

## Pandemics – Probable, Prolonged and Perilous: Are the Risks Properly Covered?

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### Introduction

The swell of concerned interest about pandemics continues to build in the business community, particularly in those businesses that have invested a substantial amount of time, money and resources preparing for business interruptions. These are businesses that carefully considered and selected their business interruption coverage to insure the replacement of the property and content impacted, to protect against third-party liability and to cover extra expenses. Many have insured over and above the typical business interruption insurance with coverage for flood, lost revenue and/or collateral damage. However, what if half the workforce was out sick? What if vendors couldn't deliver because their workforces were decimated? The typical business interruption coverage requires damage to insured property or to that of a collateral business. Absent such damage, business interruption coverage in its current form, likely is inapplicable to damages resulting from a pandemic. This likelihood is prompting consideration of whether

business continuity plans protect against the business issues that would result from a pandemic. Insurance companies face these questions on two sides of the equation: as businesses on behalf of their employees, and as insurers on behalf of their insureds. Thus, they have a dual interest in addressing these questions and perhaps considering the expansion of typical business interruption coverage to address such potential risks.

### What is a Pandemic?

President Bush announced a National Strategy for Pandemic Influenza in November 2005. Congress has approved \$251 million to detect and contain outbreaks and for the creation of the International Partnership on Avian and Pandemic Influenza, led by Mike Leavitt, secretary of the U.S. Department of Health and Human Services (HHS). At the time of the preparation of this article, 10 Federal Agencies had formulated strategies, developed plans and prepared checklists for

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pandemics. Still, most business people know little about pandemics, the resulting impact to their business operations, or how to adjust their business continuity plans.

Secretary Leavitt describes a pandemic as a “disease without borders”:

*“Adequate planning for a pandemic requires the involvement of every level of our nation, and indeed, the world. The ubiquitous nature of an influenza pandemic compels federal, state and local governments, communities, corporations, families and individuals to learn about, prepare for, and collaborate in efforts to slow, respond to, mitigate, and recover from a potential pandemic. The development, refinement, and exercise of pandemic influenza plans by all stakeholders are critical components of preparedness.”<sup>1</sup>*

Since a pandemic can occur at any time or any place, it is imperative to understand how a pandemic is determined and how it is different from the influenza that emerges each year.

The World Health Organization (WHO) is the United Nations’ specialized agency for monitoring disease outbreaks and assessing the performance of health organizations around the globe.<sup>2</sup> On March 6, 2006, WHO convened a meeting in Geneva with international world health experts “to discuss a rapid response strategy in the event of an influenza pandemic emerging.”<sup>3</sup> This organization has defined three conditions that must exist in order for a viral outbreak to be identified as a pandemic:

1. The emergence of a disaster new to the population;
2. The virus agent affects humans causing serious illness; and
3. The virus agent spreads easily and is sustainable.

WHO has further defined three periods of progression for a pandemic:

1. Interpandemic:
  - Phase 1 – No new virus detected in humans.
  - Phase 2 – An animal variant threatens humans.
2. Pandemic Alert:
  - Phase 3 – Human infection, no human-to-human spread.
  - Phase 4 – Small clusters of infection, but localized.
  - Phase 5 – Large clusters of infection, but localized.
3. Pandemic:
  - Phase 6 – Increased and sustained transmissions.

In 2004, the Avian Flu made the transition from birds to humans, confirmed by stringent laboratory testing required for confirmation of infection.<sup>4</sup> The Avian Flu has been slowly spreading for two years across Asia and Europe initiating the Pandemic Alert, Phase 3 defined by WHO - “human infection, no human-to-human spread.” As of Feb. 27, 2006, 193 people have contracted Avian Flu and 93 have died.

## What Happened Last Time: SARS and Other Flu Pandemics

Businesses should not be lulled into complacency by the slow progression of the Avian Flu. The next virus that surfaces may proliferate rapidly like the SARS virus of 2003. SARS was first reported in Asia in April 2003. Two months after the first confirmed case, the virus reached the North American Continent. “Over the next few months, the illness spread to more than two dozen countries in North America, South America, Europe and Asia before the SARS global outbreak of 2003 was contained (nine months later).”<sup>5</sup>

If a pandemic occurs, despite the containment efforts of WHO and HHS, it could paralyze normal business operations of companies in cities, counties,

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## Breaking News: “OFC” Proposal Introduced – As the Big Debate Continues....

On April 5, 2006, U.S. Senators Sununu (R-NH) and Johnson (D-SD) introduced the anticipated Optional Federal Charter (OFC) proposal entitled the “National Insurance Act of 2006,” S.2509. The bill allows insurers and producers to choose being regulated by state insurance departments or by an Office of National Insurance (ONI). While there are certain state regulatory carve outs (e.g., workers’ compensation and certain motor vehicle insurance standards), the majority of licensing and oversight functions currently performed in state insurance departments – including enforcement, solvency monitoring, conversions and receiverships – would be potentially transferred to the ONI. State insurance regulators and lawmakers were quick to voice their opposition to the OFC approach, while many insurer and producer trades applauded the bill, and others expressed a more tempered response, perhaps wondering whether it might overshadow or otherwise confound the SMART Act – the less sweeping State Modernization and Regulatory Transparency Act, which is expected to be introduced in the House in coming months.

Of course, most folks close to the issue say that the proposal has no real chance of passage.

