

CHAPTER 15

MANAGING INSURANCE

15.1 INTRODUCTION TO INSURANCE

15.2 TYPES OF COVERAGE

Property-Casualty

Liability

Employee Liability

Dram Shop

Health/Dental/Vision

Workers' Compensation

15.3 SELECTING AN INSURANCE CARRIER

15.4 SELECTING THE INSURANCE POLICY

15.5 POLICY ANALYSIS

“THAT WAS TRULY a great meal!” said Trisha Sangus as she left the lobby area of Chez Louise, one of her favorite restaurants in the city. Trisha was in a festive mood, as she walked back to the restaurant’s parking lot with Bob Zaccarelli, editor of *The Community News*, her city’s largest newspaper. Trisha and Bob had just enjoyed dinner while they worked together on planning the print advertising for the city’s annual Taste of the Town festival. As they approached Bob’s car, he shouted, “What the . . . !!!!!”

Trisha looked at Bob’s brand-new sports car. The driver’s side window had been smashed. Shattered glass was everywhere, and Trisha noticed on the ground beneath the car window that it included the

distinctive brown glass of a beer bottle with its wrapper still partially attached.

“Did they take anything?” asked Trisha, as Bob examined the inside of the car.

“No, I don’t think so. My CD player’s still here,” replied Bob still angry. “I can’t believe this. We were only inside for an hour! I thought this restaurant was in a safe neighborhood. It will take me a week to order a new window and get this fixed! I’ll have to rent a car in the meantime.”

Trisha looked up at one of the halogen lamps in the well-lighted parking lot. Nearby, other cars passed on a busy commercial street.

“I’m really sorry, Bob,” she said. “It looks like the work of some kids with nothing better to do. If they

had been car thieves, you would have lost the whole car! By the looks of things, I would guess someone drove by and threw the bottle from the street. I'm sure the police will be able to determine what happened better than we can. I have my cell phone. Would you like me to call them?"

"Don't bother," replied Bob. "The police are not going to be able to fix my window. Besides, as you say, it looks like vandalism. It's unfortunate, but I guess it goes with doing business in the city. Anyway, I'm sure the restaurant has insurance for this type of thing."

"The restaurant?" asked Trisha quizzically. "Won't you file a claim with your own auto insurer?"

"No way," said Bob. "This happened in a restaurant parking lot. The owners' insurance should pay. My car is supposed to be safe here. It wasn't, and that's their

responsibility. Just as if the car had been vandalized in your hotel parking lot, it would be your responsibility. It's as clear-cut a case of liability as I have ever seen. I'm going back in to see the manager!"

"Clear-cut," repeated Trisha to herself. She wondered what type of reception Bob would get from the manager at Chez Louise. She had never seen Bob so upset. She wondered how the hotel managers on her own staff would react if Bob approached them with a similar complaint. She knew what she would say, but what about her manager on duty? Just as important, if they said the wrong things, she wondered what impact that might have on the hotel's liability insurance coverage. Trisha made a mental note to add this issue to the top of her agenda for tomorrow's staff meeting.

IN THIS CHAPTER, YOU WILL LEARN:

1. To understand the value of insurance in protecting a business from financial loss.
2. To become familiar with the different types of insurance required of hospitality operations.
3. To understand the role of workers' compensation and the requirements of an employer.
4. To critically evaluate the financial rating of an insurance company and other information to help you select an insurance carrier.
5. To distinguish between the terms "primary" and "umbrella" insurance coverage, and determine appropriate amounts of coverage.
6. To analyze an insurance policy and determine what types of claims will be covered and what types of claims will not be covered.

15.1 INTRODUCTION TO INSURANCE

LEGALESE

Insure (insurance): To protect from risk.

Every individual faces risk. Illness, accidents, the acts of others, and even death, are all potential hazards each of us faces in life. Your business will face possible calamities, also. Floods, fire, and the acts of guests, employees, and others can all put your business at risk. To guard against the financial loss these risks can bring, both individuals and businesses need to *insure* themselves. In its simplest form, insurance involves the spreading of risk from one person or business to a larger group.

Hospitality businesses seek *insurance*, or protection from risk, for two basic reasons. First, because doing so makes good financial sense. Second, some types of insurance coverage are required either by law (such as workers' compensation) or by lenders to protect their collateral. Consider, for example, the restaurateur who owns a business that provides her with a salary of \$100,000 per year. The restaurant is her sole source of income. If the restaurant were to burn down, she would lose this source of income. To protect her business, and her income, she would want to buy a fire insurance policy that would pay to completely replace the restaurant in the event of a fire, provided that the cost of the insurance was reasonable. Not buying the insurance would put this restaurateur and her family at great financial risk. Buying the insurance would provide the restaurateur with both financial security, in the event of an accidental fire, and the peace of mind that such security brings.

To be protected from risk does not mean that hazardous events will not occur. Insurance does mean, however, that the person with insurance is provided some protection against the financial loss he or she may incur as a result of a hazardous event. The insurance industry is built on four fundamental premises:

1. The type of hazard the insurance company is underwriting must be faced by a large enough number of individuals or businesses so that statisticians can use actuarial (*actuary*) methods to predict the average frequency of loss involved in the risk.
2. The monetary value of the loss must be calculable against an accepted standard. For example, if a hotel seeks coverage for broken windows caused by vandals, it must be possible for the *insurer* to fairly determine the cost of replacing such a window.
3. The *premiums* (fees) for the insurance must be low enough to attract those who seek to be *insured* but high enough to support the number of losses that will be incurred by the insurer.
4. The risk must not have the possibility of occurring so frequently during any given time period that the insurer cannot pay all legitimate claims. Insurance companies spend millions of dollars annually researching industries to determine the risk factor of providing insurance for a specific market, such as hospitality. Obviously, the fewer number of casualty losses, workers injured, lawsuits, and so on, the lower the risk that the insurance company may have to pay out money on a claim. Logically, then, the safer the operation, and the safer the industry as a whole, the lower the cost of insurance.

