Interruption insurance cannot shoulder risks of load shedding

Business interruption insurance is not a solution for load shedding risks and 90% of business interruption insurance claims related to load shedding will not be paid out.

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Blackouts are estimated to have shaved 0.3% off the GDP, or $940 million, in 2014 after the country experienced weeks of rolling power cuts, the first since 2008. A continuation of this trend this year has placed increasing strain on an economy struggling to eke out even 2% growth, and as a result, many businesses are mistakenly taking out business interruption policies as cover against power outages.

Bryan Verpoort, Head of Corporate and Business Insurance at Standard Bank, says business interruption insurance should not be seen as a solution for load shedding. "In terms of insurance if a risk is not foreseeable, then you need to take precautions, but load shedding is foreseeable, which makes it challenging to insure.

"What this means is that a loss of profits needs to have been caused by an unforeseeable physical event like a fire, explosion, or flood, but can't be attached to Eskom not providing adequate power."

He says because load shedding is likely to be an ongoing problem, businesses should rather consider implementing long-term strategies to deal with power outage issues. "It is important for businesses to adapt to this changing environment to limit financial losses and 'do business differently' to get around inefficiencies, for example, investing in a generator."

Load shedding means businesses and residences lose power during peak periods. Shopping malls shut down on weekends, a peak period, while industrial users have had to cut down usage by as much as 10% during the workweek - when they would normally be in their highest production phase. An added problem has been water failures due to a lack of power to pump the water.

"Businesses need to understand that as a general rule, load shedding is not automatically covered, it will depend on which policy has been taken out and the reason for the power failure."

Business interruption insurance includes perilous events like wind, snow, fire, or an explosion as the underlying cause. "Load shedding happens because demand is exceeding supply, which is not an insured event. It's a fact that the economy has outgrown supply, which is not an insured peril if you look for the proximate cause of the loss or damage."

Insurance not the answer

Businesses should be careful when considering business interruption insurance, if ultimately they will not be covered but in a majority of cases, the policy will not respond. The problem is that many businesses are not properly educated about this and think they are covered, or buy insurance that will ultimately not cover them. Depending on the policy, coverage would generally apply up to a limited amount, where power surges cause damage to equipment, such as servers or printers.

Big companies with electricity offtake agreements would likely have wide, extensive coverage. They could then argue that as a direct consequence of a silo collapse, for example, they suffered downtime at a furnace. It is likely that peril would be covered. However, smaller businesses would not have this type of extensive coverage. Businesses should not assume, for example, that because there is an explosion of a transformer at a utility down the road, that the explosion would be covered in most policies.

"Blackouts are bad enough, but an increasing risk is that most businesses do not understand how little insurance coverage they have when the lights go out. It is therefore important for businesses to understand what their policies cover and also work on long-term strategies to deal with power outage problems," he concludes.