PERSPECTIVES

Event Cancellation Insurance: Calculating Ascertained Net Loss in Practice

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

INTRODUCTION

"An event cancelled is better than a life cancelled," according to World Health Organization Director-General Tedros Adhanom Ghebreyesus when speaking in December 2021 in response to the spread of the COVID-19 Omicron variant. The COVID-19 pandemic gave rise to a significant increase in events being cancelled, which in turn led to an unprecedented level of event cancellation insurance claims.

This paper will discuss the purpose of event cancellation insurance, how such losses can be calculated, and some common issues encountered when quantifying such claims.

WHY HAVE EVENT CANCELLATION INSURANCE?

Events mainly consist of a significant amount of upfront costs such as paying for talent, designing the event space, choosing the venue, hiring staff to organize and run the event, and advertising. The revenue is built up gradually during the lead up to the event, based on sponsorships and ticket sales. Consequently, the Event Organizer has significant risks due to how the event's working capital cycle occurs.

For example, if a ticketed music event is cancelled the day before the event, due to severe weather, the vast majority of the expenses would have been incurred (such as the venue hire, stage costs, artist fees, security, etc.). Additionally, it would be likely that most of the tickets would have been sold for the event, and hence the Event Organizer most likely will have to fully refund all the tickets (subject to the terms and conditions of the tickets). Accordingly, the Event Organizer will have incurred all the expenses without generating any revenue (no retained revenue).

EVENT CANCELLATION INSURANCE

Event Cancellation Insurance can protect an event's (or a series of events') revenue and expenses against the risk of cancellation, postponement, curtailment, relocation, rescheduling or abandonment of the event for reasons beyond the control of the Event Organizer (the policy holder). This can protect the event against perils such as:

- Civil Commotion
- Communicable Disease (although since outbreaks such as Covid-19, this may not be included in the standard cover)
- Key Talent (non-attendance / illness)
- Labor Strikes
- National Mourning
- Severe Weather Conditions
- Terrorism
- Venue Unavailability

ASCERTAINED NET LOSS

Once triggered, the response set out in the insurance policy is often based on an Ascertained Net Loss wording. This may cover, for example:

- Expenses which have been irrevocably expended in connection with the insured event, less any savings the Event Organizer is able to effect to mitigate the loss,
- The reduction in Profit (when stated in the Policy Schedule) which the Event Organizer can satisfactorily prove would have been earned had the insured event taken place,
- Less such part of the Gross Revenue received or receivable.

In practice, this generally includes the expenses that the Event Organizer has already incurred (or is contractually obligated for) that they are unable to mitigate, plus the Net Profit that the Event Organizer would have generated if there was no loss, less any revenue that the Event Organizer can retain, such as ticket cancellation fees or sponsorship revenue already earned.

In the ticketed music event example above, this is likely to cover all the expenses incurred, plus the profit that would have been made if the event had run as planned (i.e., absent of the severe weather). This would be calculated as the ticket revenue less the total expenses. If all the ticket revenue was refunded there would be no retained revenue to deduct from the Ascertained Net Loss calculation.

Issues that can make the quantification of Ascertained Net Loss claims more challenging include the following:

- For events that are not intended to be profit making, coverage is likely to exclude the profit element, and only include the costs that have been incurred.
- Some policy holders may elect to only partially insure the costs associated with an event, which may have been overlooked when the claim was being prepared.
- Revenue may be retained by the Event Organizer for future events, in which case if it can be demonstrated that this is a contractual obligation, the associated revenue is unlikely to be treated as retained revenue.
- Event Expenses could be mitigated, or rolled over to future events, and therefore although the expense is incurred, it is not incurred for the covered event.
- Under-insurance: the actual event may be in excess of the declared value of coverage for the event and therefore the loss may be limited to the value declared.

CONCLUSION

Every claim is unique, requiring careful analysis and review of the supporting evidence, which is where a forensic accountant can aid in all aspects of validating Ascertained Net Loss claims. This is particularly true when verifying the expected net profit, assessing the actual expenses irrevocably expended, or determining whether the Event Organizer has been able to mitigate their loss by retained revenue or reducing expenditure.

ACKNOWLEDGMENTS

We would like to thank Giles Archer for providing insight and expertise that greatly assisted this research.

Giles Archer is a Vice President in J.S. Held's Forensic Accounting Practice in London. For the last 10 years he has specialized in preparing economic damage calculations: including business interruption and event cancellation / contingency losses, extra expenses, political risk, and stock losses. He has quantified losses across the world in various industries, such as, automobile, construction, financial services, food, hospitality and tourism, manufacturing, mining and refining, power generation, retail, sports, and the entertainment industry.

Contact Giles Archer at giles.archer@jsheld.com or +44 20 4576 0624.