

RISKY BUSINESS

By Susanne Ross
Small and Medium Enterprise Consultant

Is your business adequately insured? As entrepreneurs we must manage many diverse aspects of our business, not the least of which is risk. But what does risk mean? Simply put, risk is the chance of loss - loss of business, of property, money or other valuable assets, even of health or life.

It isn't possible to eliminate risk altogether, unless you're willing to operate your business and your life from inside a bubble. Even then, the most well managed bubbles burst. So how can entrepreneurs calculate and manage risk? The Insurance Bureau of Canada identifies four stages in risk management¹. They are:

1. Identify your risks
2. Evaluate your risks
3. Minimize your risk
4. Shift the risk to others

Identify your business's exposure to risk. Every business is different and so are the uncertainties surrounding them. There are also many kinds of risk, some of which you can insure against, others you can not:

- Market-oriented risk which reflects market pressures, competitive threats and repercussions of poor management;
- Personal risk involving bodily injury, illness or death;
- Personnel-related risk, occurring due to the actions of employees or the loss of key personnel;
- Property risk arising from the destruction or damage to property, both directly and indirectly; and
- Liability risk, which is the obligation to pay damages because of injury to or death of another, or damage to another's property.

Market-Oriented Risk

Poor economic conditions, bad planning and ineffective decision making can result in debilitating revenue losses and ultimate bankruptcy. Market-oriented risk is difficult to insure against and is generally avoided through improved management practices and legal or contractual safeguards.

Personal Risk

Because so many SME's depend on the activities of the owner and a few key employees, it is important to protect the business against income losses due to the inability of those principals to perform their duties. Disability insurance will provide short- or long-term compensation in case of accident or illness. Key personnel insurance offsets losses due to the death or departure from the firm of an integral employee.

Business owners must also consider reductions in personal income that might arise due to early retirement or just plain old age, as well as medical and dental expenses that are not

covered under social programs. Firms may also wish to offer an employee group benefits plan as incentive to retain a stable and dedicated work force.

Personnel-Related Risk and Liability

An employer may be legally responsible for the actions of employees who are acting on behalf of the firm. Liability generally arises from negligence of some kind, causing damage or loss to another or another's property. Negligence can relate to a person's conduct (either doing something that a reasonable person would not do, or not doing something that a reasonable person would do), the operation of vehicles or equipment, the ownership of property, the manufacture of products or the rendering of professional services.

General liability insurance is often provided in a package, sometimes called a business office package policy, with other items such as property insurance. Professional liability insurance, "Errors and Omissions" (E&O) insurance, is generally sold as a separate item. It is a kind of "malpractice" policy, protecting consultants and designers that give advice, make educated recommendations, provide solutions, etc. Some of the risks associated with these activities can be mitigated through carefully worded contractual clauses.

You may also suffer losses due to employee theft or dishonesty or from competition from previous employees who have left your organization. Generally these issues are best handled through legal employment contracts rather than insurance. Be sure to conduct thorough background and reference checks before hiring.

Property Risk

Businesses can suffer losses directly, when an insured asset is destroyed or damaged and must be repaired or replaced, or indirectly as a consequence of direct loss. For example, consider the loss of income to your firm if your delivery vehicle is stolen or a key piece of equipment is damaged and you cannot carry on business without it. Fire, flood and sewer backups, vandalism and burglary, accidents and shoplifting can have a critical effect on your business.

Consider business interruption insurance that will offset lost income if your company cannot carry on due to damage covered under your property insurance policy. It takes into account lost profits you would have earned, and ongoing operating expenses like electricity, that continue even though business activities have come to a temporary halt.

In order to assess property risk, take careful stock of your assets- facilities and equipment, vehicles, inventory, signage, leasehold improvements, etc. Consider property that is both on- and off-premises or in transit, owned, leased or rented.

If your business is home based, identify what property is shared between household and business use and make sure that you are adequately insured. Homeowners' policies often limit or exclude assets engaged in commercial use, as do vehicle policies. Be sure of the extent of your coverage and advise your insurance provider of your business activities. A

simple rider or combined plan may be all you need to better serve both your home and business needs.

Evaluate the risks: Risk has been defined as “calculated uncertainty”. Once you have identified your potential exposure to risk, your insurance representative will work with you to evaluate the likelihood and extent of losses.

Minimize the risk: There are many things a company can do to minimize risk. Undertake preventative measures such as installing and maintaining safety equipment and processes (fire alarms, smoke detectors, sprinkler systems), providing training for use of dangerous equipment and materials, employing anti-theft devices, storing hazardous materials in a safe place and backing up and protecting computer files.

Assume or shift the risk: You can assume some of the risk yourself, either by paying for losses when and if they occur or self-insuring by setting aside contingency funds to cover future potential losses. This is particularly prudent if you have assets that depreciate or become obsolete quickly, such as computer or other electronic equipment. Funds that may have been tied up in insurance premiums, when invested in interest-bearing accounts should, over time, more than offset the potential insurance payout.

The risk that you do not want to assume or self-insure, is what you transfer to an outside insurer. Once you have determined your business's exposure to risk and have taken steps to reduce them, speak to an insurance agent or broker who is familiar with your industry about the best insurance program for your business. Acquaintances in similar fields or industry trade associations may be able to refer you to the best practitioner for your business.

The cost of insurance premiums will be determined by the extent of risk to which the insurer believes your business to be exposed. Also, the higher the deductible you are willing to assume, the less you will pay for the policy. Be sure to shop around for the best value, but remember that the true merit of insurance is never realized until you need it.

1 <http://www.ibc.ca> Insurance Bureau of Canada, “Business and Commercial Insurance”