The insurance contract between an insurer and an insured is called a *policy*. There are a variety of policy types, but they can be conveniently grouped into three categories:

1. Life insurance
2. Health insurance
3. Property-casualty (often referred to as “property-liability”)

Life insurance policies generally are written to pay a certain amount of money at the time of the insured’s death, or to pay the insured an *annuity* upon the insured’s reaching a specified age. Health insurance is generally created to pay for hospital and doctor bills, as well as annuity payments for those who are disabled. In the hospitality industry, it would be common for you, as a manager, to receive some level of both life and health insurance as part of your compensation package.

Property-liability insurance provides financial protection (*indemnification*) in the event of occurrences such as floods, fires, lawsuits, and automobile accidents. As a manager, it is important to know the types of insurance policies that make sense for your operation, and how to evaluate the quality of the companies that offer insurance, as well as the merits of the actual policies.

It is also important to remember that insurance companies, like hospitality companies, are in business to make a profit. Profits in the insurance industry are the result of increasing premium amounts, increased return from the investment of premiums, and the reduction of costs, including the payment of insurance *claims*. Because this is true, insurers are very careful to pay only those claims that are proven to be legitimate and within the terms of the insurance policy.

Because insurance protects against risk at an agreed-upon price, it is critical that you as a hospitality manager know:

- The risks you are insuring against
- The amount of coverage you will receive
- Any exceptions to your coverage that are written into your policy

LEGALESE

Actuary: A mathematician or statistician who computes insurance risks and establishes premium rates.

LEGALESE

Insurer: The entity that provides insurance.

LEGALESE

Premium: The amount paid for insurance coverage; it can be paid in one lump sum or over time, such as monthly.

LEGALESE

Insured: The individual or business that purchases insurance against a risk.

LEGALESE

Policy (insurance): The contract for insurance agreed upon by the insurer and insured.

LEGALESE

Annuity: Fixed payments, made on a regular basis, for an agreed-upon period of time or until the death of the recipient.

LEGALESE

Indemnification: To insure against possible liability and loss, and/or to compensate financially for losses incurred.

LEGALESE

Claim: Demand for money, property, or repairs to property.

- How much the insurance will cost
- The likelihood that the insurance company is financially sound enough to pay, if it becomes necessary

To purchase insurance, a potential buyer must demonstrate that he or she has an insurable interest in the premises to be insured. That is, he or she must demonstrate that a loss would, in fact, affect him or her in a material way. This insurance concept is fundamental and helps protect against possible intentional acts of destruction or fraud. In addition, an insured must honestly divulge information needed by the insurer to enable the insurer to establish appropriate premium rates.

» ANALYZE THE SITUATION 15.1

SAMUEL RENKO, PRESIDENT OF Senframe Hotel Management Company, authorized the purchase of a \$2 million fidelity insurance policy, the purpose of which was to protect the company in the event of employee theft or fraud. In discussing the purchase with the insurance agent, Jana Foster, Mr. Renko assured Ms. Foster that all hotel controllers were subject to a thorough background check before they were hired. As a specific condition of the insurance policy, background checks on controller candidates were required prior to employment.

The insurance policy was purchased and went into effect on January 1, 2011. On June 1, 2011, the Senframe Hotel Management Company took over the management and operation of the Roosevelt Hotel, a 300-room property in a resort area. As part of the operating agreement with the Roosevelt Hotel's owners, the hotel's controller and its director of sales were retained by Senframe. On December 20, 2011, Senframe management discovered that the Roosevelt Hotel's controller had been creating and submitting false invoices. The invoice payments were deposited in a bank account he had established for himself five years earlier. Total losses for the five-year period that the falsification occurred were over \$500,000.

The controller resigned, but the hotel owners sued Senframe for the portion of misappropriated fund (\$70,000) taken during the period the hotel was under Senframe's management. Ms. Foster maintained that her insurance company was not liable to indemnify Senframe, because the controller had not been subjected to a background check, as Mr. Renko had promised. Mr. Renko countered that the controller, although not background-checked, had no criminal record of any kind, and thus a background check would not have prevented the hotel from hiring the controller.

1. Must Ms. Foster's company defend Senframe in the litigation brought by the hotel's ownership?
2. If you were on a jury, would you hold Senframe responsible for the employee theft?
3. Regardless of the outcome of this situation, what changes in operational procedure should be implemented by Mr. Renko and the Senframe Hotel Management Company?

As with any purchase, careful comparison shopping before selecting insurance is a very good idea. Because insurance is a contract between the insurer and the insured, it is also a good idea to read the contract carefully, or to have an expert evaluate it for you. As with any type of contract, it is critical that the insurance policies be kept in a safe, secure location.

Purchasing insurance is often complex and can be confusing. You may find it easier if you think of buying insurance as a three-step process:

1. Determine the type of insurance coverage you need. Here, you are looking at various aspects of your operation and deciding which risks to protect against.
2. Determine the ideal monetary amount of insurance coverage, and the type of policy you will require. Remember, as the dollar value of your coverage increases, so will the premiums you have to pay.
3. Select a specific insurance company from which you will buy your policy.

The next three sections of this chapter examine each of these steps in detail, and offer some guidelines for helping you determine the appropriate type of insurance coverage.

15.2 TYPES OF COVERAGE

Because the hospitality industry is made up of a variety of operations in different locations, the insurance needs of restaurants and hotels will vary considerably. A hospitality establishment's insurance policies will reflect the unique characteristics of the type of business being operated and the location in which it does business. For example, a restaurant on the United States Gulf Coast may well feel that hurricane insurance makes sense, while the same type of operation in South Dakota would not. Similarly, the resort that offers overnight camping excursions for families may desire insurance against animal attacks, while the yogurt store in a shopping mall would be hard-pressed to justify purchasing such a policy.

