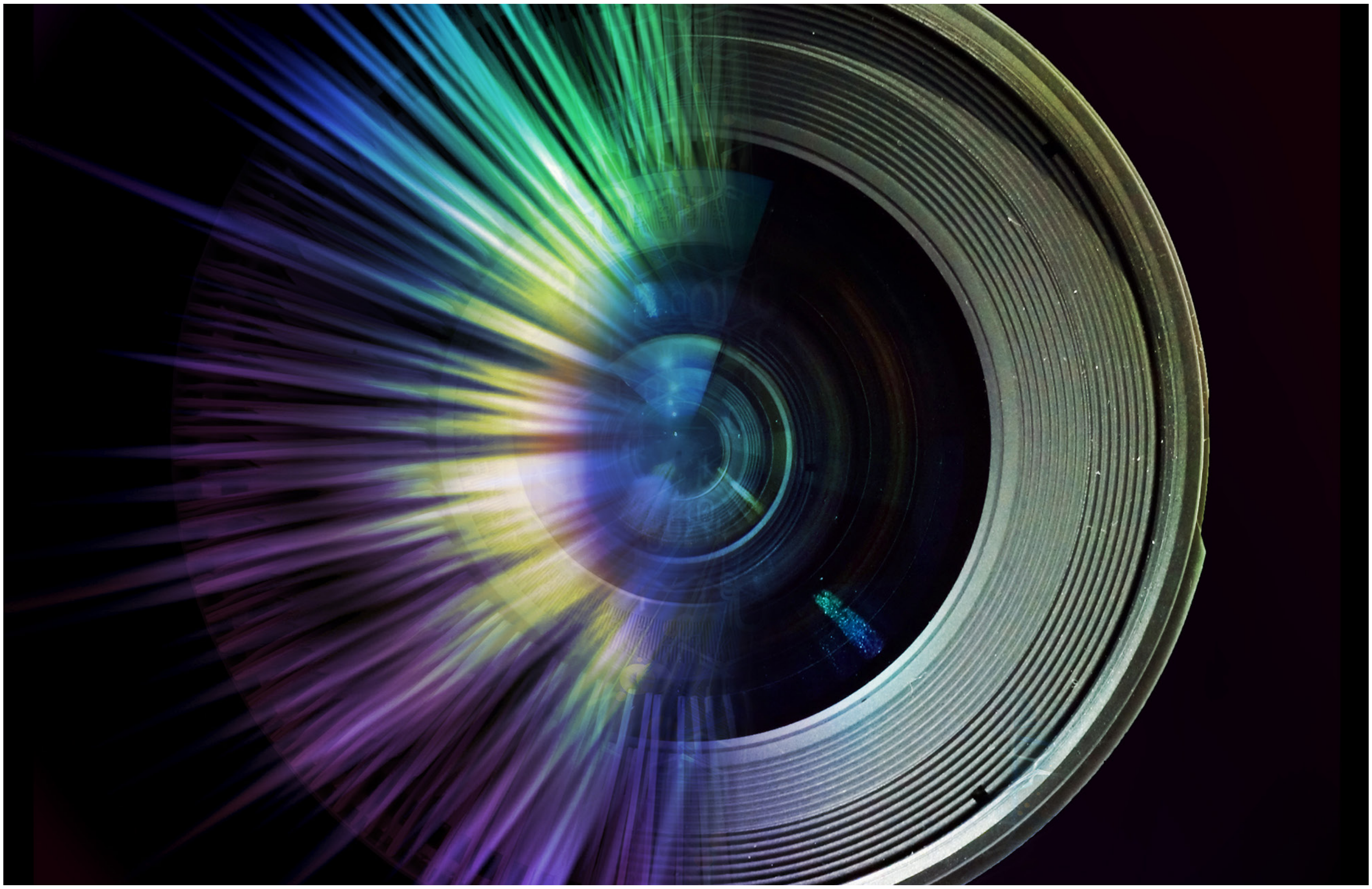

Forensic Focus on COVID-19

A series from Deloitte Risk & Financial Advisory

Valuing business insurance claims.

To address the financial impact of COVID-19, organizations are taking initial steps to recover losses, including standing up loss accounting centers; implementing tools to aggregate, analyze, and monitor business impact; and developing relief recovery strategies. At this point, those pursuing or expecting insurance reimbursements and other potential sources of funding, such as the Coronavirus Aid, Relief and Economic Security (CARES) Act or government agency programs, should be preparing well-supported impact assessments as well as claims and relief recovery substantiation. In addition to tracking revenue declines, refunds, and expenses, this may include maintaining daily timelines of events including but not limited to government orders, customer cancellations, refunds, personnel, and production changes and the like. Organizations should be collecting and preserving supporting documentation including but not limited to internal labor charges associated with response, invoices, receipts, refunds and notices of cancellation, as well as budgets and forecasts that demonstrated how the organization expected to perform before the pandemic.

Due to the unprecedented nature of this pandemic and its widespread economic impact, valuing business impact—including those that appear to be expressly covered by commercial or captive insurance policies or government programs—presents challenges. Business impact may not be precisely defined, may be open to interpretation, and options for loss mitigation—which is an expectation of stakeholders and oftentimes insurance contracts —may be nebulous or nonexistent. There is also the open-ended nature of this crisis.

Determining the period to recovery or of restoration will be complex in a global economy where business and consumer demand may be slow to return which will require careful analysis in separating COVID-related versus overall GDP impacts. The task of isolating business impact clearly recoverable through insurance from those not as clearly recoverable will likely complicate the claims process. Isolating various impacts may benefit from artificial intelligence (AI) analysis and other technologies. For example, in some cases, geospatial analytics incorporating a geographic information system (GIS) can assist in identifying changes in customer buying activities; premises exposures; and other location-related impacts on supply chains, operations, workforces, and financial performance. In others, "blanket" analytics capabilities can connect disparate data sources, enterprise resource programs (ERPs) and specialized claims technologies that collect and preserve data to reduce the manual nature and increase the accuracy of the analyses.

