Advanced Accountancy – I

B.COM.III

INSURANCE CLAIM

(Loss of Profit Policy)

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Introduction :-

When a fire occurs, the business is dislocated for a certain period of time and the normal business cannot be achieved. During this period of dislocation, the sales are comparatively less than what they are supposed to be under normal working conditions. When sales are reduced, the corresponding profits are also reduced. Consequential loss insurance indemnifies the insured any loss of profit suffered by him, consequent on the destruction of business by fire. An ordinary fire insurance policy does not cover loss of profit due to reduction in sales on account of fire. So a separate policy known as consequential loss policy is taken to cover the following losses due to fire.

1. Loss of profit due to reduction in turnover / output.
2. Payment of standing charges.
3. Increased cost of working (which is necessary to avoid or diminish reduced turnover)

IMPORTANT POINTS FOR CALCULATION OF CLAIM

1. Period of Indemnity :

Indemnity period means the period which commences on the date of damage by fire and ends on the date when normality is restored. The indemnity period is generally stipulated in the insurance policy. This period is selected by the insured himself.

The policy is taken generally for a period of one year and can be renewed annually, whereas the indemnity period commences on the day on which the accident takes place and runs up to a period of twelve or more months. It is necessary that the policy must be in force at the time of fire accident.

* The period of dislocation or indemnity period, which ever is less, is considered

2. Short Sales

The term "Short Sales" refers to the loss of sales due to the dislocation of business. That is, short sale is the difference between standard turnover and actual turnover during the period of fire.

Short Sales = Expected Sales – Actual Sales

3. Percentages

I) Gross Profit Ratio

$$= \frac{\text{Net Profit} + \text{Insured Standing Charges (Last Trading Year)}}{\text{Sales of Last Trading Year}} \times 100$$

I) Indemnity Ratio

$$= \frac{\text{Sum Insured}}{\text{Standard Sale (Sales of Current Trading Year)}} \times 100$$

4. Claim

= Short Sales × Lower of the above two percentage
(i.e. G/P Ratio & Indemnity Ratio)

Any Question

Thank You