Insurance companies offer a wide variety of products designed to meet the needs of their customers. Because this is true, hospitality managers must be very careful to make sure that they select the proper insurance coverage for their specific situation. With too much coverage, or with coverage that is not necessary, operational profits are reduced because premium payments are unnecessarily high. With no insurance, or too little insurance of the right type, however, the economic survival of the hospitality operation and its members may be at risk.

Many states have laws requiring businesses to carry certain types of insurance, at specified minimum amounts, in order to conduct business within the state. In addition, when hospitality firms lease space in buildings, the lease agreement may also require them to carry minimum amounts of insurance.

Although the specific types and amounts of insurance needed for any given hospitality operation will vary, the following types of insurance coverage are common.

Property-Casualty

Just as its name indicates, property-casualty insurance is purchased to protect against the loss of property. These losses include damages incurred due to a fire, flood, or storm. Some insurance companies will classify threats to property in different ways, but in all cases, property-casualty insurance protects property and its contents. The determination of which risks to insure against must be made on the basis of each hospitality operation's special circumstances.

Consider the case of Ralph Escobar. Ralph operates a seafood restaurant that is housed on a ship that is permanently docked on one of the Great Lakes. Ralph, unlike many other restaurateurs, must insure his operation against a variety of water-related

events that could destroy his business. These include accidentally being hit by another boat, high- or low-water damage, and seasonal storms that could damage his floating restaurant. Ralph must select casualty insurance that will cover these incidents and reimburse him for the cost of repairs and any potential loss of business.

Property-casualty insurance, in its many forms, is the most common type of business insurance purchased. It may be purchased in policies covering losses as small as a few hundred dollars or as large as many millions of dollars.

Liability

General liability insurance is selected when you wish to protect against injuries to other people resulting from the operation of your own hospitality facility. For example, Diane Sulayman operates a French fine-dining establishment that serves a variety of items, including flamed desserts. One evening, her server accidentally sloshes flaming alcohol out of a flambé pan and it splashes onto the suit of a diner. The diner is not injured seriously, but suffers some minor burns and is quite upset. Should the diner elect to bring a lawsuit against Diane, her general liability insurance would help cover the expenses and potential damages that might be awarded in such a lawsuit.

There are a variety of liability insurance types on the market today. The following are some of the most popular:

- Property damage liability coverage is selected when you wish to protect against claims resulting from damage to the property of others.
- Personal injury liability coverage provides you with protection for such offenses as false arrest, libel, slander, invasion of privacy, and food poisoning.
- Advertising injury liability coverage helps cover your legal liability for offenses arising out of the advertising of your business's goods and services.

Insurance companies have the right and obligation to defend any lawsuit against their insured customers that seeks damages for bodily injury or property damage, even if the allegations in the suit are groundless, false, or fraudulent. The insurance company can also enter into any settlement agreement it deems expedient. It is important to remember, however, that the company is not obligated to pay any claim or judgment or to defend any suit after the applicable limit of the company's liability has been reached, or that falls outside the coverage of the policy.

Consider the case of Roger Kuhlman. Roger owns and operates a hotel in which a guest accidentally discharges a pistol in one of the guestrooms. The shot passes through the wall of the room and injures a guest in the next room. The injured guest sues both Roger and the guest responsible for the accidental shooting. Roger's insurance company defends his hotel in the lawsuit. In the resulting jury trial, Roger's hotel is deemed to be partially responsible for the accident, and is ordered to pay the victim \$3 million. The hotel's insurance policy provides only \$1 million of coverage. In this case, Roger's hotel is responsible for paying the remaining \$2 million.

With the increasing monetary value of awards resulting from litigation today, wise hospitality managers are attempting to confirm they have sufficient liability coverage. This is not an easy task. You must weigh the cost of coverage (the premium payments) versus the risk (possible damages), and assess your ability to absorb or pass on these insurance costs to your customers.

Employee Liability

An employee liability policy is selected when, as an owner or manager, you wish to supplement your general liability coverage with additional coverage for any harmful acts your employees may commit in the course of their employment. Some areas of coverage to be considered include those related to:

Wrongful termination
Workplace harassment
Sexual harassment
Breach of employment contract
Discrimination
Failure to employ or promote
Deprivation of a career opportunity
Negligent evaluation
Employment-related misrepresentation
Defamation
Theft

Dram Shop

Liquor liability, or dram shop, insurance provides establishments that sell alcohol coverage for bodily injury or property damage that may result from any or all of the following acts:

- Causing or contributing to the intoxication of a person
- Serving alcoholic beverages to a person under the legal drinking age
- Serving alcohol to an intoxicated person
- Violating any statute, ordinance, or regulation relating to the sale, gift, distribution, or use of alcoholic beverages

Serving alcoholic beverages in today's society makes a hospitality manager subject to great risk. Dram shop insurance is truly a necessity in today's legal environment, and states may require it as a condition for granting a liquor license.

Health/Dental/Vision

One of a hospitality manager's greatest costs, and one that continues to rise dramatically, is that of employee medical insurance. Although medical coverage such as health, dental, and vision insurance is not a requirement, the degree to which it is offered can have a significant effect on a manager's ability to retain and maintain a quality workforce.

Like all types of insurance, the varieties of coverage available for medical insurance are tremendous. In addition, this is one area of insurance where the cost is generally split, in some manner, between the employer and the employee. Employers can choose from contributing 100 percent of medical insurance premiums for their employees to simply making such coverage available to employees on a voluntary basis. Employees often depend on such coverage for their families and can maintain that insurance even if they lose their jobs.