Nevertheless, there will be debates. There will be speeches. There will be lobbying. There will be editorial and legal opinions on the good, bad and ugly of federal preemption. There will be spending. So, what’s all the hubbub about? Why push OFC (or SMART) when the proponents do not appear to have any chance of prevailing? One answer (aside from creating speaking or lobbying opportunities) would

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appear to be simple. The debate puts heat on state officials to reexamine their approach to the industry; and with that heat, it logically follows that there will be positive results on the state regulatory side. For example, the debate will almost certainly force continued fast-tracking of the interstate compact implementation and other modernization tools within the state regulatory

system; more coordinated approaches between state regulators on multi-state enforcement and examination issues; more dialogue between regulators and law enforcement personnel; continued improvements in dealing with natural catastrophe issues; and perhaps most importantly, a heightened awareness of national economic issues and where the states fit in. In the end, even proponents of state regulation must admit (even if not in public) that the debate does appear to have a positive side. ■

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and regions that have reached the Pandemic, Phase 6 - “increased and sustained transmissions” level. The most recent pandemic SARS, for example, illustrates the following progression of containment methods: international travel was shut down first, hospital visitors were prohibited next, social events were then cancelled, followed by school closings, leading to building shut downs, and finally people were quarantined in their homes.

The containment methods used in SARS would adversely affect businesses that have not anticipated the ramifications of having their facility shut down and their employees quarantined. They are unprepared. Point-of-sale businesses would suffer from loss of income; unfulfilled contractual obligations from companies that have been closed down would make it impossible for the companies receiving their services or products to continue their business operations; lawsuits would be spawned to recover damages for breach of contracts; and technology-dependent businesses that have not deployed mobile computing and enabled their employees to work from their homes would come to a hard stop.

Beyond the paralyzing effect of mandated shut downs and quarantines, there is a huge potential for loss of life, unrestrained by age, gender or job function. History tells of three perilous pandemics in the United States during which the loss of life was formidable:

1. The Spanish Flu in 1918 to 1919 was unusually virulent and deadly. It killed 500,000 in the United States.<sup>6</sup>
2. The Asian Flu in 1957 to 1958 killed 70,000 in the United States.
3. The Hong Kong Flu in 1968 to 1969 killed 34,000 in the United States.

If Avian Flu outstrips containment, its historic high rate of fatality per infection portends a significantly worse outcome than the two most recent pandemics experienced in the United States.

## How Could It Affect You?

For businesses, employee loss of life or incapacity would create two key issues:

1. Loss of the employee who performs a job function.
2. Loss of the employee’s intellectual property or knowledge of how to perform the job.

The loss could be a key employee, one the business depends upon for a critical function. The business could have overlooked the importance of position succession planning and even fostered the proliferation of a single point of knowledge through its lack of action. The impact of that type of loss would cause inefficiency to the business operations and loss of capital. The loss could also be to a *group* of employees, such as in sales, accounting, or IT, the loss of whom could easily shut down the subject business. Estimates are that 400,000 bird-flu deaths could occur in Europe and 209,000 in the U.S.<sup>7</sup> Insurance companies face these risks, as would any business.

Insurance companies also face financial risks as a result of life, health and disability claims arising out of their insureds’ flu-related losses (as opposed to their employees’). Business interruption insurance will largely not be affected because there shouldn’t be any property damage from a flu pandemic, a usual requirement to trigger such coverage. However, insurance companies may want to explore expanding coverage and underwriting such a risk as a means of generating revenues that could offset future losses. Now is the time, since the business world is only beginning to focus on this very real risk.<sup>8</sup>

## Conclusion

In summary, a prolonged pandemic lasting as much as a year would create an “economic Tsunami” effect globally. The World Bank has estimated that a pandemic lasting a year would cost as much as \$800 billion.<sup>9</sup> Anything that can be done by businesses to lessen that

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impact should be done now. And insurers have an opportunity now to address their business interruption products and determine how and if they can provide coverage in some form for the impending threat of a human flu pandemic. But insurers must proceed with extreme caution; the decision to provide such coverage is only the first step. Insurers must carefully and cautiously underwrite such expanded coverage in order to avoid adverse economic consequences should the pandemic arrive.

<sup>1</sup> Department of Health and Human Services "Pandemic Influenza Plan," November 2005

<sup>2</sup> "About WHO" - [www.who.int](http://www.who.int).

<sup>3</sup> "Media Centre" - [www.who.int](http://www.who.int).

<sup>4</sup> "Countries With Human Cases in the Current Outbreak" - [www.who.int](http://www.who.int).

<sup>5</sup> "Situation Updates" - [www.who.int](http://www.who.int).

<sup>6</sup> "Pandemics" - [www.en.wikipedia.org](http://www.en.wikipedia.org).

<sup>7</sup> *Business Insurance*, March 27, 2006.

<sup>8</sup> According to a new Mercer Human Resources Consulting report, while 70% of businesses surveyed about the possible impact of a flu pandemic believe it will negatively impact their bottom line, only 47% have a business-continuity plan in place. Only 7% of U.S. companies polled have an avian-flu preparedness budget. *Business Insurance*, March 30, 2006.

<sup>9</sup> [www.birdfluindex.com](http://www.birdfluindex.com).

*This article was co-authored by Stradley Ronon Stevens and Young, LLP and IDC Partners. Founded in 1991, IDC Partners is a business-continuity consulting firm serving clients nationally and internationally with a focus on regulated industries. The company specializes in reducing risk and improving business process management from a people, process and technology perspective. Practice areas include business-continuity planning, business process excellence, and information technology management and direction. For more information, visit their Web site at [www.idc-partners.com](http://www.idc-partners.com). ■*

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