed by a client, due care would involve the agent and client in a discussion concerning the various types of life insurance available: term, whole life, modified whole life, single premium whole life, universal life, variable life.

The attributes of these different policies are best left to a course on basic life insurance. However, it is critical, under due care, that agents recognize the pure risk need of clients and counsel them on the proper choice. For example, persuading a client to accept a high monthly premium whole life policy with a settlement payoff that leaves a significant financial gap at the death of a breadwinner, is not exercising due care. This is not to imply that whole life forms of insurance are inappropriate. Rather, there are situations here a client's age and situation call for the agent to consider future estate settlement costs and liquidity as prime directives in making policy choices. There may even be conditions where due care by the agent might involve a recommendation for a client to carry little or no life insurance at all. Issues regarding life insurance needs for singles, non-working spouses and children are often debated among financial planners and agents alike.

One process for determining an estimate of the amount of life insurance needed is called capital needs analysis. Financial planning courses cover this process in considerable detail and typically include a sample capital needs worksheet. For purposes of proper sales conduct by agents, factors to consider by agents include:

**Capital needs for family income**

Most families will be able to maintain their standard of living with about 75% of the former breadwinner's income. Depending on the skills and resources of the surviving spouse, this fund may be large enough to provide lifetime income or for a specified period of transition.
Capital needs for debt repayment

Typical debts to consider include home mortgages, charge cards, bank notes, business debt, etc. A decision can be made to totally liquidate the debt or to use life insurance proceeds to set up a "sinking fund" to make payments for the life of the loan or a specified period.

Other Capital Needs

This might include emergency reserve funds, estimated to be between 50 percent to 100 percent of a client's annual after-tax income, and possible college education funds for surviving children.

Estate Settlement Costs

Final expenses can be expensive. Uninsured medical costs and funeral expenses are one aspect. In addition, there are federal and state death taxes. Although the Economic Recovery Tax Act of 1981 eliminates the federal estate tax on property passed to a surviving spouse, the estate of the survivor may face a large death tax liability.

Current Assets Available for Income Production

What current assets, such as savings accounts, investments, real estate, pension plans, etc., are currently available for income production or liquidity needs to offset the capital needs above?

Net Capital Needs

By combining the above factors, the agent can arrive at the net capital needed to be replaced by life insurance.

Where capital needs analysis indicate that a $500,000 gap will occur at the death of the breadwinner(s), the agent's due care life insurance recommendation should be for $500,000 of life insurance. Anything less could leave the client underinsured.

Lesser amounts may be purchased where the client cannot afford the premiums or make the choice to carry less. If there are additional concerns, such as a client’s long-term health, the agent might be advised to disclose his recommendation even though a more expensive policy with less coverage is purchased.

Ongoing monitoring of capital needs is necessary to plan for new client objectives, repositioning of debt, inflation, estate settlement changes and potential health problems that may prohibit coverage in the future.
Another due care consideration concerning life insurance is ownership or title of the policy ownership or title of the policy. Agents should recognize conditions where it would be beneficial to keep life insurance proceeds out of a client’s estate by using a life insurance trust or alternative ownership.

Due care may be sufficient where agent disclosure of estate tax consequences of life insurance owned by a client and a proper referral to a competent estate planning attorney is pursued.

**Essential Due Care Questions for Life Insurance:**

- What existing death benefit sources does the client have? Group life, survivor's income, individual plans, association group life plans, pension plan death benefits.
- Who is insured?
- Is someone contributing economically who must be added?
- Do all death benefits, along with available assets, meet client objectives?
- Are there other needs to consider such as dependents with special problems? Business debts? Personal debts?
- Are there existing life policies that can be cash surrendered or tax exchanged to more efficient plans?
- Is waiver of premium available? Is this a desirable benefit for this client?
- Is there accidental death benefit or double indemnity? If so, is this desirable or can it be dropped in favor a lower premium?
- Is coverage guaranteed renewable? To what age? Is the client's health stable enough to change policies?
- Is coverage decreasing term? Is the balance sufficient?
- Is there a substandard rating that can be removed?
- Are there policy dividends? Is the client making the best use of these dividends? Or, would reduced premiums be recommended?
- What are the settlement options available at death? (Lump sum, payment options, insurance trust, etc.)
- Is there a plan for the "common disaster" involving both husband and wife?

**HEALTH INSURANCE**

The continuing escalation in health care costs makes a well-designed health insurance program essential to your client’s family financial security; one or two days in the hospital could equal thousands of dollars in expenses.

The most efficient form of health protection is by group coverage. Group insurance is the predominant way of providing health insurance today with a definite trend toward HMOs (health maintenance organizations).
HMOs offer a different approach from traditional health insurance, in which your client picks the doctor, pay as treatment is received and receives reimbursement from an insurance company. With an HMO, your client’s employer pays and annual fee, for which the plan’s own doctors handle almost all of your client’s health needs.

HMOs typically cost less in that there are usually no deductibles and they coverage higher percentage of costs than traditional plans. However, your clients will be limited to the services of this organization, it is important that your client know the answer to the following questions:

- Where do I go if I require hospitalization?
- What about emergency treatment out of the local area?
- How substantial is the local staff and are all specialties represented?
- How long must I wait to get an appointment?
- Is the plan facility oversubscribed?

Due care in health counseling would involve fact finding to determine sources of social insurance available to the client such as Medicare and occupational worker’s compensation. Any gaps in coverage need to be filled through blanket health coverage or medical benefits under a liability policy if the health condition developed as a result of an accident. In addition, an agent-to-client discussion should cover points concerning:

**Basic Eligibility**

- Exactly who is covered?
- Does "family" include the subscriber, spouse, one, two or more children?
- How old can the children be and still be covered?
- Does this change if the children are married?
- Will family members lose their eligibility when they turn 65 and Medicare takes over?
- How will a divorce affect a member’s coverage?
- Will a foreign or out of state residency longer than six months affect coverage?
- How long will a retarded or physically handicapped child or member be covered?

**Total Maximum Coverage**

A limit to coverage could be present in form of duration and/or a dollar cap.

- Is this a ”lifetime cap”?
- Is this cap per family member or for the entire family? Family benefit maximums should be unlimited or extremely high, e.g., $1,000,000, due to potential costs of a major surgery, hospitalization, a series of family illnesses, etc.
A lifetime cap of between $2 and $5 million, per family member would not be uncommon and might be considered a minimum considering the high cost of medical care.

**Deductibles**

- How much is the deductible, if any exists? How much of the initial costs must your client absorb in the way of a deductible?
- Is it per family member? Is there a limit of two or three deductibles per family or must each member satisfy it?
- Per year? Is it charged only once in a calendar year?
- Is there a maximum deductible per family?
- Are there specific deductibles for medicines vs. health care?
- Are there deductible surcharges if the client does NOT pre-register with the insurer, say for non-emergency care?

**Stop Loss & Co-Payments**

- After deductibles, is the client expected to share or co-pay any medical expenses?
- Beyond the deductible, what percentage of the expense must your client pay, 10%, 20%? Is there an established time, usually after a specific amount of expenses have been incurred, that the co-pay will stop and benefits will be 100% covered by the insurer? Most important, is the stop-loss provision that eliminates all co-insurance and pays 100% of the charges after you reach $1,000 (or some specified dollar amount) in out-of-pocket expense?

**Pre-Existing Conditions & Waivers**

- Are certain known pre-existing health conditions prohibited or waived?
- If waived, for how long?
- Is there a waiting period for unknown pre-existing conditions?

Some policies specify a 6 to 12 month waiting period for listed conditions such as: hernia, tonsils, adenoids, hemorrhoids, varicose veins, nasal surgeries, foot and toe surgeries, breast reductions, ear problems, etc.

**Exclusions**

Possible policy exclusions or highly limited protection might include conditions and services as follows: medical costs exceeding limits, unlisted services, service covered by occupational insurance (worker’s compensation, etc.), health problems due to acts of war, government provided services, Medicare benefits, services from relatives, private nursing fees, custodial care, long-term care, inpatient diagnostics (x-rays not related to specific surgery), dental and hearing aids, vision care, speech therapy, cosmetic sex
changes, infertility, weight reduction, orthopedic devices, maternity care, outpatient drugs, acupuncture, nutritional counseling, physical or occupational therapy outside the hospital.

Some "bare bones" plans may cover costs only at prescribed hospitals, although emergencies are typically covered no matter where. Some only pay for procedures incurred in the hospital by hospital employed physicians, i.e., regular doctor visits or follow-up sessions are not covered unless specified by the hospital doctor.

Inside limits should also be address, like $200 for X-rays, etc., should be avoided in favor of comprehensive coverage, i.e., a flat percentage of the cost insured.

Some medical plans call for the use of a preferred supplier and provide a list of doctors or hospitals from which you must choose.

Outpatient benefits should be examined carefully since many procedures are now done on an outpatient basis, e.g., preadmission testing, diagnosis, etc., due to the high costs of hospitalization.

Further, many plans may cover certain hospital procedures but not the supplies, e.g., a blood transfusion procedure may be covered, but not the cost of blood. One of the latest trends is the requirement that certain procedures, such as organ and tissue transplants, be pre-authorized. Additionally, some procedures, like bone marrow transplants, are considered experimental and not covered under any conditions.

Mental health and home health care are usually very limited areas of care. Dollar limits per day with annual maximums are not uncommon, as are maximum visits per year.

**Guaranteed Renewability & Rate Changes**

- Can the insurer modify or change premium costs?
- Under what conditions?
- Can a class or "block" of subscribers be changed without changing rates for all subscribers?
- Can the subscriber be canceled?
- If so, how long will benefits last if client is in the middle of a health crisis?

**Important Dates & Notification**

While many of the above exclusions and limitations are typically spelled out in policy brochures or in bold print, issues of important dates and notifications can "fall through the cracks". Proper due care would involve a discussion or memo to the client concerning policy time lines. Examples include:

- "All claims must be filed within 15 days on approved claim forms"
- "The insurer must be notified within 60 days of any newborn or adopted children"
• Annual notice is required to sustain coverage for a retarded or handicapped child who is older than the specified age limits"
• "A family member must apply for his or her own plan within 31 days of the main subscriber's ineligibility"

Agents who handle multiple lines of insurance must consider the impact of health insurance on the client's financial planning. A medical catastrophe can permanently devastate a family. Despite the importance of life insurance, disability protection and certain property/casualty coverage, health insurance is a clear priority.

It would not be considered due care for an agent who handles different product lines to market a $250 per month whole life insurance plan to a financially limited client when there was no health insurance in place. A more prudent approach would combine a "basic hospital plan" for major medical emergencies at $150 per month and a term life plan for $100 per month.

Even the agent who specializes in a specific product line should exercise due care to inquire that clients have health coverage in place or at least budget for same before selling other forms of insurance.

Essential Due Care Questions with regard to Health Insurance:

• What available sources of health care are available to your client group plans (employer provided), HMO's, Medicare, other?
• Does your client have enough medical expense benefits to meet basic hospital needs or major medical expenses?
• What family members of the client require coverage and are they eligible?
• Does the client or family member need supplemental coverage?
• Should the client terminate any existing or duplicate medical expense premiums?
• Does the client have dependents who have or will soon terminate coverage under the family plan? If so, can they purchase their own? What conversion rights do they have?
• Is your client's policy guaranteed renewable?
• Does the client's health care continue to protect dependents in the event of his or her death?
• Does the client have a substandard rating or waiver of coverage? Will the insurer remove it? When? Will another company write without the waiver or rating?

LONG-TERM CARE INSURANCE

Long-term care is the kind of help your client needs if he is unable to care for himself because of a chronic illness or disability. Most long-term care policies and state regulations define a “chronically ill” individual as someone unable to perform at least two activities of daily living for a period of at least 90 days and/or someone who requires “substantial supervision” to protect themselves from threats to health and safety due to severe cognitive impairment.

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Long-term care services can range from help with daily activities of living, such as bathing, shopping or dressing, to skilled nursing care in a nursing home. Care can be provided by friends and family, local home care agencies, adult day care programs, nursing homes, and residential and retirement facilities.

