



HOME-BASED AND MICRO BUSINESSES
**CASHING IN ON
BUSINESS OPPORTUNITIES**

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INSURING AGAINST CATASTROPHES

PREFACE

This guide includes the basic text for teaching risk management concepts. If the types of businesses are identified before the workshop, you can use related examples.

How you use this curriculum depends on the needs of your audience and the time allowed for presentation. It is developed to be presented in 45 minutes to one hour. The liability section can be used alone in a workshop setting (one hour) or as a presentation (20-30 minutes).

Throughout the text, suggestions for use of slides and handouts that are in the appendices are on the left side of the page. Nine case studies are included. Select ones that are relevant to the participants in your workshop. Insurance regulations may differ among states; a good source of generic information is the Bureau of Insurance in each state. You also may want to invite an insurance broker or a business person who has experienced insurance claims to come in as a resource person. A list of additional resources is also included.

Goal: The goal of this session is for business owners to assess risks and develop strategies to manage those risks.

Objectives: On completion of this unit participants will be able to do the following:

- Recognize the importance of risk management for their businesses
- Understand risk management strategies
- Define insurance types and their relationship to a home-based or micro business
- Assess risks and determine management strategies for individual businesses

HANDOUTS

Handout 1 – Liability Insurance Needs for the Home-Based or Micro Business

Handout 2 – Home-Based Business Liability Insurance Information (Sample of Survey)

Handout 3 – Risk Management

ADDITIONAL RESOURCES

Burkhart-Kriesel, C., Gessaman, Paul H. (1996). Setting Up Your Own Business: Planning Your Insurance Coverage. Cooperative Extension, University of Nebraska-Lincoln, NF 96-277.

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Don Hofstrand, Assessing Financial and Risk Management Skills, Iowa State University, Extension, File C6-65, March 2008, <http://www.extension.iastate.edu/agdm/wholefarm/pdf/c6-65.pdf>

Weagley, R. O., Risky Business: Family Insurance Planning, University of Missouri Extension, GH3420, Reviewed June 2009, <http://extension.missouri.edu/publications/DisplayPrinterFriendlyPub.aspx?P=GH3420>

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INSTRUCTIONAL MATERIALS

Risk management is the process of identifying situations involving risk to determine the appropriate means for its management. Although most of the discussion will center on insurance issues, it is important to recognize other ways of managing risk.

RISK MANAGEMENT

What is risk?

Risk is uncertainty about the outcome of a situation or event. As it relates to the business, it is usually thought of as a situation or event that would cause a financial danger to the business.

SLIDE

1

Four basic ways to manage risk:

Avoid it. Avoid it by not participating in risk-taking activities. Examples: to avoid a motorcycle accident, you wouldn't ride a motorcycle. In business, you might deliver finished products rather than risk someone's coming to your home and having an accident.

Reduce it. You can reduce risks by trying to prevent certain losses. Examples: in the home - safety precautions such as smoke detectors, locks, a fire extinguisher; automobile - use of seat belts, following safety laws, keeping vehicle in good repair.

Accept it. Any time you don't avoid, reduce, or transfer a risk, you are, in essence, saying "I accept that risk and can afford to cover any loss." Examples: establishing an emergency fund to cover deductibles on insurance policies.

Transfer the risk. A transfer is an arrangement where you would be reimbursed by another party in the event of financial loss - usually by purchasing insurance.

Insurance is a procedure for transferring and reducing risk by having a large number of individuals share in the financial losses suffered by members of the group. The contract with the insurance company usually includes a responsibility on its part to defend you in the event of a claim or legal action against you that is covered under the policy.

Much of the insurance needed for your business is an expansion of your personal insurance needs. You can insure only against financial loss. It is not reasonable or practical to insure against all possible losses.

Insurance protects you, your family, and your business against financial losses you cannot afford to accept. The cost of insurance coverage needs to be included in the financial plan for your business. The secret is to get the coverage you need but not more than you need at a cost the business can support.