The Consolidated Omnibus Budget Reconciliation Act (COBRA), passed by the federal government in 1986, requires employers to continue providing health, dental, and optical coverage benefits to employees who have resigned or been terminated, and to family members of employees who have lost their health insurance due to death, divorce, or dropping out of school. COBRA participants may continue their benefits for up to 18 months, with possible extensions to a maximum of 36 months, following the loss of their insurance; although they are responsible for paying the entire cost of their premiums.

In March 2010, President Barack Obama signed the Affordable Care Act into law. This legislation seeks to give individuals better health security by passing comprehensive reforms that hold health insurance companies accountable, lower health care costs, guarantee more choice to Americans, and enhance the quality of healthcare for

all Americans. The bill is comprehensive and extremely detailed, and any possible effects that the law will have on your particular hospitality entity should be discussed with competent counsel. The important thing to note about the law is that the changes it implements will be done on a staggered scale constituting five main phases that will take place periodically through 2018.

Workers' Compensation

The Workmen's Compensation Act of 1908 was the first effort to provide injury-related insurance to those workers who were hurt while on the job. This law, passed by Congress, which covers federal employees, spurred the states to enact similar legislation covering workers in their states. Today, all states require public- and private-sector employers to provide some form of mandatory workers' compensation insurance.

Workers' compensation policies provide payments to workers or their families in the event of an employee's injury or death. Coverage normally includes medical expenses and a significant portion of the wages lost by the employee being unable to work due to the injury. In more serious cases, lump-sum payments can be made to those workers who have been partially or permanently disabled. In addition, if a worker is killed while on the job, payments may be made to the worker's family. The injury must have happened in the "*course and scope*" of employment. The courts have broadly defined course and scope to sometimes include commuting to and from the place of employment, during mealtimes, or on or off the work site.

Injured employees are generally prohibited from suing their employer for damages beyond those awarded by workers' compensation. Only in the case of gross negligence or an intentional act will an employer potentially be subject to paying greater damages than those normally imposed by workers' compensation.

It is important to know that some states will designate specific doctors who will examine those employees who appear to have been injured. This is an effort on the part of the state to hold down premium costs and reduce incidents of fraud. It is also important to remember that employers cannot claim the negligence of the worker as a defense for a work-related injury. Usually, only in cases where the worker has been proven to be under the influence of drugs or alcohol at the time of the injury, or if the injury was fraudulent, will an employer be able to mount a legally valid defense against a workers' compensation claim.

In cases where another employee or third party has caused a worker injury, or when the employer challenges the legality of a worker's claim for compensation, a hearing is held before the state workers' compensation board. A judge will determine whether the claim has merit and how much compensation the worker is entitled to receive, if any. Both parties have the right to appeal the judge's decision, if they choose.

Because some form of workers' compensation is mandatory in every state, the failure on the part of management to provide it is punishable by fines and/or imprisonment. Employers are also required by law to accurately report on-the-job accidents to the state agency overseeing the workers' compensation program. This information is significant, as the cost of providing workers' compensation insurance varies based on the safety history of the employer, and the potential risk of injury to employees working for a specific employer. For example, a restaurant manager who does not encourage the immediate clean-up of spills in the kitchen, and thus experiences a greater-than-average number of employee injuries due to slips and falls, will pay a higher premium than an employer in an identical situation whose internal policies help prevent such accidents. Many state workers' compensation boards use experience ratings, which categorize businesses by the number of injury claims that are paid out, to determine the amount of insurance premiums that will be assessed.

Depending on the state in which they are operating, an employer may provide workers' compensation insurance through a private insurance company, a state

LEGALESE

Course and scope: The sum total of all common, job-related employee activities dictated or allowed by the employer.

agency, or itself. If the state allows a self-insurance option, the security deposit required can be substantial since, under the self-insurance option, an employer might be solely responsible for the payment of large awards in the case of a serious accident.

» ANALYZE THE SITUATION 15.2

CHRISTINA FLEISCHER WAS 16 years old when she was hired to work as a busser for a private country club. On Sundays, the club operated a popular brunch that served 500 to 1,000 people between the hours of 9:00 A.M. and 3:00 P.M. On Christina's first day of work, her supervisor quickly detailed the job requirements. As part of her job, Christina was to remove the guests' used dishes from the table, take the dishes to a bussing station, and scrape any leftover food from the dishes into a garbage receptacle lined with a plastic trash bag. Periodically, she was to bring the dishes to the kitchen to be washed and take the garbage receptacle to a designated area, where she would then remove the plastic trash bag and replace it with an empty one. The filled bags were left in the designated area until they could be taken out to a dumpster by a member of the dishroom staff. The garbage receptacles would often get very heavy, and all bussers were instructed to replace the plastic bags in them when they were half-full. Christina's supervisor made it a point of mentioning that during their 15-minute training session.

The club was very busy with Sunday morning brunch patrons on Christina's first day of work. Halfway through her shift, Christina forgot to replace one of the garbage bags until it was nearly full. She placed the garbage bag with the others in the designated location. Later that afternoon, a dishroom attendant, while taking out the 20 plastic garbage bags filled from the brunch, attempted to lift the bag that Christina had accidentally overfilled. The dishroom attendant seriously injured his back.

The injury was deemed within the scope of his work, so the dishroom attendant was awarded a monetary settlement by the workers' compensation board in his state. However, he then threatened to sue the country club, claiming negligence in Christina's training, and stated that this negligence was the direct cause of his accident. He also stated that management had provided workers with garbage receptacles that were too large and thus directly contributed to the accident.

1. Was management negligent?
2. Does the dishroom attendant have a viable claim against the club?
3. Do you feel the workers' compensation premiums for the club should be increased because of this incident?
4. What steps might the country club take to avoid paying higher premiums?