**Long-Term Care Policy**

The traditional long-term care policy is defined as any accident and health insurance policy or rider advertised, marketed offered or designed to provide coverage for not less than 12 consecutive months for each covered person on an expense incurred, indemnity, prepaid or other basis for one or more necessary or medically necessary diagnostic, preventive, therapeutic, rehabilitative, maintenance, or personal care services, provided in a setting other than acute care unit of a hospital.

**Today’s continuum might consist of the following:**

- **Chore services:** Volunteers buy groceries, mow lawns, vacuum, run errands, etc.
- **Home visitors:** Meals-on-Wheels, story reading, companionship, etc.
- **Senior centers:** Social activities, dances, bus tours, etc.
- **Adult day care:** Daytime activities, lunches, therapy, games, etc.
- **Home health care:** In-home services by nurses, physical therapists and dieticians, etc.
- **Rehabilitation programs:** Provide extensive physical therapy, occupational therapy and speech therapy.
- **Respite care:** Individuals provide relief to aid primary caregivers.
- **Retirement housing communities:** For the independent elderly, offering individual units, security, social activities, etc.
- **Continuing care communities and centers:** Designed to meet residents’ changing needs from retirement housing through skilled care.
- **Assisted living centers:** Offer medical attention, as well as assistance with eating, bathing and other activities of daily living.
- **Nursing facilities/skilled nursing:** Provide intensive nursing care around the clock.
- **Sub-acute care:** Provide post-acute or heavy skilled care that is expected to be of shorter duration than usual skilled care.
- **Acute care:** Surgical or hospital with lengths of stays limited by diagnosis related insurance coverage.

The continuum is in a constant flux as it responds to new terms, new legislation, coverage limitations, medical breakthroughs and other market-driven demands.

Similarly, long term care policies, both old and new, must be placed in the context of continuum changes. Residential Care Facilities and Adult Day Care, for example, are increasingly covered in today’s newer policies. Earlier policies restricted benefit payments to only those facilities that offered Adult Day Care, a much more restrictive definition.
Another example is policies that covered home care, but required that services were needed because the person would require institutional care without them. Agents need to understand how the policies they offer relate to Continuum of Care services in from the standpoint of policy triggers, ADLs, mental deterioration, etc. This can only be accomplished by evaluating individual policies and client needs.

**Essential Long-Term Care Policy Questions**

- Is the benefit amount enough to meet the cost of local nursing homes? Costs can range from $209 in the mid-west to $576 in Alaska. Be sure to advise clients that costs may exceed benefits.
- Does the policy indemnify for a fixed daily amount or simply reimburse for actual costs? Most policies are indemnity plans which can cover incidental costs versus reimbursement contracts which cover actual costs. Reimbursement plans generally pay less, but cost less.
- What is the daily benefit for home care and assisted living? Typical policies cover these conditions at 50 percent of nursing home benefits. Unfortunately, the cost of either can meet or exceed nursing home expenses.
- Can benefits be used as a pool of money for both nursing and assisted living/home care? A pool of money may use the maximum benefits of the policy sooner but at least the cost of both assisted living and home care is covered for the meantime.
- Can the benefit amount be increased later? If so, will underwriting be required? This can be a valuable option for meeting unanticipated care down the road. However, added benefits are usually associated with higher premiums, especially if the new insurance is written at the insured’s attained age.
- Can the benefits be decreased if the cost of the policy becomes too much to pay? Coverage will drop, but at least some benefits will be paid.
- Can benefits be purchased jointly for a married couple? The discount is typically 10 to 15 percent.
- Is a survivorship benefit available? Some insurance policies that cover both spouses have a “survivorship” benefit. Under a survivorship benefit, when one spouse dies, the other owes no further payments, as long as the policy has been in force for at least ten years.
- Will benefits be paid if the caregiver is a friend or family member? What about caregiver training? Some policies allow this under home care benefits. The daily benefit for informal care is typically one-half the home care benefit.
- How much does home care coverage add to the premium? Home care benefits are typically one-half the nursing home benefit but could raise premiums by 30 percent or more. Policies where home care benefits equal nursing benefits will probably increase rates about 50 percent.
- Is the premium for benefits more than 5 percent of the client’s income? Some industry analysts believe that the cost of long term care should not exceed this threshold.
- Are premiums guaranteed to stay level? It’s doubtful. Clients should know that rates can increase by state residency or by class of policyholder. Some say that clients should prepare for an average 50 percent increase over time.

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Remember, extremely low premiums today, might guarantee rate increases later.

- Is there a limited pay or “paid-up” feature? Non-forfeiture or paid-up features are an option that clients should know about. They can be expensive now but useful later, e.g., a working couple with strong income today can retire with a paid-up policy.
- Is there a restoration of benefits clause? If a policyholder receives care in a nursing home and recovers, the policy benefits may be restored to the original level.
- Does the insurer count days or years? Most benefits are expressed in years but insurers actually count days. In some cases insurers will count three or four days as a week. This is a completely unacceptable condition.
- Do benefits paid through an HMO count as a full day? Although it is rare, some policies count a day of care provided through an HMO as less than a full day. This could be a bonus for the insured.
- Do home health care and adult day care benefits pay for a full day? This can be important to the relief and effectiveness of the primary caregiver.
- Do nursing home/home health care benefits increase automatically? Nursing home costs have been increasing between 8 and 9 percent since 1985. A cost of $110 per day today will run up to $513 in 20 years at 8 percent inflation.
- Is the increase based on the Consumer Price Index, Medical Price Index or is it fixed? No one knows the future, but if benefits at least kept pace with inflation the policyholder should have some form of additional protection against rising costs.
- Is there a “cap” on the amount benefits can increase? Beware of companies that “cap” their inflation increases to two or three times the base benefits.
- Are future benefit increases available on demand? Some policies offer the option to increase benefits every so often at the client’s attained age. Look for additional underwriting and be alert to any condition that eliminates this option if it has been offered and refused by the policyholder a specific number of times.
- What kind of inflation protection is offered? Protection can increase at 5% compounded or 5% simple. The corresponding increase in premium would be about 60% and 50%. A daily benefit of $110 today will grow to $292 in 20 years at 5% compounded vs. $220 under 5% simple.
- What is the cost of waiting to buy inflation protection later? Policies that allow the purchase of additional coverage later can be cheap today but expensive down the road. A 65-year old might pay only $770 today for a policy with optional increases compared to $1,598 for one with automatic protection. In 20 years, however, the policy with optional increases could cost over $5,000 compared to the same $1,598 for automatic benefit increase protection.
- If inflation protection is too expensive for a client today, is it cheaper to just increase benefit levels? Perhaps. A premium for higher benefits but no automatic inflation protection will most likely cost less today. The risk taken is that clients may be unable to afford the coverage needed in 10, 20 or 30 years or simply have to accept lower benefit levels than would have been provided with automatic protection. These are trade-offs that need to be discussed with clients.
• Are bathing and dressing on the list of daily activities? If a bathing or dressing disability is a trigger of coverage, policyholders will have a much easier qualification and will qualify sooner since these are two of the first daily activities that chronically ill people are likely to lose.

• Are activities explained in different ways than other policies? Some define an eating disability as the inability to feed oneself while another may define it as the need for someone to watch over the party eating. Look for clarification on all activities of daily living as well as terms like: assisted living, walking or wheeling, cognitive impairment, ambulating, transferring, etc.

• Does the policy assess physical activities on a “standby” or “hands-on” basis? IRS 97-31 rules clarify the difference: “Hands-on” assistance means the physical assistance of another person without which the individual would be unable to perform the ADL. “Standby assistance” means the presence of another person within arm’s reach of the individual that is necessary to prevent, by physical intervention, injury to the individual while the individual is performing the ADL. Policies that cover only individuals requiring “hands-on” assistance would generally provide fewer benefits than one that included “standby assistance”.

• Will the policy pay on a “medical necessity”? Patients can be too frail to care for themselves from a medical condition like coronary disease, yet still able to perform daily activities. “Tax qualified” plans do not recognize medical necessity.

• Are there special underwriting definitions? One company uses the term “standard” to describe its worst class. For another, it means mid-grade.

• Is there “lifestyle” underwriting that will automatically cause an application denial? One company says that anyone who needs assistance with housekeeping, shopping and household finances is simply unacceptable.

• Does the policy require special equipment installation before benefits can begin? Some insurers may require the insured to install grab bars or a shower stall in place of a tub before they will pay benefits. These restrictions are not favorable to the policyholder.

• What are the measures of cognitive impairment? Look for methods that fairly measure cognitive impairment using terms like thinking, reasoning, remembering, memory, etc. HIPPA provisions measure cognitive ability based on whether the individual needs “substantial supervision” to protect himself from threats to health and safety.

• Is cognitive impairment measured separately from physical measures of ability? A company that uses physical methods to determine cognitive assessment may overlook people who can pass the test or perform daily activities but forget how or why they did them. Worse yet, their mental impairment could become a threat to how they do them in the future.

• Does the policy pay for home care alterations? Some will pay for stair lifts, ramps, grab bars, etc.; allowing an insured to receive care at home.

• Is there a return of premium or non-forfeiture option and how much does it cost? Clients are always concerned about paying insurance premiums and getting nothing in return. Offering them this option may increase premiums by 30 to 50 percent, but they will be certain to get something out of the policy.

• Is there a vesting schedule on any return of premium? Return of premium riders typically start or “vest” after five years. Some return more as the years
go by. The return of premium is paid upon termination of the policy by lapse or death.

- Determine how the policy’s non-forfeiture options work. Non-forfeiture options will either return premiums or pay benefits. The benefit may be purchased as “full” (it accrues regardless of claims paid) or “limited” (claims are subtracted from any premiums or benefits paid).
- Non-forfeiture and return of premium options may be better suited to the policyholder who doubts he will use his coverage but still wants something out of the policy. He would have discretionary income and liquid assets to make the increased premiums. In essence, the cost of these additional options represents a potential loss in the time value of money.
- Is there a cognitive reinstatement option? Where mental impairment has set in, policyholders may forget to make premiums payments and risk cancellation. This clause allows reinstatement for up to five months so long as all back payments and proof of cognitive impairment is made.
- What about other useful policy features? Some examples of options to discuss with clients include bed reservation (If an insured goes home, bed space is reserved in case he returns within a specified period) for nursing homes, waiver of premium, respite care and survivorship benefit.

ANNUITY ANALYSIS

Sales conduct concerning annuity investing first involves fact finding to determine what portion, if any, annuities should play in a client’s overall financial plan. Next, a needs analysis should be conducted to uncover growth vs. income requirements, risk tolerance, liquidity specifications, now and in the future, and whether tax deferral benefits are worthwhile to pursue.

Who should invest in annuities? One rule of thumb follows that a client looking for a long-term investment with a tax bracket greater than 15 percent might consider annuities. Other likely candidates include moderate or high tax bracket individuals looking for a conservative way to shelter current income or growth over a long period of time, i.e., retirement monies.

Fixed rate annuities might be an alternative for CDs, GNMA (Ginnie Maes), TBills or other similar obligations. Variable annuities are better geared to individuals who seek tax deferral, yet willing to ride with the ups and downs that accompany stock and mutual fund investments.

Once an annuity can be established as an appropriate investment opportunity, agents must carefully weigh the following choices and discuss same with each client:
Immediate Annuity vs. Deferred Annuity

Clients may have current income needs or the desire to defer income for greater growth. Perhaps a combination is appropriate. Tax planning and liquidity are key considerations for the agent.

Single Premium vs. Flexible Premium

Client's generally have a lump sum to invest or need to accumulate by paying into a savings plan. Short and long-term liquidity is an important consideration.

Fixed Rate vs. Variable Rate

Client's may have needs to lock-in their yields or go for growth. One group is typically a CD type investor as opposed to those who are willing and able to incur greater risk. Agents need to carefully explain the potential loss of principal possible in variable plans. Agents should review potential interruptions in return of principal and yield that can develop with either fixed or variable contracts.

Yield vs. Guarantees

It is logical that the stronger the guarantee the lower the yield. Agents must explain that a higher first year yield may include bonuses or special incentives to invest that later disappear. This type of contract should be compared to other contracts that may offer a slightly lower yield that is locked in for a specific period, i.e., determining overall predictable yield over time is important due diligence.

