

Taking Care of Business

Assessing Insurance Needs for Small Companies

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What defines “small” in small business depends on what industry the business is in, but the types of insurance coverage needed by a small business are essentially the same as those for a big business, only smaller in limits and premiums.

Nearly every business needs commercial property insurance to protect it from direct loss or damage to business property from perils such as fire, wind, water, theft, and vandalism. Indirect property loss resulting from the loss of use of the business property is included in this type of coverage. For example, loss of net income or loss of rental income is an indirect property loss, as are certain extraordinary expenses incurred because of a loss.

Depending on the nature of the goods or services provided, small businesses need four broad types of liability insurance to protect them from injury or damage to third parties and to defend against lawsuits.

- All businesses need general liability insurance for financial loss from bodily injury, property damage, medical expenses, and personal injury such as libel, slander, and unlawful detention or false arrest.

Takeaway

Except for the coverage limits and premiums, insurance needs for small businesses are much like those for big businesses. Insurance representatives are well-placed to assist the business owner in assessing the needs and reviewing how the selected policies work to protect the small business.

- Businesses that make or sell products need product liability insurance to protect against financial loss from a defective product or faulty workmanship.
- Businesses that make or sell products or provide services such as building a deck or installing cabinets need product liability or completed operations insurance to protect against financial loss from a defective product or faulty workmanship.
- Small businesses should have umbrella insurance, which adds higher limits to liability coverage purchased in the basic insurance policies and extends coverage over some activities or exposures not

specifically covered in the basic insurance policy but not excluded in the umbrella.

Other Types of Coverages

Businesses that operate motor vehicles as part of their business activities should have business automobile insurance. This coverage protects against the physical loss of the vehicle as well as liability to third parties for bodily injury or property damage. In addition, liability arising from the business use of vehicles not owned or leased by the business, such as the business owner's or employee's personal auto, can be covered.

While some types of crime coverage are provided in the basic property insurance, loss of money, checks, and securities are excluded or limited. Theft and crime coverage protects against loss of money and securities caused by theft, robbery, or burglary. For small businesses that have an employee benefits plan, the Employment Retirement Income Security Act of 1974 requires a fidelity bond, a special type of crime coverage protecting the assets of the benefit plans.

Workers' compensation insurance is needed for nearly all businesses with employees. Because this coverage applies to a state-regulated plan to pay medical bills and replace some lost wages for employees injured at work or those who have a work-related disease or illness, the requirements as to which business must have the coverage differs significantly. A listing of workers' compensation laws by state is available at forbes.com/advisor/legal/workers-comp/workers-compensation-laws/.

All states except Texas require businesses to purchase workers' compensation coverage or be approved by the state as a self-insurer (a process that generally is not applicable to most "small" businesses). Texas employers have the option of being a nonsubscriber, meaning the business is solely responsible for providing the state-regulated benefits of medical and wage replacement expenses without important legal protections, including immunity from most lawsuits by injured employees.

Businesses might want to purchase certain specialty coverages for property that is high-valued or restricted or limited in the basic policies. For example, "inland marine" or "floater" policies insure property that is highly mobile and seldom at the business location, such as tools, equipment that is moved from one job site to the next, property in transit, or property that is stored by a third party. Block policies are another type of specialty policy. They provide coverage for such businesses as jewelry stores or furriers where the merchandise is of high value and a likely target for thieves.

Block policies complement coverage provided in the basic property policy.

Businesses that rely on e-commerce should consider data compromise coverage or cyber liability to protect against disruption of commerce and security breaches that expose confidential customer information.

Disability, health, and life insurance are other types of insurance that any small business should consider providing to its owners and employees. However, when such benefits are provided, the small business should also consider purchasing employment practices liability (EPL) to protect against lawsuits resulting from the administration of these benefits, either as an endorsement to a general liability policy or a separate EPL policy. The EPL policy would also provide liability coverage for general employment-related lawsuits such as those involving discrimination, wrongful termination, various types of harassment, or a hostile work environment.

Creating an Effective Insurance Program

To create an effective insurance program for the small business, the business owner should follow these four steps.