15.3 SELECTING AN INSURANCE CARRIER

Most insurance companies sell their products through agents, rather than directly to the public. Some companies use agents that represent them exclusively, while others use independent agents. These independent agents may represent several insurance companies, and can be a real asset in selecting the best policy at the best price. The premium rate, however, is set by the insurance company, and generally it cannot be changed by the agent.

LEGALESE

Underwrite: To assume agreed-upon maximum levels of liability in the event of a loss or damages.

An insurance agent does not provide insurance. The agent merely represents the insurance company that *underwrites* the actual insurance policy. When you buy an insurance policy, it is critical that you purchase it from a credible insurance company, and not just from an agent who is an effective salesperson.

If an insurance company is to protect against risk, it must have the financial capability to pay any and all claims you are held responsible for during the coverage period. The last thing you want is to buy an insurance policy, then relax, believing you have coverage, only to find out after a claim has been filed that your insurance company does not have the assets to pay the claim. It is important to remember that if your insurance company will not, or cannot, pay a claim, you will be held responsible for payment.

Insurance companies are rated based on their financial capability to pay claims. According to analysts, the stronger the rating, the more financially solvent the company is projected to be. Rating categories vary based on the organization doing the rating, but generally use either an A1, A, A2, B1, and so on, system, or an AAA, AA, A, BBB, and so on, system. Today, it would be difficult to justify purchasing an insurance policy from an underwriter with a rating of less than A2 or AA. It is best to buy from those companies that have achieved a rating of A1 or AAA.

Ratings can be verified by contacting the rating companies directly. A.M. Best and Standard & Poor's are two such companies. Alternatively, you can contact your state's insurance regulatory department. It can also provide you with a list of complaints filed against the insurance companies for failure to pay claims in a timely fashion or to act in good faith. This is information you need to know before you buy your policy.

Search the Web 15.1

Log on to www.insure.com.

1. Click on: Insurance Company Ratings under the "Insurance Tools" section.
2. Select: What the Ratings Mean.
3. Read the definitions of AAA through B insurance ratings.
4. Select: Access Ratings Lookup Tool.
5. Type the name of your own automobile or life insurance company into the search box, and click OK to find the rating of your own automobile or life insurance company.
6. What is your insurance company's rating?
7. How does it rank among the insurance companies in your state?

15.4 SELECTING THE INSURANCE POLICY

Once you have found two or three companies that you feel are financially sound, the next step is to get quotes, or bids, to provide coverage from each of the companies.

Consider the case of Vasal Bakar. Mr. Bakar is seeking to add a dental plan to his employees' health coverage. He selects three companies, all of which are rated AA, and proceeds to request a bid from each. When he asks for dental insurance bids to cover his 240 employees, he gets the following response:

| Dental Insurance Quote for Vasal Bakar | |
|--|----------------------------|
| Insurance Company | Coverage Cost per Employee |
| Company One | \$45.00/month |
| Company Two | \$43.25/month |
| Company Three | \$17.80/month |

While at first glance it might appear that Company Three is offering the best policy price, it will be important to determine whether the level of dental coverage is the same under the terms of all three policies. When Mr. Bakar investigated further, he found that in the proposals of the first two companies, annual per-employee maximum benefits were \$3,000, while in the case of Company Three, the per-employee annual maximum was only \$1,000. Under these circumstances, the price for each \$1,000 of employee dental insurance provided was actually highest from Company Three. The decision of whether to pay for the higher amounts of coverage, and whether the employees would be asked to contribute partial payments, is of course, left to Mr. Bakar.

To understand how much insurance you are actually purchasing for your premium dollar, and to realize how much total insurance you have for the period of time covered by the policy, it is critical that you understand the terms used in marketing insurance products.

Tina Shulky, the owner of a bagel franchise, is seeking liability coverage for her business. She selects some potential insurance providers, based on their financial ratings, then requests quotes on a *primary policy* with a *per-occurrence* amount of \$500,000, an *aggregate* of \$1 million, and an additional *umbrella* policy of \$1 million.

If the policy that Ms. Shulky ultimately selects states that she has \$500,000 of coverage per occurrence, it means that for each and every incident that occurs for which Ms. Shulky could be held liable, her insurance company will pay up to \$500,000 on her behalf, less any *deductible*. If the judgment exceeds that amount, she would be responsible for anything over and above \$500,000.

If her insurance policy has the term *aggregate* after the amount, it means that this is the total amount her insurance company will pay for all incidents and damages incurred during the coverage period. Thus, if she had a \$500,000 per-occurrence policy and \$1 million aggregate, two claims of \$500,000 would wipe out her total insurance coverage (as would four claims of \$250,000).

It's also important to understand how a deductible affects your total insurance costs. The deductible is an amount of money you are responsible for paying on a claim before your insurance company will begin paying for it. If you choose a high deductible, your premium payments will be lower, because you are assuming more risk by agreeing to pay a higher share of any claim filed against you. Managers must learn to factor the cost of the deductible into their insurance buying decision, and balance the needs of having a set amount of coverage that will be paid out by their insurance company with the amount of premium payments they are willing to make.

LEGALESE

Primary policy: The main insurance policy that provides basic coverage and the amount of insurance provided by the policy.

LEGALESE

Per occurrence: The maximum amount that can or will be paid by an insurer in the event of a single claim.

LEGALESE

Aggregate: The maximum amount that can or will be paid by an insurer for all claims during a policy period.

LEGALESE

Umbrella: Insurance coverage purchased to supplement primary coverage. Sometimes referred to as excess insurance.

LEGALESE

Deductible: The amount of money the insured has to pay before the insurance coverage will begin to pay. Accordingly, the higher the deductible, the less risk to the insurance company, which should equal lower premiums.