Achieving efficient, effective recovery calls for fact-based, data-driven analyses of business impact that may be claimed under relevant insurance policies and other potential funding sources. At this still-early stage, it's essential for an organization to assume nothing about coverage or applicability of other relief mechanisms. Instead, they should be focused on critically analyzing impact with the right experience, including legal counsel experienced in interpreting insurance contracts and government relief mechanisms as well as those with understanding of valuing organizational impacts across operations, the supply chain, and other functional areas. It is just as important to document everything, which can support not only a thorough analysis but also a substantiation of the impacts which can then lead to informed decisions as to where to pursue relief, if applicable, and a potentially less cumbersome path to recovery.

Far from the usual claims—In a typical disaster such as a fire, flood, or earthquake, an organization may see a couple of revenue-generating facilities affected. Outside the affected facilities, business as usual may continue. By the same token, mitigation opportunities are typically apparent and property and other losses are usually readily quantifiable, allowing for relatively straightforward claims preparation. Not so in the current environment.

To assess COVID-19-related business impacts in a systematic manner, it may be useful to explore valuation in terms of two broad parameters – lost revenue and margin, and the loss period.

To substantiate revenue and margin losses, look to similar prior-year results, business plans and projections, and data analytics and modeling which help determine what were anticipated versus actual earnings. Lost margin may arise not only from direct losses due to reduced or absent customer activity and supply chain disruptions, but also to incremental and extraordinary expenses.

For example, supply chain disruption may generate higher raw materials costs as well as increased transportation costs, such as air versus ship, increased customs or inspection fees, and other charges. Other costs may include personal protective equipment and supplies, employee housing, or electronic equipment used to protect employees to keep operations continuing. Such costs, which can translate to lost margin, need to be analyzed to determine what may be recovered through government agency programs or insurance or other means. Organizations should also be able to relate higher materials costs to the potential sales lost.

Loss periods associated with the pandemic present potentially thorny issues. As of now, no one can know how long disruption to business as usual will continue. This suggests the need for the organization to establish an ongoing loss documentation, evaluation, and monitoring process against performance that was anticipated pre-COVID-19. Bear in mind, however, that just as losses may continue to mount, new methods of mitigating them—such as innovations in supply chains and business models—may also quickly emerge.

The evolving nature of business disruptions wrought by the pandemic may affect the viability of claims over time. Further, funding sources from government agencies worldwide are also evolving and should be closely monitored. Eligibility for disbursements will vary by jurisdiction and types of losses incurred. Insurance companies and government authorities are not intending duplication of benefits and may carry compliance requirements associated with drawing on funds so applicants will need to consider which relief resource is most appropriate for each type of loss for which they are seeking recovery with is continuing to evolve .

Industry impacts may vary—Ilssues within specific industries may affect the scope of business impacts and valuation calculations for individual organizations.

Consumer products and manufacturing: Lost profits from lost revenue and lost margin from the pandemic's effects on the supply chain may or may not be recoverable and thus should be separately calculated, as should the impact of any product recalls. Government stay-at-home, state-of-emergency, and other declarations could shut down production facilities and impact key customers and suppliers in certain regions. Extended shutdowns could lead to raw material spoilage, product expiration, inventory obsolescence, and other property damage related to loss of use or inability to produce and sell.

Health care: Loss assessments for providers should consider tradeoffs between fewer elective procedures versus increases in patient census due to COVID-19. Entities able to provide only elective procedures may have increased business impact. Even providers seeing increased revenue may see it partially offset by decontamination expenses, personal protective equipment and medical supply purchases, overtime pay, and other extra costs. In addition, the mandate to treat all affected individuals, including the uninsured, may increase costs (without associated revenue). Government funding can help offset or compensate for some losses, as well as the costs of efforts to prepare for future disruptions.

Hospitality: Airlines, cruise ships, and hotels are seeing reduced occupancy now and will likely continue do so well after most features of everyday life resume. Postponed conventions and other events may or may not initially trigger event-cancellation coverage; however, if the event was entirely canceled at a later date, that coverage may then go into effect. Again, changing conditions over the course of this crisis may lead to varying coverage options. Also, in contrast to more local disasters, the pandemic may preclude hotels from diverting guests to other nearby properties due to government restrictions, which may reduce the ability to mitigate losses. The hospitality sector is one where separating COVID-19 and broader GDP impacts in terms of determining the period of recovery will require careful analysis.

Oil and gas: Numerous factors have recently affected the oil and gas industry, severe demand contractions, OPEC + production decisions, and commodity price declines. Such conditions will require careful analysis to separate the impact of the pandemic from the impact of industry dynamics. Reduced driving, aviation and shipping; idle facilities; shifting fuel mix; purchase deferrals and cancellations; delayed maintenance; and postponed production and storage capacity buildouts—have all aggravated the situation and require careful analysis continued evaluation. For example, certain state regulatory agencies are exploring enacting rules to limit oil and gas production. Additionally, it is possible that oil & gas is considered in future government relief bills which could expand recovery resources available.

Accordingly, it is important to continuously monitor macroeconomic, regulatory and company-specific facts. For organizations in these and all other industries, having the appropriate specialized knowledge, experience and analytical horsepower can assist in establishing policies and procedures, gathering internal and external data, monitoring finances and operations, identifying causes and effects, tracking and forecasting business impacts, and—ultimately—preparing valuations that are accurate, organized, and well-supported. Such valuations can help make the entire process more cordial, efficient, and beneficial for both the source of recovery and the recipient.

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