Assess the risks. The first step should always be identifying the exposures, or the assets of and activities conducted by the business. The business owner must consider what kind of accidents, natural disasters, human actions, or lawsuits could arise from those assets or the activities of the business.

Once the exposures are identified, the focus should shift to the possible causes of the loss, such as fire, theft, wind, and the like, and the extent of the financial impact on the business.

Finally, the business owner should be aware of the hazards present wherever business activity is conducted. Examples of hazards include puddles of water on the floor, poor housekeeping, or equipment that is in a bad state of repair. The business should remedy these conditions as soon as they are noticed to minimize the likelihood of a loss or lessen the seriousness of the loss.

Find a reputable licensed insurance representative. The insurance representative is the access to insurance coverage. The choice of using an independent insurance agent or broker to procure coverage from an insurance company or using a direct employee or contractor (often called a direct writer) who works exclusively for an insurance company does not matter. The key is to find a representative who is competent and has a good reputation.

Representatives with professional designations such as Certified Insurance Counselor (CIC) or Chartered Property Casualty Underwriter (CPCU) have passed a series of rigorous tests and agreed to follow a strict code of ethics, and they are good choices.

Shop around. While good insurance is tailored to customers according to their needs, prices and benefits vary between insurance companies.

The business owner should consider comparison shopping, particularly if using a direct writer or exclusive agent of the insurance company. A professional independent agent who represents several insurance companies should do this shopping for the consumer as part of her insurance placement services. However, comparing both prices and benefits for the average business owner is challenging, as insurance is a technical subject.

Because it is generally counterproductive to shop around every year, it is prudent to make this type of intensive review every three years unless there is a sudden increase in prices or a dramatic decrease in coverage limits at renewal time.

Reassess the program annually. As businesses grow and change over the year, the needs will also change, and the program should be reevaluated to make sure it is still meeting the identified needs.

The annual reassessment should address property insurance to account for changes in property values because of inflation, acquisition, or divestiture.

Reassessment of liability limits is more challenging. The generally recommended procedure is to purchase sufficient limits to protect the business from being taken over as the result of a lawsuit. As businesses grow in their scope of activities or size of assets, the likelihood of a lawsuit also increases. The professional insurance representative should help with this as part of the annual insurance renewal process.

Insurance Coverage Options

For the truly small “small” business that is home-based, three of the basic required coverage types can be purchased by an endorsement to the business owner’s homeowner’s insurance policy. This endorsement adds a small amount to the limit for business personal property automatically provided by the homeowner’s policy as well as liability insurance, including products liability, for injury to third parties. The endorsement does not extend coverage to “other

structures,” such as a detached garage at the location that is used for business purposes, or increase the small limit on business property that is located away from the home.

However, loss of use of property, workers compensation coverage, business auto, inland marine or floater policies, and the other types of insurance coverage are not available by endorsement to the homeowner’s policy. If those are needed, an insurance representative should be able to place the coverage for the business as stand-alone policies.

When the scope of the business is beyond the simple home-based business, separate insurance coverages must be purchased. Most of the basic types of coverage—both direct and indirect property, general liability, crime, and some automobile coverage—can be written in a package policy called a Business Owners Policy (BOP). This option combines the typical coverage types into one policy, which simplifies the purchasing process and provides a discount in the premium. Except for selecting limits of coverage, the business owner has few options to customize the BOP to their specific business needs. The business owner still must consider a separate policy for the business auto, workers compensation, inland marine, umbrella liability, and other types of coverages.

For still larger “small” businesses, individual policies can be purchased. Some of these policies can be combined into a package policy, typically including property, general and product liability, and crime, with the other coverages provided on separate policies. These policies can be customized and tailored to the specific needs of the business.

Requirements When Providing Services for Government Agencies

Many small businesses provide services or products to government agencies of all types.

Often, a government agency will require minimum limits of liability or specific wording, such as an additional insured endorsement, a waiver of subrogation, or a nonstandard notice of cancellation clause.

When selecting the policies, the small business owner must consider whether or not the contemplated policies will meet the demands of those agencies. ➔

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