BASIC TYPES OF INSURANCE

This section discusses basic types of insurance and needs created by having a home-based or micro business. Insurance needs will vary, depending on whether the business is the only source of income for the family and the type of business. The next section will provide a guide for determining insurance needs of your business.

If you are leaving a job where some kinds of insurance were previously provided by your employer, you will need to replace this coverage as well.

Health Insurance. Health insurance protects against financial losses resulting from illness, injury, and disability. High uninsured medical costs for you and your family could jeopardize the business.

Life Insurance. Life insurance protects against financial losses resulting from death. If you think this isn't a business need, ask yourself, How much of my family's financial support comes from the business? Are there business debts that need to be covered? In the event of my death, how much money would be needed to keep the business running until it could be sold or closed?

Income Insurance. Income insurance protects against the loss of future income. If you employ others, you will need to check your state laws to determine how to purchase the following:

- **Unemployment insurance** - paid to employees who qualify but no longer work for you.
- **Worker's compensation insurance** - paid to employees who are injured on the job while working for you. You pay a premium to the state, and the state makes the payments to the employee when he/she meets the qualifications.

To protect yourself you will want to consider these:

- **Disability insurance** - to provide income if you cannot work as a result of an injury or prolonged illness.
- **Business interruption insurance** - that compensates for income loss to you and protection against not being able to honor contracts, in the event of your disability, "damage to goods or production location, causing an interruption of the business."

Property Insurance. Property insurance protects against financial losses resulting from damage to or destruction of property or possessions.

- **House.** Your house is insured as a dwelling place for you and your family. Adding a business to the house could negate that coverage unless you add insurance covering the house and other property for business use.

Additional coverage may be needed for the following:

- the dwelling that houses the business
- a computer and/or business records
- equipment to produce a product
- inventory of raw supplies

- inventory of finished products
- injury to employee or customer on the premises
- **Automobile or other vehicles may need additional coverage.** If you use your personal car to make deliveries and merchandise is stolen, or if you get into an accident as you are driving to a customer call, your insurance may not cover the loss if you have not insured the vehicle for business use.

Insurance coverage on property for business use may be in the form of a rider to current policies or require a separate business policy. This would vary with the type of business and the insurance company.

SLIDE

3

Liability Insurance. Liability insurance protects against financial losses suffered by others for whom you are responsible. This may be the result of negligence or when a contract, law, or court judgment requires you to pay for the losses of another. Liability and the threat of lawsuits appear to be what individuals starting up businesses worry about most.

HANDOUT

1

The number of insurance claims and the costs of these claims continue to increase. Anyone who produces any item or provides any service in exchange for money is vulnerable to a liability claim.

SLIDE

4

Types of liability insurance that may be needed:

- **General liability insurance.** This protects the business from financial loss because of bodily injury or property damage to employees or customers caused by negligence.
- **Personal injury.** A customer or delivery person is injured at your home or by your vehicle. Example: A customer slips on a rug as he enters the home and breaks an arm.
- **Property damage.** Property damage to another's property by you in the course of doing business or at your business. Example: Your child breaks the window of a customer's car.
- **Product liability.** Someone is hurt using your product. One thing to keep in mind is that products are subject to the laws of the state in which they are sold as well as the state in which they are produced. If items are sold across state lines directly or by mail order, you would want to check on this. Product liability laws are not uniform, but your attorney or insurance agent should be able to help you determine what your needs might be. Example: A child chokes on the button used for an eye on a teddy bear.
- **Professional liability.** This provides protection for a business that provides a service or gives advice such as beauticians, cleaning or maintenance, tax preparers, or financial counselors.
- **Service provided causes property damage or personal harm.** Examples: A weed killer application damages other plants. A hair dye causes damage to a client's hair.
- **Omissions or commission.** An error on your part or failure to do something created a loss to a customer. Example: An error on a tax report you completed.
- **Breach of contract.** This protects against failure to fulfill a signed contract due to business interruption, damage to goods, inability to get supplies, or any other reason; and the holder of the contract sues. Examples: A wedding cake cannot be delivered, since it was destroyed in an accident. An order for several hundred items cannot be

filled because of equipment breakage.