In the same vein, a disclosure would be appropriate as to the method used by the insurer to adjust yield. A contract with a guaranteed yield spread may be more appropriate for some clients than a yield that is adjusted by the insurer's board of directors.

Equally important is whether yield is banded, i.e., are yields adjusted separately for certain blocks of investors or are investors who entered five years ago given the same yield as new investors.

Yield vs. Liquidity

Clients demanding easy access to their money should be prepared to settle for lower overall yields. Agents need to go farther to determine special needs such as the potential for large sums of money to pay for a potential illness or nursing home. Certain contracts allow penalty free withdrawals for special circumstances.

Due care dictates that agents carefully and clearly explain all surrender charges associated with the contract and when they occur.
Maturity options

Annuity contracts may mature at specific ages. This can affect both a client's long-term investment planning as well as tax planning. A client wishing to plan for long term deferral to age 95, for example, might be disappointed to learn that the contract must annuitize at age 85. Further, agents must disclose the potential tax effect of a maturing annuity.

Pre-1981 Annuities deliver principal first, then tax interest or appreciation. Post 1981 annuities tax interest or appreciation first then deliver principal. Also to be considered is annuitization of the contract where a systematic withdrawal and payoff of the contract over time delivers some principal and taxes interest and appreciation with each payment.

Withdrawals & IRS Penalties

Where the client is withdrawing all or part of an annuity contract PRIOR to age 59½, he should be apprised of the 10% IRS penalty for early withdrawals. At present, this can only be avoided where the annuitant dies, becomes substantially disabled, or where annuitization is chosen over a minimum five-year period.

Guaranteed Death Benefits

Where agents assist in estate planning, due care would involve a disclosure concerning death benefits. Most fixed rate contracts guarantee the return of principal and any appreciation (interest left to grow). However, agents should uncover and review factors concerning potential surrender penalties or how they may be avoided, as well as the basis of the guarantee (e.g. is the death benefit guarantee, for example, the greater of all contributions of principal or simply the value of the contract on the date of the annuitant's death?).

Settlement Options & Taxes

Clients should be made to understand that, at best, annuities represent tax deferral, not tax-free income. Unless the beneficiary of the annuity is a surviving spouse, taxes on the accumulated growth will be due. There is no step-up in basis. The tax liability is the difference between the amount invested subtracted from the value of the annuity contract, multiplied by the beneficiary's tax bracket.

Options to mitigate this include five year or lifetime annuitization of the contract. Other settlement options that should be discussed with the client include possible options such as life annuity, joint and last survivor, lifetime with period certain, etc.
State Guaranty Fund Coverage

Rules governing state guaranty coverage should be disclosed to the client. If the State does not permit advanced disclosure concerning guaranty fund protection, the agent should privately exercise diligence in planning annuity purchases.

The primary concern is whether the full amount of the annuity is covered against insurer failure. Perhaps due care is served by diversifying among several insurers and/or between fixed and variable contracts to take full advantage of guaranty protection.

**Essential Annuity Due Care Questions**

- Is the client interested in growth or income?
- Is the client interested in current income or retirement income? How soon does he need to start receiving income?
- How much risk is the client ready to accept today and in the future? Could he stand the loss of his entire investment? How would an interruption in income affect him?
- What are the client's liquidity needs in the short-, intermediate- and long-term?
- What is the client’s federal/state tax bracket? Does tax deferral through annuities make sense?
- Is the client under age 60, and is it likely that he will need to withdraw major portions of the annuity in the future? Will the ten percent penalty offset the benefits of tax deferral?
- Does the client demand full and complete protection of principal? Or, can the client afford to take risk in hopes of greater appreciation using variable contracts?
- Is the preservation of principal more important to the client than the effects inflation may have against a fixed yield?

What are the survivor spouse/family needs in the event the client dies? How can these needs be accomplished?

**DISABILITY INSURANCE**

Statistics have surfaced which indicate that the average person is 3 times more likely to suffer a lengthy disability than die. Providing a source of financial income in the event of a major disability is probably the most overlooked portion of client financial planning. By definition, a disability can be a temporary or permanent loss of earned income due to illness or accident.

**Essential Disability Due Care Questions**

- How much monthly protection is needed? Is an individual policy needed to supplement work plans?
- When does protection need to start? (30, 60, 90 days, etc. -- the elimination period), i.e., can the client "self-insure" for a period of time?
• Does the client have discretionary income to buy needed protection?
• Is the coverage non-cancellable or guaranteed renewable? Can a block of insureds, including your client, be canceled?
• If multiple policies are owned (employer, association, individual), will the benefits of one be reduced by the other? Is there a case for eliminating a policy?
• Is there an employer supported uninsured sick-pay plan available?
• What is the definition of a disability in the client's policy? How severe? How long?
• Does the policy include occupational and non-occupational coverage?
• Is there a substandard rating or waiver of condition? Will the company remove it? Will another company write without a waiver?
• Is there a waiver of premium benefit? Would this be necessary for the client?

Similar to life insurance, due care analysis by the agent involves "need analysis". Through inquiries and available financial papers, the agent should determine the current after-tax income needs of the client. This amount could be reduced by expenses that might be eliminated due to the disability. For example, if the client is homebound, he will not need to cover transportation costs of commuting to work or other work-related expenses. Next, an adjustment for possible government benefits can be made using amounts that might be available from Social Security. Minimum employment history and limitations on the term of protection covered should also be considered. Other adjustments that an agent should investigate include earned income continuing from other family members, investment income that might be derived from current assets and inflation to keep pace with cost of living increases.

For just about every client, the above process will establish that some form of disability protection is generally needed beyond the limits granted social security, and in some cases private, employer provided protection. Once a disability need is established, it can be compared to the participation limits allowed by insurers and the ability of clients to afford it.

Disability sales conduct would involve an agent/client discussion explaining how disability insurers may only offer certain maximum allowable coverage tied to income, e.g. a client who earned an after tax monthly income of $7,500 might be eligible for a maximum of $3,000 of monthly disability coverage.

There may also be limits of how long this protection is covered, e.g., 24 months, 5 years, or to age 65. Further, there may be minimum waiting periods before coverage begins, e.g., 90 days, 180 days, etc.

Also, there may be reductions in the amount of disability protection paid based on the degree of the disability, e.g., a partial disability that allows a client to continue working may reduce benefits substantially. Finally, watch for renewability features.

Clients need to be counseled that the "gaps" in coverage outlined by these events require them to seek alternative forms of protection, develop contingency plans or rely
on available pension plans, family members and accumulated savings to make ends meet during times of disability.

**PROPERTY & CASUALTY INSURANCE**

Risk management in the property and casualty arena is extremely complicated, yet the primary goal is the same as other forms of insurance: the transfer of risk. However, a higher standard of due care and agent liability exist in property/casualty because of binders, indemnity disputes and redlining.

A binder can be written or oral. At the point when the client says, "I want it" and the agent says, "You're covered", a binder has occurred. Immediately upon creating any oral binder, the agent should make note of the terms of coverage, when the binder was made and the parties involved. Further, to reduce the possibility of disputes, the agreement should be reduced to writing as soon as possible. Abuses occur where agents do not have binding authority yet lead clients to believe they do. Likewise, clients may use binders as a means of obtaining free insurance for limited periods.

Property and casualty insurance contracts are contracts of indemnity in that they provide for compensating the insured for the amount of loss or damage. Due care is accomplished when an adequate amount of compensation is provided that will avoid profit or loss from a peril or hazard.

Elementary insurance defines a peril as the cause of a loss. Fire, lightening and collision are all examples of perils. A hazard is anything that increases the chance of loss. A loose gas connection to a main heater system is an example of a hazard.

Hazards, however, can also take shape in "morale" form. Reckless driving is one such example of a morale hazard. While there are, as yet, no formal rules on insurance redlining, there is pending legislation that would force insurers to comply with rules similar to Community Reinvestment requirements now imposed on banks. If passed, a majority of the burden would fall on underwriters. However, agents should be aware that clients living in inferior, low income or minority communities should not be denied application for coverage. The logic behind this is obvious. Without access to insurance, clients would not be able to buy housing.

Compared to life and health contracts, it can be said, that fewer property/casualty policies are read by clients. This is generally caused by a lack of understanding of liability or casualty matters, and therefore, a greater reliance is placed on agent advice and counsel. That is why proper sales conduct would encourage clients to read their policies and help them review the fine print to fully understand exact limits of coverage, define perils, clarify what constitutes a hazard and recognize policy owner duties. Having specimen policies available for this purpose should be standard procedure.

Areas where agents should exercise additional due care involve the "agent as counselor". Insurance is the first line of defense in asset protection. The role of the property/casualty agent in preserving what clients have already accumulated is vital.
This should not occur, however, without also recognizing the value of other forms of insurance.

A deluxe homeowner’s policy should be scaled back where high premiums might not allow clients to purchase basic health insurance. There may also be validity to the argument that insurance premiums should not be so excessive as to preclude clients from starting necessary retirement savings plans.

In addition to these points, there are many contributions that can be made by agents to promote greater client understanding of risk, loss control and proper valuation. By educating clients in these disciplines, a higher level of insurance efficiency will be realized. The result can be stabilized or lower premiums through a lower claims experience.

**Essential Due Care Questions Regarding Liability:**

- What is the insured’s "insurable interest"?
- Is the peril covered?
- Is the property covered?
- Is the type of loss covered?
- Is the person covered?
- Is the location covered?
- Is the time period covered?
- When does the policy take effect?
- Are there hazards that exclude or suspend coverage?
- What are policy owner’s duties after a loss?
- What are the insurer's options in settling a loss?
- What are the time limits for the policy owner to recover from the insurer?
- What are the time limits for the insurer to pay a claim?

Next, a discussion to help determine the needs of the client and to explore the client’s perception of risk, loss control and valuation might include:

**Risk**

A client's perception of risk influences how insurance dollars are spent and, to some extent, how the industry is regulated. Unfortunately, much of society has set a low priority on reducing risk relying on the motto: "That's why I buy insurance". Many in the industry, however, feel it is extremely important to reassess societal views on risk by assuming more responsibility for risk consequences. An example would be clients who continue to build in flood plains or high-risk fire areas, despite knowledge of their existence. When disaster strikes, should these individuals receive subsidies through taxpayer financed state and federal disaster aid, government flood control projects and mandatory shared-market insurance programs?
Should accident victims who violate seatbelt laws receive full compensation? Should people who live in hurricane and earthquake country be responsible to better secure a structure with inexpensive metal ties? Some believe that people must realize what they can do for themselves before risk priorities can change. Agents can play a valuable role in helping clients accept a certain level of risk and strategies to reduce it.

**Loss Control**

In the insurance industry, the process of risk reduction is called loss control. Loss control procedures involve the steps necessary in eliminating exposures to risk and reducing their frequency or severity. Today, loss control makes the workplace safer and reduces a broad range of liability exposures in homes as well. Offering loss control advice and services to clients has potential rewards as well as risks.

Reasons agents might consider advising clients on safety issues include: client credibility, client retention, new client generation, insurer qualification and attractibility, favorable insurer status and additional profits where "advice fees" are permitted by law.

With competition stiff, some larger agencies are establishing entire subsidiaries to perform loss control-for-fee services. In these cases, loss control fees can represent from two percent to ten percent of total agency revenues. Smaller companies may contract to outside loss control consultants or simply rely on insurer provided services. Loss control services can run the gamut from standard, non-controversial safety recommendations to complicated compliance advice.

Whatever level of service provided to attract or retain clients, agents should realize that loss control advice exposes him to additional liability. There may also be statutory violations, particularly in the commercial area, for offering safety expertise without required licensing.

Code compliance is an extremely important area of loss control. It is a discipline usually reserved for underwriters and typically outside the venue of agents. This does not mean it should be ignored by the agent. Due care should involve the agent at least to the extent of a physical inspection of the property to determine that fire sprinklers are indeed in place or that a security fence has been installed around a construction site before delivery of materials.

The importance in doing so is underscored by a mitigation of exposure when an accident hits: particularly by third parties.

**Valuation**

A recent survey by a well-known real estate statistics firm found that almost 70% of the homes in the U.S. are underinsured by an average of 35%. With an increased awareness of this problem, many insurers of large policies are sending appraisers to high value neighborhoods to determine if policy replacement values adequately reflect current values.