Basic coverage is referred to as primary coverage. In addition, you can purchase an umbrella, or what is commonly referred to as excess coverage. Be aware that umbrella coverage ordinarily pays only when and if your primary per-occurrence coverage is completely exhausted from a single claim.

To illustrate this point, assume the following scenario: You have a \$500,000 per-occurrence policy with \$500,000 aggregate, plus you have \$1 million in umbrella, or excess coverage. The policy period runs from January 1, 2012, to December 31, 2012. An accident occurs on January 20, 2012, and the claim is settled for \$750,000. The primary coverage will pay the first \$500,000, less any deductible you might have. Your umbrella policy will pay the remaining \$250,000. However, if you have a subsequent claim from an incident that occurs on February 15, 2012, how much coverage do you have available to pay this claim? The answer is zero. You have depleted your coverage under your primary policy because it has a \$500,000 aggregate. Your umbrella policy is not available, because it pays only if you have exhausted your primary per-occurrence amount on a given claim. If you do not have any primary per-occurrence coverage left, the conditions for coverage of your umbrella policy cannot be met, unless you are able to pay out of your pocket the first \$500,000. If you find yourself in this situation, you need to buy additional primary coverage.

15.5 POLICY ANALYSIS

LEGALESE

Face sheet: A one-page document briefly describing the type and amount of insurance coverage contained in an insurance policy. Sometimes referred to as a declaration page.

Analyzing an insurance policy consists of determining both what is and what is not covered. You are responsible for knowing and understanding the types and amounts of coverage that are written into your insurance policy. Additionally, be aware that when you purchase insurance, you ordinarily do not immediately receive a copy of the actual policy, because it takes some time for the insurance company to put the formal policy together with your unique coverages and exclusions. Instead, you receive a one-page *face sheet*, which generally sets out the types and amounts of coverage; it does not contain detailed information on what is specifically included and excluded from the policy's coverage. The actual policy will contain this information, but usually, you will not receive it until 30 to 60 days from the date of purchase. In other words, the face sheet contains the large print, or overview, while the actual policy contains the fine print, and you won't get the latter until after you buy.

Figure 15.1 shows a segment of language taken from an actual insurance policy. It is important to remember that, despite the difficulty of reading documents such as this, the courts will hold an insured party responsible for reading and understanding his or her policy. If you are at all unclear about what your final insurance policy will and will not cover, have your attorney review a sample policy, which can be provided by the insurance company.

Because you will not receive the actual insurance policy until after you purchase the policy, it is imperative that you discuss any unclear issues with the insurance agent before you buy. Ask for written answers to your questions, and continue to request information until you are satisfied with your comprehension of the details. Once the policy arrives, read it and make sure you fully understand:

- The policy's language, and whether it is consistent with your agent's earlier explanations.
- The policy's coverage, *exclusions*, *exceptions*, and clarifying language.

Most insurance policies will have both exclusions and exceptions. The insurer will almost always retain the right to exclude certain types of liability claims. If, for instance, a restaurateur has purchased fire insurance, but proceeds to intentionally set fire to his or her own restaurant, the insurance company would exclude, or refuse to cover, the cost of replacing the restaurant. Common exclusions include those involving intentional acts and fraud by the insured.

Exceptions are also common in insurance policies, and it is best to be well aware of all that apply. An exception is a statement by the insurer that it will not pay for an otherwise legitimate claim if certain conditions have not been met. For example, the

LEGALESE

Exclusions: Liability claims that are not covered in an insurance policy.

LEGALESE

Exceptions: Insurance coverage that is normally included in the insurance policy, but that will be excluded if the insured fails to comply with performance terms specifically mentioned in the policy.

B. Limits of Liability

Regardless of the number of persons or entities insured or included in Part I.D. Covered Persons or Entities, or the number of claimants or Claims made:

1. The maximum liability of the Company for **Damages and Claim Expenses** resulting from each **Claim** first made against the Insured during the **Policy Period** and the Extended reporting Period, if purchased, shall not exceed the amount shown in the Declarations as each Claim;
2. The maximum liability of the Company for all **Damages and Claim Expenses** as a result of all **Claims** first made against the Insured during the **Policy Period** and the Extended Reporting Period, if purchased, shall not exceed the amount shown in the Declarations as Aggregate.

The Company shall not be obligated to pay any **Claim** for **Damages** or defend any **Claim** after the applicable Limit of Liability has been exhausted by payment of judgments, settlements, **Claim Expenses** or any combination thereof. **Claim Expenses** are a part of and not in addition to the applicable Limits of Liability. Payment of **Claim Expenses** by the Company reduces the applicable Limits of Liability.

The inclusion of more than one Insured, or the making of **Claims** by more than one person or organization, does not increase the company's Limit of Liability. In the event two or more **Claims** arise out of a single negligent act, error or omission, or a series of related negligent acts, errors or omissions, all such **Claims** shall be treated as a single **Claim**. Whenever made, all such **Claims** shall be considered first made and reported to the Company during the **Policy Period** in which the earliest **Claim** arising out of such negligent act, error or omission was first made and reported to the Company, and all such **Claims** shall be subject to the same Limit of Liability.

Figure 15.1 Insurance policy language.

insurance company may require a restaurant to have a valid license to serve food, in order to protect that restaurant in the event a guest claims damages resulting from food poisoning. Likewise, a fire insurance policy may require that an operator purchase and install specific types of fire suppression equipment, and that the equipment be inspected and approved on a regular basis by a qualified inspector.

In most cases, your insurer will require you to notify the company immediately if a claim is made by you, or if you believe something has occurred that might lead to litigation. In addition, if an attorney serves you with notification of intent to sue you, you must contact your insurance carrier. Some insurance policies are “claims made” policies. This term means that the coverage is available only if an actual claim is brought to the attention of the insurance company during the policy period. Most insurance policies, however, cover claims that occur during the policy period, even though they are not brought to the attention of the insurance company until after the coverage period has elapsed. Obviously, this type of policy is preferable to the “claims made” policy.