- **An umbrella policy** that covers all forms of liability can be purchased. This may be a separate policy or a rider on your homeowner's insurance. The cost of the coverage varies depending on the business to be insured, location, and the insurance company.

(The handout is a brief survey done in one locality of costs for different amounts of insurance for different businesses. You may want to do one for your locality.)

STEPS TO DETERMINE INSURANCE NEEDS FOR YOUR HOME-BASED OR MICRO BUSINESS

This section lists some steps to be taken to determine the risks related to your particular business. This will help you think about how you will do business and what risks need to be insured.

Define the related risks. What are some of the risks your business involves? Think about how the business is conducted, where a product is made, and who is responsible for the product.

Rate the likelihood of loss. Look at each of the risks identified and think about how likely it is to occur. For example, if there are no trees near the driveway, it is not likely that one would fall on a customer's car.

Rate the size of loss. If the loss occurred, what would be the financial damage to the business? Example: if one craft item is broken, the loss is minimal. If a van load of the items is destroyed, the loss could be substantial.

Consider risk management strategies. Which of the risks that have been listed can you avoid, reduce, accept, transfer to insurance?

Discuss with an insurance agent/broker. To find insurance for the home-based business, start with your current insurance agent. The coverages you need may be available using riders on your current household and vehicle insurance.

Another source is trade organizations, which may be associated with the product made, the marketing region, or some other related group.

Best's Insurance Guide, available online at www.ambest.com/ratings/guide.asp, is a source to check the reliability of an insurance company before you do business with that company.

(Handouts 1 & 2 may be used with the case studies to analyze risks related to different types of businesses.)

2

HANDOUT

5

SLIDE

3

HANDOUT

6

SLIDE

4

HANDOUT

SUMMARY

1. To organize your insurance program, you must first recognize the risks you and your business face.
2. Decide which things to insure against and how much loss you would suffer from each.
3. Select an insurance agent/broker who can help you secure protection for your business within the limits of its ability to assume risk and pay insurance premiums.
4. Cover your largest loss exposure first.
5. Use the highest deductible you can afford to lower premium costs.
6. Plan for adequate care and protection of insurance and business records and keep complete records of your insurance coverage.
7. Review your insurance program periodically to ensure adequate coverage and that there is no duplication.

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HANDOUT 1

LIABILITY INSURANCE NEEDS FOR THE HOME-BASED OR MICRO BUSINESS

LIABILITY INSURANCE - protects against financial losses suffered by others for whom you are responsible. Such responsibilities arise when you are negligent or when a contract, a law, or court judgment requires you to pay for the losses of another.

My business is:

Types of liabilities Personal injury - home or vehicle:

Property damage - home or vehicle:

Product liability:

Professional liability Service:

Omissions or commission:

Breach of contract:

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HANDOUT 2

HOME-BASED BUSINESS LIABILITY INSURANCE INFORMATION

	Insurance Company #1	Insurance Company #2	Independent
Bed & Breakfast	No Requires Business Policy	No Requires Business Policy *	No Requires Business Policy
Child Care	Yes Limit \$500,000 Premium \$155 Deductible \$250	Yes Limit \$500,000 Premium \$144 Deductible \$250	Yes Requires Business Policy
Desktop Publishing	Yes Limit \$500,000 Premium \$28 Deductible \$250	Yes Limit \$500,000 Premium \$66 Deductible \$250	Yes Limit \$1,000,00 Premium \$300 Deductible \$250
Catering	No	No	No

*Notes:

1. Unless specified, each policy is a rider to existing homeowner's policy.
2. Bed & Breakfast liability insurance requires business coverage. Basic rates start at \$280 per year.
3. Each insurance company will provide literature.
4. Insurance professionals recommend "umbrella" liability policies for coverage up to \$1,000,000
5. Insurance will not insure home-based catering firms.

