



Are Your Franchisees Prepared for a Disaster?

Lately it seems that every time we turn on the tv or log onto social media, we are greeted with news of another disaster. From the hurricanes that recently pounded the southeastern United States and Puerto Rico to the wildfires currently raging in California, we are reminded again and again that disaster could strike at any moment. What measures should a franchised business take to prepare? In this Alert, we focus on one important aspect of a disaster readiness plan—insurance. Specifically, we discuss three critical steps a franchisor should take to verify that its franchisees have proper insurance in place before disaster strikes.

(1) Review types of insurance required or recommended system-wide.

Franchisors of start-up and mature franchise systems alike should regularly revisit the types of insurance required and/or recommended for franchisees. This is important as prudent types and amounts of coverage change over time. For example, many franchisors now require that franchisees obtain cybersecurity insurance, something that was not on most franchisors' radar 20 years ago. Considering many franchisees are small business owners that may own only one or a few franchised locations, will they be able to survive the loss of revenue during the shutdown and rebuilding period following a disaster? Many may not. For this reason, franchisors should consider requiring, or at least recommending, that franchisees obtain business interruption insurance in addition to property coverage.

(2) Consider endorsements based on location.

Though insurance requirements are typically uniformly imposed on all franchisees in a franchise system, franchisors should consider whether it is necessary or advisable to require franchisees to obtain specific endorsements based on their particular location. A standard insurance policy may not cover damage caused by a hurricane or flooding, so a separate endorsement or deductible may be required. For insurance policies to cover damage caused by these disasters, there likely needs to be very specific language within

the policy to ensure the damages are not exceptions to the coverage provided. While franchisees located in Gulf Coast states should be concerned with named storm insurance coverage, that is not a concern for franchisees located in the Midwestern states, who instead are more at risk for windstorm damage from tornados. For this reason, franchisors should consider making recommendations, or imposing requirements, that are location specific in addition to the uniformly imposed system-wide insurance requirements. This might include recommending that franchisees with the greatest risk for flood, wind, or earthquake damage obtain insurance through government supported programs to the extent possible.

(3) Collect certificates of insurance now.

Including a provision in the franchise agreement that requires each franchisee to provide certificates of insurance demonstrating that it has the requisite insurance and that the franchisor (or other designated parties) is included as additional named insured is only the first step. It is extremely important that franchisors enforce that provision by collecting copies of the certificate of insurance both before the franchisee commences operation of the franchised business and regularly during the term of the franchise agreement. Now is the time to make sure you are enforcing this provision for all of your franchisees, not after a disaster strikes. If you don't have the human resources to follow up on obtaining evidence of insurance coverage, consider engaging a third-party to do so.

Insurance aside, a franchisee suffering the loss of its business, or severe damage to its business, as a result of disaster is certainly a sensitive matter that needs to be handled tactfully. Decide now who is responsible for reaching out to franchisees after a disaster and how best to handle any loss. What support will you offer your franchisees to help them get back on their feet and reopen their franchised business? Let them know that you are there to assist in their time of need.

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