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In addition, companies are directing it encouraging agents to re-evaluate coverage levels. In many cases, this involves inspections of properties to account for recent improvements, such as finished basements, patio covers, garage conversions; deterioration; code compliance to rebuild; i.e., new hurricane or earthquake standards; and illegal uses (a business run out of the home).

Bringing inadequately covered premises to full coverage levels increases underwriting income, which may allow a carrier to lower rates within a class of policy owners. Equally important is the liability protection afforded carriers and agents.

**HOMEOWNERS INSURANCE/CONDOMINIUM UNIT INSURANCE/RENTER’S INSURANCE**

**HOMEOWNERS**

Agents should exercise due care in several important capacities:

**Selection of Policy**

The selection of policy type (HO-1, HO-2, HO-3, HO-4, HO-6 and HO-8) should be a function of client need. Obvious factors to consider include dwelling type, dwelling size, dwelling construction, dwelling replacement, additional structures, type and extent of personal property, loss of use and basic liability.

Refinement of the process occurs where agent due diligence uncovers the client’s true "limits of need" and special circumstances. This can only be accomplished by interview or systematized fact finding concerning key issues:

**Value**

The amount of dwelling insurance requested is typically a reflection of the mortgage amount. Does this reflect the true replacement value? Is an appraisal in order for larger policies or where a special construction has been used?

Remember, like kind and quality does not mean "exact" kind and quality. Clients must understand that replacement cost is limited to the style, quality and function of the destroyed or damaged property. Few or no allowances are made for increased costs of repair or reconstruction caused by ordinances or laws regulating construction or repair. An example is new construction school fees or special fees that are currently charged for construction that were not around when the client's house was built. Concerning personal property, does an inventory exceed policy limits? Is replacement value available? Should items be "scheduled" like paintings, historical documents, original manuscripts, exotic pets, etc.?

Are "sub-limits" of the policy meeting client needs, cash, gold, coins, stamps, securities, deeds, trailers, jewelry, watches, furs, precious stones, silverware, guns, etc.?
After primary values are established, the client's "insurable interest" must be determined since a policy owner will not recover for an amount greater than their insurable interest.

**Eligibility**

Due care discussions with clients should cover circumstances where their eligibility to recover a claim may be jeopardized.

- Is the policy owner the intended owner occupant or does he intend to rent the property? Will only one family occupy?
- Is a business being operated out of a home?
- Are there code violations like additions without permits, zoning violations, etc.?
- Will the client be able to perform his duties to mitigate losses (draining pipes to prevent freezing, maintaining heat if the structure is vacant, minimal repairs to protect the property from further damage, etc.)?
- Is a detailed inventory necessary to track descriptions, purchase dates, values, etc.?
- Are clients aware that they should hold on to damaged property and make it available for adjuster inspection?
- Do clients need to produce books of account or fill out a proof of loss?
- Will the client be available to assist and cooperate with the adjuster?
- Are insureds aware that they should not make any voluntary admissions of guilt or make voluntary payments to someone they have injured?
- Many of these circumstances can be brought to surface in an initial meeting or physical inspection of the property.

**Deductibles**

Clients should be apprised of their deductible options. Although higher deductibles mean lower premiums and lower agent commissions, they represent a fair opportunity for clients to accept part of the financial consequences of risk taking. This, in turn, can lead to fewer claims and a generally more stable client.

**Policy Exclusions**

If the policy is in "readable form" it should be easier for the client to pinpoint policy exclusions. Some obvious disclosures, however, should include exclusions related to damages caused by earthquakes, flooding, sewer flooding, flooding driven by wind, power interruption, owner neglect, war, freezing of appliances or pipes (especially if vacant over 30 days), theft from a dwelling under construction, breakage of glass if vacant over 30 days, continuous or repeated seepage from plumbing or heat & air system, normal wear & tear, latent defects, mechanical breakdowns, rust, mold, wet or dry rot, contamination, smog, settling, cracking, expansion of pavements, patios, foundations, walks, walls, floors, roofs or ceilings, rodent or pest infestations.
Liability & Liability Exclusions

Primary to determining liability limits is the client's overall exposure. What is his or her personal net worth that could be at risk? Will the limits of the policy or an umbrella cover the exposure? Are there any liability exclusions in the policy that leave the client uncovered?

Some common areas of neglect include: Boats over 50 horsepower, aircraft, motor vehicles loaned or rented by the insured, certain professional services, most business pursuits, outside premises, cases where insured is liable for worker's compensation, for damage to property used by or rented by the insured, etc.

CONDOMINIUM UNIT INSURANCE

Your client may ask, “Why do I need Condo Insurance?” You may want to explain that whether it be a single-family dwelling or a condominium unit, it is usually the largest investment that most individuals will ever make; it is typically the largest asset on the family balance sheet. Also, the contents of a typical home/condo, in the form of furniture, appliances, clothing, family heirlooms and other movable personal belongings represent a substantial additional investment. An unprotected loss or partial loss of a home/condo and its contents, to theft, fire, windstorm or some other disaster could be financially devastating to your client.

Another aspect of condo insurance is the risk of personal liability. An example would be if a visitor to the residence would slip and fall. Your client needs to realize that such accidents can result in court decisions awarding large sums to the injured party for medical expenses as well as pain and suffering.

When determining the needs of your client, it may be a good idea to explain that the protection available under a condo unit owner's policy differs from a typical homeowner's policy primarily in the type of coverage provided for the dwelling. A typical condo unit owner’s policy can provide coverage as stated below, remembering that specific coverage and terms of a policy can vary from company to company and state to state.

- **Condo Unit**: This section of the policy would provide protection for the unit owner’s real property as is also referred to as “unit owner’s additions and alterations.” (this has also been described as “from the bare wall in). The items included here will vary with state law, but can include such interior furnishings as wallpaper, paneling, kitchen and bathroom cabinets, carpeting or wet bar. Coverage is generally provided on a named-peril basis for an additional premium.
- **Other Structures**: These might include a detached garage or tool shed, if owned solely by the insured.
- **Personal Property**: Covers the contents of the unit, such as furniture, appliance or clothing. Certain types of property may have specific dollar limits (jewelry,
silverware, securities, cash and collectibles are examples of personal property subject to the internal policy limits). When determining the needs of your client, your client needs to be aware that as far as personal property is concerned, that the standard policy will insure the condo unit for actual cash value, e.g., replacement cost less an allowance for depreciation or wear and tear. The client should also be made aware that for an additional premium, the policy can be endorsed to protect covered property on a replacement cost basis (the cost to buy the item new today), without considering depreciation.

- **Loss of Use or Additional Living Expenses:** If a condo unit is damaged by a covered peril, loss-of-use coverage helps meet the costs of hotel bills, apartment rental or rental home, eating out and other living expenses while the home is being repaired.
- **Personal Liability:** Provides protection against legal liability for bodily injury or property damage if a third part is accidentally injured.
- **Medical Payments:** Also known as guest medical payments, this section provides coverage if a third part is accidentally injured and needs medical treatment.
- **Loss Assessment:** If the homeowner’s association suffers a loss, it may assess each owner to pay a portion of the loss. If the loss were the result of a covered peril, this policy provision would pay the insured’s portion of the assessment, up to the limit specified in the endorsement.
- **Inflation Guard Rider:** A standard policy can usually be endorsed to provide for an automatic, periodic increases in policy limits. The increases in policy coverage would generally apply to both the dwelling and the contents and help prevent your client from being underinsured due to inflation.

**Policy Exclusions**

When determining your client’s needs, it is also important to discuss what the policy will not cover or the specific exclusions from the standard policy and that a separate endorsement with payment of an additional premium may be available. Typical policy exclusions include the following:

- **Earth Movement:** Losses caused by an earthquake, a volcanic eruption or a landslide.
- **Water Damage:** Refers to damage from water that backs up from sewers or drains or water seeping through walls. Some policies contain dollar limits for water damage due to such things as a broken pipe.
- **Flood Damage:** Refers to damage from rising water, mud slide or wave action.
- **Mold Exclusion:** Due to high claims activity for losses caused by mold, many insurance companies are excluding coverage for mold damage.
- **Other Exclusions:** Such as wear and tear, war, nuclear hazard, neglect and intentional loss.
Once you have discussed and determined your client’s needs, be sure that you have at least answered the following questions in the conversation with your client:

- What perils are covered?
- What perils are not covered?
- What are the limits of coverage?
- What are the deductible amounts?
- In the event of a loss, what are your duties to the insured (how you, as the agent, would assist with the claims process).
- Have I explained the availability of endorsement?

RENTERS INSURANCE

Your client may ask, “Why do I need Renters Insurance?” You may want to explain that whether it be a single-family dwelling, a condo unit, apartment, etc., the contents of the property in the form of furniture, appliances, clothing, family heirlooms and other movable personal belongings represent a substantial investment. An unprotected loss or partial loss of the contents, to theft, fire, windstorm or some other disaster could be financially devastating to your client.

Another aspect of renter’s insurance is the risk of personal liability. An example would be if a visitor to the residence would slip and fall. Your client needs to realize that such accidents can result in court decisions awarding large sums to the injured party for medical expenses as well as pain and suffering.

When determining the needs of your client, it may be a good idea to explain that the protection available under a renter’s policy differs from a typical homeowner’s policy primarily in the type of coverage provided for the dwelling. A typical renter’s policy can provide coverage as stated below, remembering that specific coverage and terms of a policy can vary from company to company and state to state.

A typical renter’s policy (specific coverage and terms may vary from company to company and state to state) can provide insurance protection for the following:

- Personal Property: Covers the contents of the home, such as furniture, appliance or clothing. Coverage is generally provided on a named-peril basis. Perils that are not names are excluded from coverage. Certain types of property may have specific dollar limits (jewelry, silverware, securities, cash and collectibles are examples of personal property subject to the internal policy limits). When determining the needs of your client, your client needs to be aware that as far as personal property is concerned. The client should also be made aware that for an additional premium, the policy can be endorsed to protect covered property on a replacement cost basis (the cost to buy the item new today), without considering depreciation.
- Loss of Use or Additional Living Expenses: If a rented home is damaged by a covered peril, loss-of-use coverage helps meet the costs of hotel bills, apartment
rental or rental home, eating out and other living expenses while the home is being repaired.

- **Personal Liability:** Provides protection against legal liability for bodily injury or property damage if a third party is accidentally injured.
- **Medical Payments:** Also known as guest medical payments, this section provides coverage if a third party is accidentally injured and needs medical treatment.
- **Building Additions and Alterations:** Covers improvements, fixtures or alterations made by your client, such as paint, wallpaper, carpet, drapes and blinds.
- **Inflation Guard Rider:** A standard policy can usually be endorsed to provide for an automatic, periodic increases in policy limits. The automatic increases in policy coverage would help prevent your client from being underinsured due to inflation.

**Exclusions**

When determining your client’s needs, it is also important to discuss what the policy will not cover or the specific exclusions from the standard policy and that a separate endorsement with payment of an additional premium may be available. Typical policy exclusions include the following:

- **Earth Movement:** Losses caused by an earthquake, a volcanic eruption or a landslide.
- **Water Damage:** Refers to damage from water that back up from sewers or drains or water seeping through walls. Some policies contain dollar limits for water damage due to such things as a broken pipe.
- **Flood Damage:** Refers to damage from rising water, mud slide or wave action.
- **Mold Exclusion:** Due to high claims activity for losses caused by mold, many insurance companies are excluding coverage for mold damage.
- **Other Exclusions:** Such as wear and tear, war, nuclear hazard, neglect and intentional loss.

Once you have discussed and determined your client’s needs, be sure that you have at least answered the following questions in the conversation with your client:

- What perils are covered?
- What perils are not covered?
- What are the limits of coverage?
- What are the deductible amounts?
- In the event of a loss, what are your duties to the insured (how you, as the agent, would assist with the claims process).
- Have I explained the availability of endorsement?
**AUTO INSURANCE**

For most Americans, the automobile is a beneficial and essential part of modern life. Owning or operating a car, however, can also be a source of serious financial risk. Personal liability arising from losses suffered by others, or the cost of repairing or replacing a damaged or stolen vehicle, can be very expensive.