Local insurance agents in one state were contacted in 1995 and asked if the company offered liability insurance as a rider to homeowner policies for the above businesses. If the answer were yes, they were then asked about coverage limits, premiums, and deductibles. Information may vary from state to state and regulations may differ.

Prepared by Constance Kratzer, Extension Specialist, New Mexico State University - College of Agriculture & Home Economics, formerly Extension Specialist, Virginia Polytechnic Institute and State University.

HANDOUT 3

RISK MANAGEMENT

Type of business:

1. Define the related risks.
 - What are some of the risks this business may face?
 - Think about how the business is conducted, where a product is made, who is responsible for the product, etc.
2. Rate the likelihood of loss.
 - Look at each of the risks identified and think about how likely it is to occur.
3. Rate the size of loss.
 - If the loss occurred, what would be the financial damage to the business.
4. Consider risk management strategies Which of the risks that have been listed can you
 - Avoid
 - Reduce
 - Accept
 - Transfer to insurance
5. What is the most critical insurance need this business should discuss with an insurance agent/broker?

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HANDOUT 4

CASE STUDIES

I. Betsy's Typing Service

Betsy has just started a typing service in her spare room. She has a computer with a word processing program, and a laser printer. She has been advertising through flyers at the local community college. The word of her good service and rates is spreading, and she is getting more business all the time. She has been making one trip a day to the student activities building on campus to pick up work and deliver the typed papers. Some of the students have started dropping off work at her home, which saves her some time.

Betsy has a comprehensive homeowner's insurance policy. She also carries full coverage on her car. This car is listed as a second car for the family. She feels as though she is well insured. Is she? How would her current insurance protect her if the following things occurred?

1. A student slips and falls on her front step while he is delivering a paper to be typed. He has a broken elbow and will not be able to finish the basketball season. He has been threatening to sue for his medical expenses and damages suffered from not being able to play basketball.
2. Betsy has an auto accident on her way to the college to deliver papers. The police find her at fault and give her a ticket. The passengers in the other car were, fortunately, not injured, but both cars were totaled.
3. There is a fire in her basement caused by an electrical short in a space heater. There is heavy smoke damage to the whole house. The computer and printer had to be specially cleaned before they would operate properly. Much of the information on the hard disk drive was destroyed. Betsy will have to replace the word processing program because the copy on the hard disk was ruined and her original copy was damaged from the smoke. She also lost most of the home furnishings, and all of the carpet had to be replaced.
4. Because of the fire, Betsy is not able to meet some of her deadlines, and some of the original student work is destroyed. One of the students sues her for damages when he gets a poor grade because the paper was late.

Prepared by: Carol Schwab, Associate Professor, North Carolina State University.

II. John's Woodworking Business

John has started a woodworking business in the garage. He is selling personalized signs and placards. He is currently selling most of the items through the Internet and at craft shows in the area. Most of his Internet business comes from classified ads in the back of magazines.

The Internet business has kept him pretty busy, and he hardly has time to amass the inventory for the next craft show.

John has a broad based homeowner's insurance policy. He also has an old van that he uses to transport the merchandise to be mailed and when he displays at local craft shows. He carries only liability insurance on the van. Since the van is old, he doesn't feel it is worth carrying comprehensive and collision coverage. He feels he is well insured because he pays a great deal for insurance each 6 months. Is he? How would his insurance protect him in the following situations?

1. On his way to a craft show, John stops for lunch. His van is broken into while it is parked in the mall parking lot. Much of his merchandise is stolen or damaged.
2. John has an auto accident while he is picking up lumber for his business. The police determine that John was at fault and give him a ticket for a traffic violation. Will his auto insurance pay for repairs to the other car? For the personal injuries to the passengers in the other car? For the lumber that was damaged in the accident?
3. During a craft show, a child was looking at the merchandise. The child cut her finger on one of the screws in a sign. The parents are threatening to sue for medical expenses and pain and suffering, as well as punitive damages.
4. While John is away at a craft show, someone broke into his garage and gained entry to his home. The burglar vandalized the garage, the sign making equipment, the inventory, and the kitchen. The loss is estimated at \$10,000 for the damage to the kitchen and \$4,000 to the garage and contents. The police have not yet determined who was guilty of the crime.