In spite of the problems and expense involved, insurance is not an option; it is a protection needed to operate your businesses with a sense of comfort and peace. You can avoid unpleasant surprises by taking the proper care when selecting insurance. This includes speaking and listening to your colleagues and asking those questions that will make it easier for you to purchase the right coverage in the right amount from the right insurance company.

Most policies are issued for a one-year period. Generally, new policies are issued annually, assuming that there is mutual satisfaction with the coverage, claim responsiveness by the carrier, and an agreement as to the premium (or cost) paid for the amount of insurance.

In Chapter 9, “Your Responsibilities as a Hospitality Operator,” we examined how you can take steps to reduce insurance costs through the effective management and training of staff. Prevention of insurance claims, like the prevention of all legal claims, should be the goal of every hospitality manager.



INTERNATIONAL SNAPSHOT

Hotels Operating Internationally Need to Think Globally about Their Insurance Programs

Due to a number of factors, international insurance issues typically lag behind the U.S. insurance market by several years. These factors include:

- Less litigious claims environment
- Lower claims counts
- Absence of punitive damages
- Social environment, as respects claims

Because of this, international insurance pricing has remained lower than that in the U.S. insurance market. Quite often, this has led multinational hotel chains to place more emphasis on claims and risk control in the United States. Most hotels, especially those chains with large properties, are fairly adept at the basics of risk management that will allow them to control claims costs, minimize litigation potential, and maximize safety and risk mitigation. Too often, these concepts are not pushed out to the overseas locations on a consistent basis due to cost or internal operational hurdles.

Meanwhile, as the hotel industry was focused on the tight insurance market in the United States, the international insurance market and global legal climate changed in ways that are critical to the way a hotel operates. Over the past five years, the international insurance industry has started to drive the development of more sophisticated risk management programs throughout the world through market selection and pricing. The increasingly tight and limited international insurance capacity for both property and casualty lines is going to force multinational hotel chains to take more risk and to manage that risk in more countries.

WHY IS THIS HAPPENING?

A number of changes within the global insurance market and global legal climate are forcing underwriters and hotels alike to reexamine international insurance:

Market capacity: Because hotels have traditionally been loss leaders in the insurance marketplace, there have always been a fairly small number of insurance carriers that are willing to look at a hospitality risk.

Additionally, in the past five years, numerous insurance companies that have done multinational programs have left the market—Kemper, Royal US, and others. More international carriers have moved away from doing hospitality risks at all. This puts fewer markets in play for a hotel risk and forces pricing and selectivity up.

Legal changes: The world legal climate still remains well behind the litigious environment in the United States. However, there have been significant increases in “claims awareness” in a number of countries. While the systems are not as developed, they are nevertheless making large strides and increasing claims for the hospitality industry. There is also a growth of global case law—that is, legal decisions in countries such as Australia have cited California case law.

Claims counts: Around the world, we are seeing sharp increases in the claims counts being recorded on hospitality business. Since underwriting pricing is traditionally much lower on international accounts, as compared to U.S. accounts, this increase will put an immediate strain on insurer profitability and insured’s costs.

Social change: More and more, we are becoming a global economy. People travel the world and expect the legal system to keep up with them—not the other way around. Legislation such as the European Union’s Tour Operators Liability is globally focused. Hotels need to protect every location they have in every country of the world, not just those where the claims occur.

WHAT SHOULD BE DONE?

Hospitality companies need to start managing the risk worldwide more aggressively than ever before. The basics of risk management need to be adhered to by all locations. Additional strategies would include:

Claims and litigation management: Hotel chains should settle claims worldwide in the same manner, whether they are self-insured or not. A claim settled in Germany should be settled in the same manner as a claim in California. This will allow a hotel to create precedent in a lawsuit situation, not be surprised by it.

Program management: Many international programs stand alone from a domestic program and may or may not require participation from all locations. This should be managed very closely: as carriers fail or exit the hospitality business, it will be much harder to be reactive to a program change than be proactive to it.

Brand-name protection: All locations bearing the company name should be required to carry the same levels of insurance or carry a documented exception. All franchises should be required to carry U.S. suits no matter where they are in the world. Since that is not available in most countries, they should be required to purchase this as part of a program that the parent company sponsors. As lawsuits go global, companies need to ensure that the brand is protected in any court in the world.

Information management: The key to underwriting and managing insurance risk is information flow. Standardize the forms for information on property and liability risks. Enforce the forms and collect them annually. Although this is an administrative burden, it is critical to managing the insurances.

Insurance programs should help a hotel manage its risk. Historically, most international hotels have used insurance as a reason *not* to manage their risk, since it did not cost them to have claims. As the changes evolve, a hotel chain must be a step ahead of its carrier to allow it to control its own insurance destiny.

Provided by Elizabeth Francy Demaret, Managing Director, Worldwide Risk Services Group, Arthur J. Gallagher & Co. in Itasca, IL. www.ajg.com.

WHAT WOULD YOU DO?

Assume that you are an insurance agent with the Arizona Business Insurance Company (ABIC). You sell ABIC products exclusively.

Your company, which is rated AA, offers insurance coverage against a variety of risks, including workers' compensation, and specializes in the hospitality industry.

You are approached by Ted Betz, the operational vice president of J-Town Smokies, a chain of pit barbeque restaurants. Mr. Betz would like to purchase workers' compensation insurance from your company because he will be opening five stores in the Southwest in the coming year.

A review of his application and claim history indicates that J-Town Smokies has experienced a rather large number of worker injuries in its four years of existence. In fact, the rate of worker injury per man-hour worked is nearly two times that of the restaurant industry average. Further investigation indicates that most of these injuries resulted from cutting meat prior to or after the barbeque process.