Also, most states have a compulsory auto liability insurance laws, requiring auto owners to maintain liability insurance as a condition of licensing or use on public roadways. Other states require auto owners to show proof of financial responsibility before and after an accident.

Auto policies are typically divided into different segments covering liability, medical, uninsured motorists and damages (comprehensive, collision, towing, labor and transportation expenses). Insuring agreements traditionally offered "split limits" which apply to each person for each occurrence of liability, damage, etc.

Today, the trend is more toward a single limit of liability, which can be expanded within the policy or through the addition of umbrella coverage, that applies to all covered liability losses arising out of an accident regardless of the number of persons injured or the amount of separate property damage.

**Coverage Under the Policy**

When discussing auto insurance with your client, he/she should be made aware of what the typical coverages include. Typical coverage would usually include the following:

- **Liability Insurance:** Coverage that protects the owner against losses from legal liability arising from bodily injury or property damage caused by an automobile accident. The coverage can be a single limit ($100,000 for each accident) or split limits such as $50,000/$100,000/$25,000 (per person/per accident for bodily injury/property damage).
- **Medical Payments Coverage:** This provision pays medical or funeral expenses because of bodily injury. The coverage is generally in increments of $1,000 to $5,000 up to $25,000 per person per accident.
- **Physical Damage Coverage:** This section of the policy is designed to cover physical damage to the insured auto. Collision covers, as the name implies, collision losses. Comprehensive (also known as other-than-collision) insurance covers losses from non-collision incidents, such as theft, fire or storm damage. Losses for physical damage are general based on the cost to repair or replace the damaged or stolen vehicle.
- **Uninsured/Underinsured Motorist:** Even though many state have enacted financial responsibility laws, not all automobile owners comply. Uninsured motorist coverage pays for injuries sustained in an accident with uninsured (or a hit-and-run) driver. (Note: In some states, uninsured motorist property damage is also included.) Underinsured motorist insurance covers the difference between...
the actual losses sustained and what an insured individual can collect from an at-fault uninsured or underinsured driver, up to the policy limits.

When evaluating your client’s needs, you may want to suggest/recommend adding additional coverage. There are a number of additional coverages that can be added (usually by endorsement) to a basic policy to provide insurance for unusual situations or to protect other types of vehicles. Two of the most common endorsements include:

- **Extended Liability:** Used to cover automobiles that are not legally owned by the insured, such as an auto furnished by an employer for the regular use of the insured and/or the family. This endorsement extends the policy coverage to situations involving non-owned vehicles, which standard policy provisions would otherwise exclude.
- **Miscellaneous Type Vehicle Endorsements:** This would allow your client to insure vehicles such as snowmobiles, motorcycles, motor scooters, go-carts, golf carts, antique and classic cars, motor homes and campers. In some states, however, a separate policy is used to cover these vehicles.

**Understand the Policy**

An insurance policy is a written contract between your client and the insurance company. The protection provided by the policy typically represents a significant part of your client’s overall risk management program. It is important for your client to read and understand key policy provisions to be sure that you have correctly discerned the needs of your client. The questions below should be addressed and reiterated to your client, even if he/she does not actually ask them:

- What perils are covered in the policy? A basic policy may not provide as much protection as is necessary.
- What perils are not offered? For an additional premium, coverage for excluded perils or situations can often be added to a policy.
- What are the limits of coverage? The maximum dollar amount the insurance company will pay in the event of a covered loss.
- What are the deductible amounts? A deductible is a dollar amount your client must pay before the insurance company pays its portion.
- In the event of a loss, what are the duties your client? A policy will usually list the steps that must be taken in the event of a loss.

**Minimum Due Care Considerations in this Area Include:**

**Policy Limits**

A needs analysis to determine that liability limits of the policy adequately shield client assets and meet financial responsibility laws of the state which may assign specific minimums relating to liability, bodily injury, property damage and/or uninsured motorist coverage.
Policy Eligibility

Clients should be apprised of the specific vehicles eligible for coverage, e.g., private passenger autos owned or leased, longer than six months, and those which are not eligible, e.g., less than four-wheel vehicles, autos used to carry persons or property for a fee and those needing to be named as additional vehicles, e.g., trailers, off-road vehicles, etc.

Clients should also be advised that new or replacement vehicles must be reported within 30 days of purchase to receive full coverage. Clients with poor driving records should be referred to assigned risk plans or “fair” plans organized through state programs.

Policy Conditions

Agents should direct clients to specific areas of the policy pertaining to "duties of the insured after an accident". Clients should be told that they should promptly notify the company of the accident, the time limits within which they should act and steps that they should take to reasonably protect the covered auto from further harm or damage. Policy owners must provide sufficient evidence of loss, cooperate in any insurance investigation and notify the police if a hit-and-run driver is involved or if the covered auto is stolen.

Policy Endorsements

Clients should know the options they have to broaden their coverage to include coverage such as full replacement cost, towing and labor costs, rental reimbursements, specialized vehicle coverage, extended non-ownership liability, additional damage coverage for special vehicles, named non-owner endorsements, coverage for special personal property coverage for items like tapes, CDS, CBs, portable phones, etc.

Policy Exclusions

Due care discussions should also disclose, to clients, items of coverage specifically excluded from the policy. Examples include: property being transported, bodily injury to an employee of a covered person, motorcycles, off-road vehicles, etc.

Also excluded is coverage in areas outside the United States, its territories or possessions and Canada.

Clients should understand that an endorsement for extended coverage should be considered when traveling outside these domains.
Policy Effective Date

It should be clear that coverage begins at 12:01 AM standard time on the date of inception to 12:01 AM on the date of expiration.

Named Insured

Who is the insured? Is the insured the policy owner, his spouse, a resident of the household, other family members?

Auto User

Is everyone who uses the auto a named insured?

Associated Named Entities

What is the name of any other person or organization who may not use the auto but may still have legal responsibility for the acts of omissions of the covered insured?

BUSINESS INSURANCE

Disability of a Business Owner

Many business owners have created buy-sell agreements to protect themselves and their businesses in case of an untimely death. These agreements are often funded with life insurance to ensure that the cash to purchase the business is available when needed.

Permanent disability is another threat faced by business owners. Disability of an owner can create immediate issues as to who will operate and manage the business. Often, the risk of a permanent disability is not provided for in a buy-sell agreement in spite of the fact that the probability of a long-term disability prior to age 65 is greater than the probability of death.

To provide for this risk, business owners can amend existing buy-sell agreements or create separate agreements. Special disability insurance policies can be used to fund a disability buy-sell agreement. These policies can be set up to pay a lump sum, a series of payments or a combination of the two.

Key Elements to consider

- Definition of Disability: How disability is defined in the agreement is very important and should probably be tied to the definition in the disability insurance policy
- Elimination Period: The period of time between the first day of the disability and the trigger date, e.g., 12 months to 24 months are frequent options.
• **Trigger Date**: This is the date at the end of the elimination period when the buyout begins and the insurance company begins paying on the policy.
• **Successive disability**: A disabled person may temporarily return to work but thereafter have a recurrence of the disability. In many plans, successive disability periods can be tied together to meet the elimination period.
• **Funding Period**: The period over which the buyout payments are made. It can be an immediate lump sum or spread out over a period of months or a combination of both. The funding period set in the policy should match the terms of the buy-sell agreement.
• **Recover from Disability**: The recovery of a disabled person after the buyout has begun can raise several questions, among them:
  - Does the funding stop?
  - Can the person return to work with the same company?
  - Lump-sum settlement plans, in some cases can remove some of the uncertainty.
• **Buy-Sell Agreement**: The buy-sell agreement must be in force at the time of disability in order for payments to be made from the policy.
• **Converting to Individual Coverage**: Sometimes the disability plan will be convertible to individual coverage if the business has no further need for the coverage, the owner needs additional individual coverage and he or she meet certain requirements.
• **Involvement in the Business**: Many insurers require that the business owner be actively involved in the business.

**Business Overhead Expense**

Another form of disability insurance especially suited to the business owner is Business Overhead Expense (BOE). BOE policies are designed to reimburse certain business expenses of the owner while he or she is totally or partially disabled. The funds provided by the BOE policy help the business survive during the period of the owner’s disability. Often, the BOE policy is the reason the owner has a business to return to after the disability. Should the disability appear permanent, the owner usually has additional time to make decisions regarding the future of the business.

Generally speaking, there are only certain types of business owners who qualify for BOE coverage. These include owners of closely held businesses, owners of small businesses and professionals with their own practices.

Some of the expenses typically covered by a BOE policy include the following:

- Legal and accounting fees.
- Utilities.
- Principal payments on debt.
- Leased equipment.
- Business insurance premiums.
• Office supplies
• Salaries of non-owner, non-family employees
• Professional dues.
• Business taxes.
• Rent.
• Workers compensation.

In NO instance is there any payment from a BOE policy to the business owner. Instead, these funds must come from his or her own disability plan.

The risk managing agent recognizes that due care extends to businesses as well as individuals, since businesses are composed of the same people. The illness, disability or death of these people represent an exposure to businesses in terms of their survivability and commitments to principals, employees and their families involves a determination of the reduced revenues and increased expenses that may result from the death or disability of a key person in the business, including the possible costs to replace or sell the business, if necessary.

Sales conduct in business analysis involves a determination of the reduced revenues and increased expenses that may result from the death or disability of a key person in the business, including the possible costs to replace or sell the business, if necessary. The degree of risk protection in business insurance varies by the person who is affected and the legal structure of the company. Following are some due care considerations for three major forms of ownership: sole proprietors, partners and corporations.

**Sole Proprietorships**

There is no legal distinction between personal and business assets; debts of the business are debts of the sole proprietor's estate. Agents should determine needs or pre-loss arrangements of the surviving family to continue the business; sell it or liquidate it in the event of the owner's death or disability. Capital deficiencies can be filled through the appropriate insurance line.

**Partnerships**

The legal relationship between partners is personal; each is fully responsible for acts of the business and business debts of all others. If a partner withdraws or dies, the partnership must be terminated or re-organized. The disability of one partner can also create a significant financial strain on the entire business.

Due care planning here involves learning the wishes of the surviving family and surviving partners. Where a deceased or disabled partner's family wishes to exit the business, a buy-sell agreement can satisfy the purchase of his share with the business passing to the surviving partner. Alternatively, the heirs of the deceased may become partners or sell the lost partner's interest, assuming this is permitted in the partnership...
agreement. Again, pre-loss arrangements covering the possibility of reduced revenues and higher expenses during this transition must be considered.

**Corporations**

Most agents will deal with the "close corporation" where the stock is closely held by a few individuals and not offered for public sale. Typically, the stockholders are also employees of the company. In this case, situations similar to the partnership can develop.

A key employee or stockholder can become disabled or die creating additional financial burdens on the company. Most corporation charters provide that remaining stockholders can purchase the share of the withdrawing or deceased shareholder. The risk manager needs to uncover the "formula" for purchase and plan available funds via buy-sell policies, disability protection, health care, etc.

Other significant due care factors concerning business insurance include planning for taxes and liability. For planning purposes, most transfers or sales of business interest become part of your client's gross taxable estate for purposes of death taxes. Income taxes become a factor in corporations where the challenge is to transfer assets out of the corporation without claims of dividend. This is a very complicated area of planning best left to other courses.

**Essential Business Insurance Due Care Questions**

- Who will control the business when your client dies or becomes ill for an extended period?
- Will there be a market for the business if it has to be sold?
- Will the business provide adequate income for the heirs of your client?
- How will the value of the business affect the taxes and liquidity needs of your client's estate?
- Will the client be able to continue in business if one of his associates dies?
- How will working capital be kept intact where a partner or owner dies or is seriously disabled?
- How can a business be transferred to a new owner without shrinkage in value?
- What will become of your client's interest in the business if he or she retires?

**Employment Practices Liability Insurance**

Another type of business insurance would be Employment Practices Liability Insurance (EPLI). This began to be offered in the 1990s as one result of federal legislation such as The Americans with Disabilities Act, The Civil Rights Act of 1991, the Age Discrimination Act and the Family Medical Leave Act. Each of these acts established new, legal rights that employees had not held in the past. These new rights sometimes provided the legal basis for an employee, former employee or potential employee to sue an employer.
What Is It?