Prepared by: Carol Schwab, Associate Professor, North Carolina State University.

III. **Terrible Two's Child Care Center**

Marjorie Brown opened a child care center in her home. She planned to care for only two children at a time, so she didn't consider this a "real" business. Everything went along fine until one day, two-year-old Jimmy was playing with two-year-old Billy. They were playing with play telephones. They were trying to talk to one another with their limited vocabulary. Jimmy got frustrated and conked Billy on the head with the receiver of the play telephone. This opened up a gash in Billy's head that required three stitches at the emergency room. Who will pay the bill? Jimmy's parents? Marjorie Brown? Marjorie's homeowner's insurance?

IV. **Jenny's Wedding Cakes**

Jenny just started a wedding cake business. She plans to deliver all cakes to the customer and never ask anyone to come to her home. She has applied for a vendor's license, a business tax number, and a business telephone number with an ad in the yellow pages. Since no one will be coming to her home for business reasons, does she need to alter her

homeowner's insurance policy? Are there other types of insurance she now needs?

V. Pete's Mail Order

Pete runs a mail order business from his home, selling all types of tack for horses. He decided to publicize his business by putting a sign on his pickup truck. Since he doesn't use the pickup to transport raw materials and inventory, he feels there is no reason to notify the auto insurance company of his business or the sign on the truck. He has an accident one day on his way to the grocery store. Is he insured?

VI. Sandy's Flower/Gift Shop

Sandy runs a small flower/gift shop in her home. She buys most of her raw materials by mail order, and most customers pick up the merchandise at the shop. Occasionally she will deliver the flowers to a church for a wedding or to a hospital for someone ill. Twice a year she drives to Atlanta, Georgia to attend the National Gift Wholesalers show to buy new merchandise. Someone told her that her car should be listed as a business vehicle on her insurance, but she is skeptical. She uses the vehicle much more for personal use than for business use. What types of insurance does she need? Should she be concerned about personal and product liability insurance?

VII. Jim and Lisa's Cleaning Service

Jim and Lisa run a cleaning service. They employ two other people to help them clean. After two years of operation, their business is going very well. Then a consumer sues them for negligence because one of their employees damaged some wallpaper in a hallway through using a harsh cleaner. Jim and Lisa have a business rider on their homeowner's policy. Are they covered? If so, to what extent? Who will pay their legal costs?

VIII. Ruth and Charles's Horse Business

Ruth and Charles moved into a house in the country. There is a barn and about 15 acres of fenced land. They decided to turn this into a business opportunity and board horses. They now board five horses. The horse owners are responsible for feeding and caring for the animals. Ruth and Charles have a "country homeowner's" policy that includes using their property in this manner. One stormy night, one of the horses gets through the fence and onto the nearby road. In the poor visibility, a car hits the horse. Who is liable for the repairs of the car, the medical bills of the horse, the repair of the fence, and any personal negligence?

IX. John's Woodworking Business

John's woodworking business has grown, and he is having trouble finding time to get everything done. He has decided to hire Joe to help him. John will continue to be the only one making the products, but instead of using his time to prepare products for mailing and trips to the post office, Joe will be the one going to the post office and picking up supplies. Joe will use his own van and be reimbursed for expenses by the business. John's business is a sole proprietorship, and since he is the only one making the products, he sees no need to change his insurance coverage. On the way to the post office, Joe is involved in a car accident, damaging several of the packages ready to be shipped, his van, and the other vehicle. What will John's insurance cover? Is he liable for any damage, even though it wasn't his vehicle?

Case studies III through IX developed by Extension Specialists at Virginia Polytechnic Institute & State University.