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PERSPECTIVES

Complexities of Projecting Revenues for Business Income Losses During an Ongoing Pandemic

Our perspectives feature the viewpoints of our subject matter experts on current topics and emerging trends.

INTRODUCTION

This paper is intended as a supplement to the white paper published last year entitled, "The Approaching Storm: Business Income Losses, Catastrophe Claims, and the Post-COVID Economy," where the concept of evaluating business income losses was introduced and wherein it was discussed why these calculations had "become increasingly complicated" due to the ongoing COVID-19 pandemic. At the time of the original publication of that article we had no way of anticipating the continuing impacts the pandemic would have on business income losses that are occurring well into 2021.

COVID-19 IMPACTS INTO 2021

2020 saw significant impacts to nearly every industry's revenue, costs, and, in many cases, viability. It challenged the status quo of relying on historical revenues and trends to project the future. In fact, the future became quite uncertain and unpredictable. By the beginning of 2021, however, many companies had found a new rhythm which, in turn, has restored some of the predictability. Or has it? The answer in many cases is no. In fact, it may have gotten more complex.

Let's dive into some of the key factors that need to be considered and evaluated when projecting future revenues for purposes of business income losses in today's environment.

Governmental Orders

We have hopefully seen our last federally directed, nationwide shutdown arising from the COVID-19 pandemic. However, we are still seeing both federal and local governmental orders that have noteworthy impacts on the businesses both within and outside their jurisdictions that need to be considered when evaluating future revenues for purposes of quantifying business income losses. These orders range in scope significantly. When evaluating business income losses during the ongoing pandemic, it is of utmost importance to gain a full understanding of how the local governmental orders have changed throughout the pandemic and of the impacts of such. These observations from the early days in the pandemic will shed invaluable light and provide bases for which to evaluate future impacts.

As an example, in response to rising cases of COVID-19, on August 12, 2021, the Mayor of New Orleans issued an order requiring proof of vaccination or a negative PCR test for participants in activities with a higher risk of COVID transmission. These activities are defined to include indoor dining/bars, indoor gyms/fitness centers, indoor entertainment, and large outdoor events. The order went into effect on Monday, August 16, 2021.[1] Hurricane Ida then caused widespread damage in the New Orleans area less than two weeks later, on August 29, 2021. When evaluating business income losses within the mandated zone, due consideration will need to be given to any fluctuations observed as a result of this mandate. Did "high risk" businesses see a change in customer behavior after this order was in place? What about similar businesses in neighboring cities? Did they see an increase for clientele that would have otherwise frequented a New Orleans business but decided to go elsewhere to avoid having to comply with the test or vaccination proof mandate? What about businesses that are not considered "high risk" per se but are reliant on such businesses? Were they impacted? All these factors need to be considered when evaluating business income losses of businesses impacted by Hurricane Ida.

Additionally, many businesses are still recovering from previous orders which had impacted them and have subsequently ended. For example, on September 4, 2020, the CDC issued an order halting evictions for non-payment of rent, portions of which are still ongoing today.[2] As a result of this moratorium, countless multi-family residences found themselves with large amounts of outstanding rent payables. Upon the expiration of the order, these properties, for the first time in over a year, have the opportunity to evict these non-paying residents. This could result in significant turnover of tenants but also allow for higher revenues once the eviction and reletting process is completed. How long will the eviction process take? Will local governmental orders extend protections to tenants with remaining unpaid rents? These types of questions will need to be asked regarding claims of this nature.

[1] https://www.nola.gov/mayor/news/august-2021/mayor-cantrell-announces-new-vaccine-requirements-in-response-to-covid-surge/
[2] https://www.cdc.gov/media/releases/2021/s0803-cdc-eviction-order.html

Further, it is important to understand how governmental orders are received both locally and nationwide in terms of public perception to ensure appropriate considerations are made. Will the mask/test mandate in the city of New Orleans impact local tourism? If so, how? Will tourists feel increasingly more comfortable, or will they stray from the area to avoid the increased requirements?

Impacts on Staffing

The United States has offered free COVID-19 vaccines to anyone wishing to obtain them. A sizable percentage of the eligible residents, however, have elected not to receive the vaccine for one reason or another. On September 9, 2021, President Biden announced his six pronged "Path out of the Pandemic" plan. Within the plan is a requirement compelling all employers with 100+ employees to ensure their employees are vaccinated or tested weekly.[3] Though this plan is not yet in place as of the publication date of this article, we have seen several jurisdictions implement similar mandates on a local basis as discussed above. These mandates directly impact the percentage of the population that has intentionally chosen not to get vaccinated and thereby could have a direct impact on staff availability upon implementation. Will these orders encourage more of the population to get vaccinated, or will they drive staff to smaller companies to avoid having to comply? How will any staffing shifts impact business operations and revenues?

Prior Year Considerations

As mentioned above, historically we have relied upon prior year revenue trends to project future revenues. Though historical revenues, specifically those in 2020, may be highly volatile, abnormal, and impacted by a multitude of extraordinary factors, they can still be an important piece when evaluating future revenues. It is imperative when evaluating losses beyond 2020 that we consider not only the current impacts from factors such as those discussed above but also what those impacts looked like in 2020. Furthermore, we also need to consider prior year losses and how those impacts affected revenues. For example, Hurricane Ida impacted areas that were also in the path of Hurricane Laura in 2020. For the unfortunate businesses that found themselves affected by both storms, what can we learn from the Laura losses to help evaluate losses from Ida? Or did a business unaffected by Hurricane Laura's destruction see an increase in revenues due to evacuations of the impacted areas? If reviewed in a vacuum, that increase may appear to be due to seasonality or a large spike in recovery (back to pre-pandemic levels) but, in reality, it is driven by an extraordinary event. These considerations have always been necessary, but they are even more important to recognize when evaluating and projecting revenues in today's world.

Policy Language

As with any business income loss, the forensic accountant will need to work closely with the adjusters and attorneys involved in these claims to engage in conversations regarding whether potential adjustments, such as those discussed herein, are appropriate for the loss at hand. The adjuster/attorney will be able to provide valuable insight into the specific policy language, applicable case law, and whether factors such as those discussed above should or should not be incorporated into the calculation of a specific business income loss.

CONCLUSION

As we have seen throughout the pandemic, different areas of the country have reacted differently to the ever-changing COVID-19 infection and vaccination statistics. When handling a business income loss during a pandemic, it is extremely important to engage a forensic accounting expert who is thorough in their review of the insured's business and also familiar with the local area in which the loss occurred. This will help ensure consideration is appropriately afforded to all aspects which could impact current and future operations.

While there is not a one size fits all solution when it comes to evaluating pandemic revenues, one thing we know for certain is that as forensic accountants we must remain vigilant and flexible in this ever-changing world. Vigilance will enable us to perform an all-encompassing review to thoroughly evaluate the revenues an insured would have earned but for the loss. Flexibility will enable us to react and adapt our methodologies as needed to accommodate the variety of factors which are impacting the insured's business.

[3] https://www.whitehouse.gov/covidplan/

ABOUT THE AUTHOR

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