EPLI provides protection to an employer, including officers and directors, against claims made by employees, former employees or potential employees relating to many types of employment-related lawsuits. Examples of some of the types of claims typically covered by an EPLI policy are:

- Sexual Harassment
- Hostile work environment
- Discrimination (age, sex, race, religion).
- Wrongful termination as a result of downsizing, mergers or acquisitions.
- Unfair hiring practice.
- Retaliation.

What’s the Risk?

With the recent economic downturn, characterized by a sharp increase in workforce reduction, has created a potentially hostile environment where the possibility of an employee lawsuit is quite high, even for those that make every effort to comply with the law.

Statistics kept by the U.S. Equal Employment Opportunity Commission (EEOC – which is the federal agency responsible for enforcing federal workplace discrimination laws.) give a rough sense of the magnitude of the risk. For FY 2014, the EEOC logged more than 88,000 new complaints (EEOC Charge Statistics FY 1997 through FY 2013.) In FY 2015 the EEOC resolved 155 individual and class lawsuits, with a total monetary recovery of over $65,300,000, an average of over $421,000 in damages per case. (Source: EEOC, Fiscal Year 2015 Performance and Accountability Report)

Why Does My Business Need This – A valid question from your client.

Defending an employment practices claim, even if the claim is groundless or fraudulent, can be costly. If the employee’s claim is upheld, an un-insured liability for monetary damages could be a significant threat to a company’s continued existence. A business cannot rely on its general liability policy to provide protection, as nearly all standard general liability policies contain exclusions for claims resulting from employment-related practices.

Cost vs. Risk – What to help your client realize.

Pricing for EPLI policies can vary widely but is usually based on the number of employees. Because the premiums are relatively inexpensive however, the benefits of purchasing an EPLI policy typically far outweigh the cost. Small business may be especially vulnerable to employment related claims as they often lack formal procedures for hiring, managing and terminating employees or fail to implement such procedures.
In addition to the insurance protection, many policies also offer valuable loss prevention services such as online resources, access to HR consulting firms, law firms, toll-free hotlines and other specialized services, all of which can help avoid EPL lawsuits.

**Understand the Policy** – Always make sure that your client understands at least key issues of the policy. Some of the more important ones for an EPLI policy may include:

- **Exclusions:** Common exclusions include intentional violations, strikes, lockouts, invasion of privacy, network security and claims made after a business files or is placed in bankruptcy receivership, liquidation or conservation.
- **Who picks the attorney?** If a lawsuit is filed against the insured, who chooses the attorney to defend the lawsuit? Some insurance companies permit the insured to choose an attorney, while others reserve the right to select the attorney.
- **Third Party Coverage:** An additional consideration for your client would be whether or not coverage is needed for vendors, independent contractors, customers, clients and other third parties. Third party liability coverage is usually available for a relatively small additional cost. You as an agent should explain the possible need for this type of additional coverage.

**COMMERCIAL AND PROFESSIONAL LINES**

**The Commercial Policy**

Commercial property insurance protects businesses from pure loss exposures so that those businesses can pursue speculative ventures. It enables them to protect their assets and ensure their economic survival. It allows them to purchase real property under mortgage agreements. It serves as collateral in securing business loans and lines of credit. It results in lower and more stable prices for consumers. Unfortunately, some businesses are not adequately or properly insured. Following a major fire loss to an office building in one downtown area, it was determined that only about 4 of 75 tenants were insured.

A coverage plan that includes a wide range of essential liability and property coverages for a commercial enterprise is the Commercial Package Policy. The package policy usually features common policy conditions, common declarations, and two or more coverage sections. A commercial property coverage part can be included in a monoline policy or in a commercial package policy. In either case, the commercial property coverage part consists of commercial property declarations, one or more commercial property coverage forms, the commercial property conditions form, one or more causes-of-loss forms, and any applicable endorsements.
Policy Limits

As with most other forms of insurance, a client needs analysis should determine the extent of assets to protect, including any personal exposures. Policy endorsements and/or commercial umbrella protection may be considered as options. Special occurrences may have individual limits that must be evaluated for each client.

For example, a "products-completed" limit may be small for a bakery but should be expanded for a lawnmower repair service.

Eligibility

Rules of eligibility in the commercial arena are very complex. Suffice to say, clients should be aware of all limitations that might exclude coverage, including: building size or height restrictions, business class restrictions, etc.

Where liability is concerned, is the policy based on a "claims made" basis or a "claims occurred" basis? Clients should be well informed that coverage may exist only while they are in business and paying premiums. A claim made ten years after a client retires can be financially devastating.

Policy Endorsements

Due care should involve the listing of available options to extend coverage, reimburse for loss of use, loss of rents, loss of income, business expense coverage, builders risk protection, for buildings under construction, add or exclude specific accidents, products, work or locations, employment occurrences (termination, defamation, discipline, discrimination, etc.), liquor liability, products completed protection, pollution liability, malpractice, errors and omissions, personal and advertising violations, contractual liability, employee use of vehicles coverage, product defects or deficiencies, product recall protections, inflation upgrade protection, replacement cost coverage, personal effects protection, debris removal, etc.

Scheduled Losses

The exact property or premises covered should be disclosed, buildings, insured's business personal property and the personal property of others located at the business premises. In the case of liability policies, premises and operations exposure is the heart of coverage.

Options should also be disclosed concerning upgrades to broader forms of coverage perils like extended reporting periods or extending coverage beyond termination of the policy, earthquake damage, crop insurance, livestock, loading/unloading accidents, window glass breakage, falling objects, weight of snow, water damage, etc.
Policy Exclusions

As important as what is covered, clients should understand exactly what is excluded: building ordinances, government actions, power failure, water damage, bursting pipes, explosion of steam boilers, mechanical breakdown, money, animals, autos for sale, illegal property, underground pipes, fences, antennas, signs, etc.

Understanding the Basics of the Commercial Package Policy

Most commercial risks are insured under ISO’s Commercial Package Policy (CPP) or its Business Owners Policy (BOP). Eligibility under a BOP is fairly restrictive and limited essentially to small, non-hazardous retail, service and processing risks, or apartment buildings and offices—coverage under a BOP is usually quite broad, with relatively few options. On the other hand, almost any risk is eligible under the CPP except for properties eligible for coverage under ISO’s Homeowner’s Program. The commercial property conditions form contains conditions that apply to all commercial property coverage forms, unless a coverage form contains a condition to the contrary.

Like the common policy conditions form, the commercial property conditions form eliminates the need to repeat these conditions in each coverage form. The purchase of property insurance is a critical business decision for virtually all commercial and non-commercial enterprises.

The ISO Commercial Package Policy

The ISO commercial package policy is the “industry standard” for commercial package policies. Many insurers sell package policies that contain either AAIS or independently developed forms.

Many smaller insureds are covered by “businessowners” package policies--the ISO version or an independent policy. Regardless of the particular forms used, packaging has distinct advantages--to insurers, insureds, and producers alike. A producer may be an insurance agent, an insurance broker, or a sales employee of an insurance company. For the insurance company, one advantage of packaging is reduced administrative expense.

It costs the insurer less to underwrite and issue one package policy instead of two or more monoline policies for the same insured. Also, an insurer will increase its premium volume if it can write a package policy covering a number of an insured's exposures instead of writing a monoline policy. Package policies can also help insurers avoid adverse selection.

If an insured has one particularly hazardous exposure, the higher likelihood of a loss resulting from that exposure can be mitigated to some degree by the insurer's obtaining
a premium for other exposures of the insured that are less likely to result in loss. For the insured, an advantage of packaging is that there are fewer policies to buy and maintain. Packaging reduces the chance of delay in loss settlement due to disputes between different insurers.

For example, losses involving loading of automobiles sometimes fall in a "gray area" between auto liability and general liability. If one insurer provides both coverages, payment of a claim will not be delayed as it might be if each coverage were written by a separate insurer and each insurer felt the claim was covered under the other's policy. Finally, insureds, like insurers, benefit from reduced administrative expense in writing package policies.

Packaging is advantageous to producers for two reasons. First, the availability of packages facilitates account selling, or obtaining a customer's entire account instead of only a piece of it. Second, some packages are more easily sold and rated than separate monoline policies. This allows the producer to more quickly provide quotes for prospective customers, and it increases the producer's efficiency.

**Components of an ISO Commercial Package**

Under the rules and forms of Insurance Services Office (ISO), a commercial package policy (CPP) must include a common declarations page, common policy conditions, and two or more "coverage parts." The common policy declarations page shows the policy number; the names of the insurance company, the producer, and the named insured; the named insured's address and business description; and the effective date and expiration date of the policy.

There is a general statement, known as the "in consideration" clause, whereby the insurance company agrees with the named insured to provide the insurance as stated in the policy in return for the payment of premium and subject to all the terms of the policy. The premium for each coverage part included in the policy is shown along with the total policy premium. The insured may cancel the policy at any time by mailing or delivering written notice of cancellation to the insurance company. If two or more insureds are listed in the declarations, only the one listed first (called the first named insured) can give notice of cancellation.

The insurance company may cancel the policy by mailing or delivering written notice of cancellation to the insured listed first in the policy declarations. In order to provide a reasonable time for the insured to obtain other insurance, the insurance company is required to give advance notice of cancellation. Notice of cancellation must be mailed or delivered to the insured at least 10 days before the date of cancellation if the cancellation is for nonpayment of premium or at least 30 days before the date of
cancellation for any other reason. This provision may be superseded by state law, in which case an endorsement would be added to the policy, modifying the cancellation provisions to conform with the applicable law.

**Commercial Property Declaration**

The declarations page of the commercial property coverage part contains the following information pertaining specifically to property insurance: The description of the property insured, kinds and amounts of coverage provided and covered causes-of-loss (basic, broad, or special), a list of mortgagees, if any, the deductible amount, and a list of the property coverage forms and endorsements attached to the policy.

The declarations also indicate the applicable coinsurance percentage and any optional coverages. Provision is made for including a scheduled supplemental declaration on a separate sheet of paper. For example, if an insured such as a fast food franchise has too many locations to show on the declarations page, a supplemental schedule would be added to show all locations.

**Commercial Property Coverage Forms**

A commercial property coverage form contains an insuring agreement, describes the property covered and not covered, sets forth additional coverages and coverage extensions, and includes provisions and definitions that apply only to the coverage form. Commercial property coverage forms do not list the causes-of-loss for which the described property is covered. That function is performed by the causes-of-loss forms. Depending on the nature of the insured’s loss exposures, more than one commercial property coverage form may be included in a commercial property coverage part.

**Causes-of-loss Forms**

The causes-of-loss forms specify the perils covered by the commercial property coverage part. The three forms available — termed “basic,” “broad,” and “special” — allow the insured to select from a range of covered perils. A commercial property coverage part may contain more than one causes-of-loss form. One causes-of-loss form (such as the special form) may apply to buildings, and another causes-of-loss form (such as the broad form) may apply to personal property.

The commercial property declarations will indicate which form applies to each type of property at each location. The three most common causes-of-loss forms are the basic form, broad form, and special form. The basic form provides the narrowest coverage, and the special form provides the broadest coverage. There also is a causes-of-loss form for the single peril of earthquake.

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Causes-of-loss – Basic Form

The basic form covers losses resulting from the causes-of-loss of fire, lightning, explosion, windstorm or hail, smoke, aircraft or vehicles, riot or civil commotion, vandalism, sprinkler leakage, sinkhole collapse, and volcanic action. Fire and lightning are not defined or explained in the form, but the other causes-of-loss are explained or restricted.

- **Aircraft or Vehicles** – In order to be covered, damage caused by aircraft must result from actual physical contact with the aircraft or objects falling there from. Spacecraft and self-propelled missiles are considered to be aircraft, but the war exclusion would eliminate coverage for damage by missiles in time of war. Covered vehicle damage must result from physical contact with a vehicle or an object thrown by a vehicle. There is no coverage for damage by vehicles owned or operated by the insured.

- **Explosion** – The form contains no formal definition of explosion. However, the form clarifies that the term includes the explosion of gases in a furnace or flues, but it does not include rupture of pressure relief valves or rupture of a building resulting from the expansion or swelling of its contents caused by water.