A review of the U.S. Department of Labor statistics reveals the following highest injury rate industries for this year and last.

| | Employees (in thousands) | Accident Rate per Thousand This Year | Accident Rate per Thousand Last Year |
|-----------------------------|---|---|---|
| Meat-packing plants | 147.2 | 36.6 | 30.3 |
| Ship-building and repairing | 102.5 | 32.7 | 27.4 |
| Steel foundries | 26.6 | 26.4 | 26.4 |
| Mobile homes | 68.0 | 24.3 | 26.2 |
| Automotive stamping | 117.7 | 23.8 | 23.2 |
| Restaurants | 250.0 | 16.1 | 16.6 |

1. What type of information would you want to see from Mr. Betz before you offer to sell him a workers' compensation policy from your company?
2. Do you believe Mr. Betz's restaurants should pay the same amount for workers' compensation coverage as other restaurants, or should he be charged rates consistent with those in the meat-packing industry?

THE HOSPITALITY INDUSTRY IN COURT

To review a case that involves the distinction between furniture and permanent fixtures, as discussed in Chapter 6, and to learn how insurance policies are closely analyzed by the courts when there is a dispute, consider the case of *Prytania Park Hotel v. General Star Indem.*, 179 F.3d 169 (5th Cir. 1999).

FACTUAL SUMMARY

The Prytania Park Hotel (Prytania) in New Orleans, Louisiana, was heavily damaged by a fire in one of the hotel buildings. The guestrooms in the hotel contained custom-made furniture, which was attached by screws and bolts to the walls of the rooms. A significant amount of the furniture was destroyed by the fire. The owners of the Prytania submitted a claim to General Star Indemnity Company (General Star), the insurer of the hotel.

The insurance policy for the Prytania covered loss or damage to the building, loss or damage to business personal property, and loss of business income resulting from business interruption. The provision in the policy for loss or damage to the building included permanently installed fixtures, machinery, and equipment. Prytania was entitled to the full replacement value of permanently installed items under the terms of the policy.

The business personal property provision in the policy included furniture and fixtures, and limited the amount of a claim to the actual cash value of items lost or destroyed. The owners of the Prytania submitted a building claim to General Star for \$276,687.96. This amount included the damaged hotel building and all the hotel furniture at full replacement value. A contents claim was also submitted in the amount of \$85,888.10, covering business personal property, but not the hotel furniture. Prytania also submitted a claim \$75,000.00 for loss of income.

General Star adjusted the claims and paid \$186,448.47 on the building claim, which did not include compensation for furniture; \$68,273.93 on the contents claim; and \$34,988.00 for loss of business income. The owners of the Prytania sued General Star to recover the unpaid portions of the claims.

QUESTION FOR THE COURT

The question for the court concerned the definition of permanently installed fixtures under the building provision and furniture and fixtures under the business personal property provision. Prytania argued the hotel furniture was permanently installed fixtures since removal from the walls would cause considerable damage to the furniture and walls. Prytania also argued the room furnishings were permanently installed fixtures based on the dictionary definition of each word. Since the owners intended the furniture to stay in one place and it had been secured to the wall, they argued it was permanently installed.

General Star argued the hotel furniture was clearly covered under the business personal property provision since the word “furniture” was used there and not in the building provision. Additionally General Star offered evidence showing removal of the furniture would cause no damage to either the furniture or the room.

DECISION

The court held the guestroom furniture was not permanently installed fixtures under the building provision of the policy. The furniture was covered under the business personal property provision since furniture was explicitly listed under the category. The court also found the furniture was not permanently attached since removal was possible without damage to the room walls or furniture.

MESSAGE TO MANAGEMENT

In insurance policies, leases, and other legal documents, it pays to clearly describe personal property, fixtures, and real property.

Insurance is a valuable tool to help protect a business and its owners from financial loss. There are many different types of insurance coverage, including property/casualty, liability, health/life, and that for injuries to workers. Not all insurance companies are the same, so an owner/operator should research a company's reputation, claims-paying record, and financial strength prior to purchasing the needed coverage for the business. A thorough understanding of the terms used in the insurance industry—such as primary, umbrella, exclusions, and exceptions—is crucial for an owner/operator to make informed decisions about coverage and pricing.

WHAT DID YOU LEARN IN THIS CHAPTER?

After you have studied this chapter, you should be prepared to:

1. Describe the importance of mathematics and statistics to the insurance industry.
2. Identify at least five types of insurance that would be needed by a nightclub or bar owner, and discuss the importance of each.
3. Assess the pros and cons of self-insurance in the area of workers' compensation.
4. Use the Internet to find a company that will likely provide liability coverage for your new hotel. Assume that the hotel is to be built in Berlin, Germany, and that your company requires a minimum of an AA Standard & Poor's financial-strength rating.
5. Assess the legal climate today, and then determine the amount of umbrella coverage your hospitality company would need to defend itself against a wrongful death suit brought about by dram shop legislation. Assume that you have \$1 million in primary coverage. Be prepared to discuss the factors that influenced your decision.
6. Describe the function and limitations of a face sheet, or declaration page.
7. Develop a checklist for purchasing insurance, beginning with the recognition of the need for insurance to the evaluation of the face sheet and actual policy.
8. Describe, in detail, an example of both an exclusion and an exception that might be in effect with a workers' compensation policy at a hospitality operation where you have worked.

RAPID REVIEW

In teams, identify and evaluate Internet sites that would enable a prospective purchaser of insurance to discover information about various types of insurance coverage, the financial status of the companies offering the coverage, and the cost for the coverage. Present to the class the top three sites, and describe why your team selected them (e.g., scope and depth of information, ease of navigation, etc.).

TEAM ACTIVITY