Keeping Fluctuating Inventory Values Properly Insured

By William F. Johnson Jr.

So far this year, we've seen lumber prices soar to near record levels only to come back down. While the price was up, lumber suppliers likely noticed a higher price when purchasing inventory. What they may not have noticed, however, is that while they held the higher-priced inventory, they may not have been insured adequately to its elevated value had disaster struck.

Insuring to value, as it is commonly called, is critical to ensure goods or property have the proper amount of insurance coverage; unfortunately, too often lumber and building material suppliers do not have the coverage they need due to fluctuating inventory values. It is recommended that building and material suppliers insure their inventories for at least 80% of their value.

According to Nasdaq, lumber prices began to rise steadily in December of last year from about $380 to a high point of $620 reached in May. Since then, prices have steadily fallen and are now hovering around $430. If a lumber supplier bought a new shipment of lumber in June, he or she would have paid a premium for it. If he or she did not report that new inventory and its cost to his or her insurance company and the facility caught on fire, the lumber supplier would not be covered for the new inventory at its current higher value. This is something insurers see all too often with business owners unable to rebuild their businesses after a tragic loss because they weren't adequately insured.

A rise in lumber prices is just one reason for lumber and building material suppliers to keep their insurance companies apprised of any changes, particularly of changes pertaining to inventory. Inventory values can fluctuate due to seasonal inventory buys or major storm events among other things. For example, lumber and building material dealers may stock up on mulch, rock, and fertilizer in the spring and summer months while their inventory values decrease sharply during the quieter winter months. Last year, after hurricanes Harvey and Irma, many suppliers in the Carolinas moved their inventories to assist in the storm zones, which affected their inventory values.

To keep up with these changing inventories, a good insurance partner will offer a stock reporting form. These forms allow business owners to pay for insurance coverage for only the inventory amounts the business has on hand. A reporting form is designed to allow the policyholder to report inventory and its values in detail on a monthly basis to protect the company from lows and highs in its inventory values. The forms instruct the policyholder to list furniture, machinery, and other equipment, as well as the value of its stock and improvements. Though this may sound time consuming, consider that most inventory lists are already automated and should be fairly easy to transfer to the stock reporting form.

The stock reporting form is helpful to carriers to understand the insureds' actual premium exposure and beneficial to policyholders who, with the form, will pay for only coverage that they need.

For many, the stock reporting forms result in lower premiums. For example, if a business owner has $12 million in coverage on his inventory, without completing a stock reporting form, at a rate of $.40 he or she would pay $48,000 in annual premium. If that same business owner used a stock reporting form for $12 million in coverage and the actual monthly inventory values only averaged $10,800,000, at that same rate of $.40, that business owner would only pay $43,200 in premium, recognizing a savings of $4,800.

Alternatively, policyholders who know their inventory levels follow a regular schedule might benefit from a peak season endorsement. With a peak season endorsement, a policyholder can increase his or her coverage for peak inventory months. For example, the business owner could increase his or her coverage from a $12 million limit to $15 million during the spring months. Again, this allows the policyholders to only pay for the coverage they use, while the insurance company has the benefit of knowing the policyholder's actual inventory values.

Although some business owners' inventories may be largely cyclical or follow a historical pattern, that can all change with a major storm or surge in lumber prices as we recently experienced. To avoid getting caught without enough coverage, lumber and building material suppliers should stay in regular contact with their insurers, and use a stock reporting form or peak endorsement where possible. These tools allow insurance companies to make their policyholders whole again in the event of an accident. A good insurer who knows the wood niche can be invaluable in helping building and material suppliers protect their inventories, their businesses, and their futures. LC

William F. Johnson Jr. serves as vice president of underwriting for PLM. In this position, he is responsible for the development of underwriting strategy, policy, and procedures, as well as for managing the underwriting quality and profitability of the commercial lines business for PLM. He is a member of the Pennsylvania Association of Mutual Insurance Companies (PAMIC), and previously served on the education committee for the National Association of Mutual Insurance Companies (NAMIC).