- **Fire** – Although the form does not define fire, the courts generally have held that fire insurance covers only damage by hostile fire (fire that is not in a place where fire is supposed to be). Therefore, the policy would not cover damage caused by a fire in a stove, but it would cover damage caused by a fire that escaped from a stove.

- **Riot or Civil Commotion** – Riot and civil commotion are not defined in the policy. However, the policy does state they include the acts of striking workers while occupying the insured premises as well as looting occurring at the time and place of a riot or civil commotion.

- **Sinkholes** – Sinkholes result from underground water dissolving stone and creating an empty space or cavern under the ground. When the roof of the cavern gets too close to the ground surface, the surface collapses, causing damage to buildings or other property located over or near the resulting sinkhole. Damage to buildings or other property is covered, but the cost of filling the sinkhole is not.

- **Smoke** – Covered smoke damage must be sudden and accidental. There is no coverage for damage by smoke from agricultural smudging or industrial operations.

- **Sprinkler Leakage** – Sprinkler leakage means the escape of any substance from an automatic fire protection or extinguishing system. It could use carbon dioxide, halon, or any other extinguishing agent. The collapse of a tank constituting a part of such a system caused the sprinkler leakage or if it was caused by
freezing. Also covered is the cost to tear out and replace any part of the building or structure to repair damage to the automatic sprinkler system.

- Volcanic Action – Volcanic action damage is covered if it is caused by lava flow, ash, dust, particulate matter, airborne volcanic blast, or airborne shock waves resulting from a volcanic eruption. Since such losses may occur over a relatively long period of time, the form stipulates all eruptions that occur within any 168-hour period are considered a single occurrence. Cost to remove dust, ash, or particulate matter is not covered except for ash, dust, or particulate matter that caused loss to insured property.

- Vandalism – Vandalism means the willful or malicious damage to, or destruction of, property. There is no coverage for breakage of glass, other than glass building blocks constituting a part of a building, but damage to other property resulting from glass breakage is covered. Loss by theft is not covered, but damage to the building caused by the entry or exit of burglars is covered.

- Windstorm or Hail – Covered wind or hail damage does not include damage caused by frost, cold weather, ice (other than hail), snow, or sleet, even if driven by wind. Also, damage by rain, snow, sand, or dust to the interior of a building or property inside the building is not covered unless the building first sustains exterior damage by wind, and rain, snow, sand, or dust enters through such damaged part.

Causes-of-Loss – Broad Form

The causes-of-loss-broad form covers all of the perils covered under the basic form plus. The itemized list of the perils that it covers is breakage of glass, falling objects, and damage to personal property in the open. The glass coverage is limited to glass constituting a part of the building and specifically excludes neon tubing. Coverage is limited for any one occurrence. When glass breakage is caused by some other covered cause-of-loss, such as fire, the dollar limitations which do not apply are falling objects, weight of snow, ice or sleet, and water damage.

Weight of Snow, Ice or Sleet

The coverage for damage by the weight of snow, ice, or sleet does not cover damage to gutters, downspouts, or personal property in the open.

Water Damage

The water damage coverage protects against loss from leakage of water or steam resulting from the breaking or cracking of a part of an appliance or system containing water or steam. This does not include an automatic sprinkler system.
Causes-of-Loss – Earthquake

All three of the causes-of-loss forms exclude loss by earthquake and volcanic eruption, other than volcanic action as defined in the forms. Coverage for these causes-of-loss can be added by using the causes-of-loss—earthquake form. The earthquake form is an endorsement that can be used only in conjunction with one of the three causes-of-loss forms. Under the earthquake form, all earthquake shocks that occur within a 168-hour period (one week) are considered to be a single occurrence.

The deductible is stated as a percentage of the value of the insured property (2% to 10%), either actual cash value or replacement cost depending on how the policy is written. Commercial property insurance may be written as a single coverage (monoline) or as part of a commercial package policy. In either format, common declarations and common conditions are required. A commercial property coverage part consists of property declarations, commercial property conditions, a coverage form, and a causes-of-loss form.

Common declarations are used to identify the insured, a mailing address for the insured, dates of coverage, a general description of the business, and the premium for all coverages provided. Common conditions describe the general provisions relating to coverage. The causes-of-loss forms indicate the causes-of-loss, or perils, that are covered under the commercial property policy.

Causes-of-Loss – Special Loss

The causes-of-loss special form, instead of listing the perils covered, states that it covers “risks of direct physical loss,” subject to the exclusions and limitations expressed in the form. This type of coverage has long been known as “all-risks.” However, the possibility for court decisions making the term “all-risks” broader than intended resulted in a switch to the new term “risks of direct physical loss.” The shorthand phrase “all-risks,” still widely used by insurance people, will be used here to mean “risks of direct physical loss.”

“All-risks” coverage is more expensive than named causes-of-loss coverage, but it offers two distinct advantages to the insured. First, it avoids the necessity for guessing in advance which perils will cause loss. Second, it shifts the burden of proof of coverage. Under a named causes-of-loss form, the insured must show that the loss was caused by a covered cause. Under an “all-risks” form, an accidental loss is presumed to be covered unless the insurer can show that it was caused by an excluded peril.

Both the exclusions and limitations sections of the special form contain all of the exclusions of the broad form plus some additional exclusions required by the “all risks”
approach. The special form does not cover loss caused by delay, loss of market, or loss of use, smoke, vapor, or gas from agricultural smudging or industrial operations, or wear, tear, rust, corrosion, fungus, decay, deterioration, smog, pollution, settling, cracking, shrinking or expansion, insects, birds, rodents, or other animals. There is no coverage for loss or damage to personal property caused by dampness or dryness of atmosphere, changes in or extremes of temperature, or marring or scratching.

However, if loss by “specified causes-of-loss” or building glass breakage results, the resulting damage is covered. Specified causes-of-loss means the causes-of-loss insured under the causes-of-loss broad form, other than glass breakage. The special form excludes loss or damage resulting from continuous or repeated seepage or leakage of water over a period of 14 or more days. The form also excludes damage caused by water, other liquids, powder, or molten material that leaks from plumbing, heating, air conditioning, or other equipment, if the leakage is caused by freezing.

However, this exclusion does not apply if the insured has tried to maintain heat in the building or, if the heat is not maintained, the insured has drained the equipment and shut off the supply.

The special form does not cover dishonest acts of the insured, or partners, directors, or employees of the insured. It also does not cover voluntary surrendering of possession of property as the result of a fraudulent scheme. Damage to personal property in the open caused by rain, snow, sleet, or ice is excluded. Damage by collapse is excluded, but some coverage for collapse is provided by an extension of coverage elsewhere in the form. Also excluded is release, discharge, or dispersal of pollutants, unless the release is caused by any of the “specified causes-of-loss.” A final exclusion eliminates coverage for loss caused by:

- Weather conditions that contribute to other excluded causes-of-loss;
- Acts, failure to act, decisions or failure to decide of any group, organization, or governmental body;
- Faulty or inadequate planning, zoning, surveying, citing design, specifications, workmanship, repair, construction, renovation, remodeling, grading, compacting, materials, or maintenance.

The exclusions section is supplemented by additional exclusions and limitations in the limitations section of the form. Some of the exclusions and limitations in this section are intended to make some of the covered causes-of-loss under the special form consistent with the covered causes-of-loss named in the broad form. For example, there is an exclusion of loss to steam boilers and other steam equipment resulting from conditions or occurrences inside the boiler; however, coverage is provided for explosion of gases
in the firebox or flue. Also, damage to hot water boilers or water heaters is not covered if it results from conditions or events within the vessel other than an explosion.

Damage to the interior of a building by rain, snow, sleet, ice, sand, or dust is not covered unless the roof or walls of the building are first damaged by a covered cause-of-loss, or unless the damage results from the melting of ice, sleet, or snow on the building or structure. Damage to gutters and downspouts is not covered if the damage results from the weight of snow, ice, or sleet. Theft loss to construction materials is excluded and there is no coverage for loss of property that is simply missing without explanation, or for loss of property transferred outside the described premises on the basis of unauthorized instructions. Loss to the following kinds of property is covered only if it is caused by “specified causes-of-loss:”

- Animals, but only for death;
- Builders’ machinery owned or held by the insured unless held for sale;
- Fragile articles such as glassware, statuary, marble, chinaware and porcelain;
- Valuable papers and records.

Payment for breakage of building glass is limited to $100 for each plate or pane and $500 for all breakage in one occurrence. However, these limitations do not apply to breakage by any of the “specified causes-of-loss,” except vandalism. An example could be that the limitations do not apply to breakage of building glass caused by a fire or windstorm. Payment for loss by theft is limited for certain kinds of property:

- Fire, lightning, explosion, windstorm or hail, smoke, aircraft or vehicles, riot or civil commotion, vandalism, leakage from fire extinguishing equipment, sinkhole collapse, volcanic action, falling objects, weight of snow, ice or sleet, water damage, breakage of building glass;
- Hidden decay;
- Hidden insect or vermin damage;
- Use of defective material or methods in construction remodeling, or renovation if the collapse occurs during the construction, remodeling, or renovation;
- Weight of rain that collects on a roof;
- Weight of people or personal property.

Settling, cracking, shrinkage, bulging, and expansion are not considered to be collapse. This clause does not increase the amount of insurance. Rather, it adds another cause-of-loss. This section of the form extends the policy to cover two kinds of losses not otherwise included which is loss to property in transit and certain repair costs related to damage caused by water or other specified substances.

Commercial and professional insurance takes many forms: investment and commercial property coverage, business owners insurance, farm coverage, commercial auto plans,
commercial liability policies, for directors, officers and professionals, workers compensation and more. A full discussion of each goes beyond the scope of this course. However, there are some important due care factors for agents to disclose and discuss with clients.

**COMMERCIAL GENERAL LIABILITY INSURANCE**

General liability insurance protects the insured business from money damages as the result of a civil wrong committed by the business or by someone for whom the business is liable. It's not unusual for judges or juries to award money damages in the millions so general liability insurance is vital for most businesses. In addition, general liability insurance provides unlimited DEFENSE COSTS for the insured business. The insured money damages may arise out of bodily injury, property damage, personal injury (insurance terminology for such offenses as libel, slander, invasion of privacy, etc.) or advertising injury. Such injuries may result from the business’s premises, ongoing operations (away from the premises), completed operations or products.

General liability insurance provides coverage for many types of liability risks. The coverage applies to claims against the insured from customers, tenants, members of the public, and more. Liability coverage has become more important in recent years as the public becomes more likely to pursue claims and suits against others. People today tend to expect monetary remuneration to compensate for discomfort as well as for tragedy. Society looks to government, businesses, other individuals, service providers, etc. to compensate them for everything from coffee which is served too hot, to an unfriendly work environment, to serious accidents caused by negligence.

It is more socially, and personally, acceptable to file a liability claim or suit today than it was twenty or even ten years ago. The need for liability protection has existed for centuries. In today’s marketplace, the need is even greater.

**Overview of Coverages**

**Bailee Coverage**

Bailee Coverage is coverage on property entrusted to the insured for storage, repair, or servicing. It is typically purchased by businesses such as dry cleaners, jewelers, repairers, furriers, etc.

**Contractual Liability Coverage**

It is common in construction and other agreements (written or oral) for one party to "assume" the liability of another. This is sometimes referred to as a "hold harmless" agreement. The extent to which one holds another harmless varies from contract to
contract, job-to-job, etc. To assume the liability of another, regardless of extent, is a voluntary undertaking which increases exposure to loss. A standard Commercial General Liability policy does cover this additional exposure subject to certain exclusions.

Earthquake Coverage

The Earthquake Coverage endorsement extends the cause-of-loss to include damage that results directly from an earthquake. Coverage is provided for replacement of buildings only. All earthquake shocks that occur within a 168-hour period (one week) are considered to be a single occurrence. A separate deductible applies and it is determined by the value of the insured property.

Replacement Cost Coverage

This form of insurance provides coverage on the basis of full replacement cost without deduction for depreciation on any loss sustained, subject to the terms of the co-insurance clause. This coverage applies to both building and contents items as specified on the face of the policy. No deduction is taken for depreciation in arriving at the proper amount of insurance needed to comply with the co-insurance clause.

