Beazley Insight
Don’t Buy into a False Economy

by Bryan Falchuk

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Small businesses, in particular, need to be wary of cutting insurance costs that may leave them open to far greater – indeed potentially crippling – costs down the road. Bryan Falchuk of Beazley Group’s Private Enterprise team shares his thoughts and advice on this issue critical to today’s small business owner.

Risks loom large in this economy

The recession poses great risks to small businesses since employees and customers who are also struggling financially may seek desperate measures to profit or recoup their own losses. These risks may surprise small business owners whose ethics and professionalism have never previously been questioned.

For example:

An independent software consultant may be extremely ethical and never breach a contract. But what happens when their client can’t pay for their services – a real and growing risk today? The client may claim breach of contract to try to get out of paying. The consultant may be innocent and a trial may vindicate them in the end. But the defense costs can be ruinous, easily running to $50,000, $100,000 or more. These costs would have been covered by professional liability insurance. The risk to the business is thinking they’re safe because they would never do anything wrong. Unfortunately, that isn’t enough protection.

More vulnerable to cyber risks

Cyber risks are very serious for small companies. Although bigger companies may spend millions of dollars protecting themselves, small companies don’t have those financial resources. Hackers are increasingly targeting smaller companies. They know these businesses aren’t spending money on network security, so hackers are stepping up their efforts to steal private data from smaller targets.

The Ponemon Institute tracks the costs involved with data breaches – someone hacking into a system and getting customer records. The cost is currently estimated to be $202 per customer record – which sounds small but adds up quickly.
For example:
• A small online retailer may make 10 sales a day. That’s more than $700,000 for a year’s worth of customers. Multiply this by the number of years the retailer has been in business, and it can easily reach multiple millions of dollars.
• An outpatient medical facility such as an MRI center is often fully booked and may have as many as 15 scans a day. That’s more than $1 million for each year in business. Again, the cost of a data breach could put a small company out of business.

Small businesses are under pressure
For most businesses, insurance is not a priority. Companies are focusing on paying rent and wages, covering their inventory needs and cutting costs. But skipping insurance, or skimping on it, is a false economy. A company may save $3,000 or $4,000 on insurance premiums but this will seem like pennies compared to the huge costs of legal defense that would have been covered with professional liability insurance. One lawsuit can bankrupt a small company.

Three steps toward a stronger financial future

1. Buy the right coverage, and not just an empty policy. Unlike auto insurance where a driver can strip out towing or rental car coverage and use public transportation or call AAA if their car is in an accident, a stripped down policy leaves a business exposed.

2. Small businesses can find affordable options, but need to be smart about their choices. Once a business finds the appropriate coverage, they should look at their deductible strategy to manage the premium costs. Like personal auto insurance, the bigger the deductible, the lower the premium. A business that chooses the largest deductible it can manage in the event of a catastrophe will end up with solid coverage at a more affordable price.

3. Pick an insurer that sells complete coverage in one unified form instead of pieces to pick and choose. Businesses that make complete coverage a priority and use deductibles wisely to manage costs will be in the best position possible in this economic environment.
For more information on other resources pertaining to small businesses, visit the US Small Business Administration website at www.sba.gov.

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