Time Element Coverage

Time element insurance provides insurance for a covered incident resulting in loss of use of property for a period of time. The loss is considered to be time lost, not actual property damage. Examples of time element coverage are Business Interruption, Extra Expense, Tuition Fees, Rents and Rental Value, Additional Living Expenses, and Leasehold Interest coverage.

Theft, Disappearance, and Destruction of Money and Securities Coverage

This provides insurance for loss of money and securities resulting directly from the following:

- Theft (any act of stealing)
- Disappearance
- Destruction

It applies while the money and securities are on the insured's premises, while in the custody of the insured or the insured's messenger while conducting business at the bank, and while off the insured's premises in the custody of the insured or the insured's messenger.
Umbrella Liability Coverage

This type of liability insurance provides excess liability protection. A business needs this coverage for the following three reasons:

- It provides excess coverage over the “underlying” liability insurance already carried.
- It provides coverage for all other liability exposures, excepting a few specifically excluded exposures. This is subject to a large deductible of $10,000.
- It provides automatic replacement coverage for underlying policies that have been reduced or exhausted by loss.

Umbrella Liability coverage provides excess liability coverage over several of the insured's primary liability policies. Most umbrella liability policies provide coverage that is broader than the insured's primary policies. An excess liability policy may be a following form policy, which means it is subject to the same terms as the underlying policies. It may be a "self-contained" policy, which means it is subject to its own terms only, or it may be a combination of these two types of excess policies. Umbrella policies have three functions:

- To provide additional limits above, each occurrence limit of the insured's primary policies.
- To take the place of primary insurance when primary aggregate limits are reduced or exhausted.
- To provide broader coverage for those claims that are not covered by the insured's primary insurance policies, which are subject to the policy retention.

Most umbrella liability policies contain one comprehensive insuring agreement. The agreement usually states it will pay the ultimate net loss, which is the total amount in excess of the primary limit for which the insured becomes legally obligated to pay for damages of bodily injury, property damage, personal injury, and advertising injury.

COMMERCIAL CRIME INSURANCE

The Basics of Commercial Crime

White-collar crime or commercial crime involves crimes such as fraud, bribery, corruption, etc. Although it does not receive as much publicity as other forms of crime, it costs a lot more as it robs an economy of much needed capital. Every time a company is defrauded of money, they have to recover this from somewhere such as price increases, fewer jobs, or even less research and development. Commercial crime is a lot easier to hide than other forms of crime, and therefore much harder to stop.
The fact is, crime is a significant cost of doing business. Embezzlement and employee theft are far more common in virtually all types of business than most people realize. Current estimates indicate these dishonest activities cost American firms around $100 billion a year. Having to make good on theft or misuse of company assets can cause financial hardship for any business. Unlike fire and auto losses, a loss due to employee dishonesty can accumulate over time and reach devastating proportions before being discovered.

Many employers leave themselves open to this risk because they have many misconceptions concerning employee dishonesty. While most incidents of employee dishonesty involve theft of cash, anything else of value may be stolen from office equipment to warehouse merchandise. The average embezzler is usually a trusted employee and considered a friend by their coworkers. Many employers do not want to consider the possibility of employee theft and believe fidelity bonds are unnecessary.

Commercial crime insurance includes several forms for covering money, securities, and property other than money and securities for various crime-related causes-of-loss. In contrast, commercial property coverage forms exclude money and securities, and commercial property causes-of-loss forms do not cover as many crime-related losses as commercial crime coverage forms. A crime is a violation of law punishable by some governmental body. Not all types of crime losses are insurable (theft by a partner of property belonging to the partnership), and some are covered under other insurance forms (vandalism or malicious mischief coverage in the commercial property forms).

The Commercial Crime Insurance Policy

Commercial crime insurance falls generally into the category of insurance referred to as fidelity coverage. “Insurance” spreads the risk of an unknown loss but is statistically certain to happen over a large number of individuals or companies, so the cost of protecting against such a loss becomes economically feasible (“the law of large numbers”). In true insurance, a policyholder exchanges a known “loss,” in the form of a fixed amount of money, or “premium,” for the insurance company’s promise it will pay for a future, potential loss. In “self-insurance,” the policyholder does not buy insurance but, by various mechanisms, pays the claim itself.

Though claims on commercial crime policies are often described as fidelity bond claims, modern commercial crime coverage is actually first-party insurance as opposed to a true bond, the latter of which involves a three-party relationship. The terms “fidelity insurance” and “fidelity bonds” often refer to coverage for losses caused by the dishonest acts of an insured’s employees; however, the terms can also refer to various protection offered for fraudulent acts of non-employees, certain acts of directors of an
insured company, failures of public officials to faithfully perform official duties, and other bonds designed to protect certain classes of people, such as probate bonds and motor vehicle dealer bonds.

WORKERS COMPENSATION AND EMPLOYER LIABILITY INSURANCE

The workers compensation insurance applies to bodily injury by accident or bodily injury by disease. Bodily injury includes resulting death.

- Bodily injury by accident must occur during the policy period.
- Bodily injury by disease must be caused or aggravated by the conditions of employment. The employee’s last day of last exposure to the conditions causing or aggravating such bodily injury by disease must occur during the policy period.

Workers Compensation Application

Workers Compensation applications are completed by the business that will provide the coverage for employees and generally include the following information:

- Name of the insured
- Address of the insured
- Type of business
- Years in business
- Total number of employees
- Number of full-time employees
- Number of part-time employees
- Number of employees under 18
- Number of employees over 65
- Number of employees who work from home
- Number of employees who drive employer-owned vehicles
- Whether the employer provide group transportation by employer-owned vehicles
- Whether the employer uses sub-contractors, and if so, the number of them
- Payroll information by class and payroll (typically based on regulating state statute)
- Excluded corporate executives (if state law allows the option for such people to be excluded from Workers Compensation coverage)
- Information related to workplace safety programs, such as:
  - Whether the business has a safety program
  - Whether safety meetings are held and if so, how often
  - Whether new employees participate in safety training
  - Whether injured employees are offered modified work
- Information related to the Workers Compensation claims process in place at the business Workers Compensation rates are based on job classifications and set by the state in which the Workers Compensation policy applies. Each job is assigned a classification code, and each code has a rate, with higher risk jobs
being assigned a higher rate. The premium is based on each $100 of payroll multiplied by the applicable rate. Underwriters then often use a retrospective rating process to adjust rates each policy year. Also affecting rates is the utilization of rehabilitation. If an employer has a rehabilitation program which retrains employees or provides physical exercise and therapy, rates may be reduced by the insurer.

Workers' Compensation Benefits Frequently Asked Questions

1. Q. If an injury occurs, what kind of benefits are paid?
   A. Workers' compensation law recognizes three types of disability — temporary total, permanent partial and permanent total — and establishes disability income benefit payments for each type.

2. Q. Who qualifies for Temporary Total Disability benefits?
   A. Temporary total disability (TTD) benefits are paid to the employee who is recovering from an injury or disease and is unable to return to work. Once the disabled worker has been unable to work for more than seven (7) days, he/she is entitled to TTD benefits for each day thereafter. If the disability exceeds two (2) weeks of lost time from work, the employee is then entitled to payment of benefits for the first seven (7) days.

3. Q. Who qualifies for Permanent Total Disability benefits?
   A. Permanent total disability benefits (PTD) are payable when "an employee...has a complete and permanent inability to perform any type of work as a result of an injury, and has an impairment rating."

4. Q. Who qualifies for Permanent Partial Disability benefits?
   A. Permanent partial disability benefits (PPD) are payable when "an employee...has a permanent disability rating but retains the ability to work". The term permanent refers to a physical disability expected to last into the future. Use of the word "permanent" does not describe the period of payment; payment for partial disability is limited, usually to 425 weeks.

5. Q. How are Permanent Partial Disability benefits calculated?
   A. Special consideration such as education and age factors can be added to the income benefits.

If an employee does not retain the "physical capacity" to return to the type of
work performed at the time of the injury, the weekly benefit is increased. If the employee returns to work at the same or greater wages, but at some point, ceases to work, payment of weekly benefits increases, depending on the law in effect on the date of injury.

**When Covered Injury Occur**

The client must advise that an injury has occurred that may be covered by the policy in place. Other duties to be performed by the client may include:

- Provide for immediate medical and other services required by the workers compensation law
- Give the agent the names and addresses of the injured person/s and as well as of witnesses and other information that may be required by the insurer.
- Promptly supply the insurer with all notices, demands and legal papers related to the injury, claim, proceeding or suit.
- Cooperate with the insurer and assist the insurer, as may be requested by the insurer, in the investigation, settlement or defense of any claim, proceeding or suit.
- Do nothing after an injury occurs that would interfere with the insurer's right to recover from others.
- Do not voluntarily make payments, assume obligations or incur expenses, except at your own cost.

**Exclusions**

- Liability assumed under a contract. This exclusion does not apply to a warranty that your work will be done in a workman-like manner
- Punitive or exemplary damages employed in violation of law
- Bodily injury to an employee while employed in violation of law with the client’s actual knowledge or actual knowledge of any of the executive officers
- Any obligation imposed by a workers’ compensation, occupational disease, unemployment compensation or disability benefits law or any similar law
- Bodily injury intentionally caused or aggravated by the client
- Bodily injury occurring outside the United States of America, its territories or possessions and Canada.
- Damages arising out of coercion, criticism, demotion, evaluation, re-assignment, discipline, defamation, harassment, humiliation, discrimination against or termination of any employee or any personnel practices, policies acts or omissions
- Bodily injury to any person in work subject to the Long Shore and Harbor Workers’ Compensation Act, the Non-Appropriate Fund Instrumentalities Act, the Outer Continental Shelf Lands Act, the Defense Base Act, the Federal Coal Mine Safety and Health Act and any other federal workers or workmen's compensation law or other federal occupational disease law, or any amendments to these laws
- Bodily injury to any person in work subject to the Federal Employers’ Liability Act, any other federal laws obligating an employer to pay damages to an employee
due to bodily injury arising out of or in the course of employment, or any amendments to those laws.

- Bodily injury to a master or member of the crew of any vessel
- Fines or penalties imposed for violation of federal or state law
- Damages payable under the Migrant and Seasonal Agricultural Worker Protection Act and under any other federal law awarding damages for violation of those laws or regulations issued thereunder, and any amendments to those laws.

The Need to Look Beyond Insurance

Risk is a fact of life to be constantly analyzed and managed. Unfortunately, the time most people devote to this process is less than the time they spend planning a summer vacation. So, who assumes the role of unofficial “risk manager”; preserving worldly goods, family security and business liability: Insurance agents?

Like it or not, you are in the asset protection business. But, just how far can you expect your product (insurance policies) to go. Every agent knows that insurance has its limitations. There are times when clients are underinsured; there are clients who cannot be fully insured; and there are times when insurance simply fails to insure. Add to this a bevy of carriers, who withdraw or are unwillingly forced from the marketplace, a few insolvencies here and there, and you know why a growing band of attorneys and financial advisers are starting to look beyond insurance; supplementing insurance coverage with multiple legal strategies.

The next time you are assessing a client’s “real” need for coverage, consider the following possibilities; all of which point to the need for “back-up” protection:

- The need for a protection structure which can be used as a replacement to insurance when premiums rise beyond a client’s ability to pay.
- The need for a protection system that can supplement current insurance, covering gaps in protection like punitive damages or an underinsured health condition.
- The need for a protection structure that will become a backup for times when, for whatever reason, a lapse in insurance coverage occurs.
- The need for a protection structure as back-up when an insurer fails to pay or becomes insolvent
- When coordinated with estate planning, the need for a structure to protect inheritances and estates from frivolous claims and plaintiff attacks.
- The need for a structure to protect business and property owners from new and exotic environmental liability which may be excluded by their insurance or entirely unknown by present standards.

Few would argue that when clients are provided safe, appropriate and sufficient levels of coverage, insurance is the world’ s most efficient asset protector (a first line of defense). Today, however, insurance by itself may not be the sole solution to protecting all assets because there are pressures at work, both legal and moral, that go beyond the resolution of good coverage.

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