

# The Fragility of Supply Chains

## Examining the Risks and Continuity Planning



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When it comes to property, insuring tangible assets, such as buildings and equipment, is often the principal concern. But in fact, not properly insuring against a loss to your revenue stream could be catastrophic to the financial well being of a company. Having a keen understanding of business interruption exposures facing an overall operation, along with the availability of insurance coverage is essential.

### **Business Income Interruption**

The goal of Business Income Interruption Insurance (commonly referred to as “BII” or BI”) is to provide a business with protection from an interrupted revenue stream (arising out of a property loss), and thus protection from lost profits. Losses to inventory, manufacturing processes, and/or supply chain elements can all lead to lost profits.

A disruption along a supply chain can come from many sources. There are external exposures, such as a natural disaster or a terrorist attack. There are also numerous operational risks. Consider the latest trend of driving costs down by keeping inventories lean, often leaving little room for error; or using a single source for raw materials in order to simplify logistics; or the overall global emphasis on outsourcing various processes. An interruption to any of these stops along the supply chain could trigger a significant disruption. Understanding all the dependencies of a supply chain with a close examination of all the potential risks is the first step in the risk analysis process.

### **Contingent Business Interruption**

No company operates alone, it takes suppliers and customers. Have you ever considered how much of your business relies on an outside entity? Or what the impact would be if you lost a key supplier? With contingent coverage, you can insure against an income loss from your company’s dependence upon others. Coverage is available to indemnify the insured for an upstream (supply) and a downstream (customer) loss that affects the company’s revenues and profitability. A close examination of all outside risks is crucial for this option.

The fundamental elements of determining a Contingent Business Interruption (CBI) exposure are to identify all of the potential areas of loss along the supply chain, including the financial impact that a loss at another business’ location would have on your company’s operations; have a continuity plan in place (a plan B or multiple material sources); and incorporate the correct policy wording and limits for each of the supplier locations. CBI insurance helps bridge the gap between losses at a supplier while returning your revenue stream to the point it was pre-interruption.

William Gallagher Associates, a leading provider of insurance brokerage, risk management and employee benefits services to firms with complex risks, within industries that include high technology, life sciences, financial risks, healthcare services, energy, and environmental services. WGA has offices in Boston, MA; Princeton, NJ; Columbia, MD; Atlanta, GA; and Paris France.

Some BI risks areas are completely insurable at a reasonable cost, but there are other BI risks that only allow for limited coverage and are relatively expensive. And of course, there are those risks that are simply uninsurable. Some examples of each of these BI risks are:

<b>Risk</b>	<b>Coverage</b>
A fire at single-source supplier	Insurable
Transport crash while delivering materials	Insurable
An earthquake at a specialized parts plant in Asia	Insurance available, but expensive and limited
Labor strike	Insurance available, but expensive and limited
Typhoon devastates an overseas port	Insurance (Trade Disruption Insurance) available, but expensive and limited
Political unrest or action by a government that may deprive a company of its assets, prevent or restrict a contract, or affect repayment of loans to financing banks and lenders.	Insurance available (Political Risk Insurance), but expensive and limited
Avian flu	Not easily insurable
Animal rights protest	Not easily insurable

Even the best laid plan will encounter situations that cannot be avoided. Consider the recent terrorist bombing in India, a global outsourcing hub, or that this year's typhoon and hurricane season is expected to be the worst we have seen. Now more than ever, organizations cannot underestimate the importance of business continuity planning. Companies need to insulate themselves from the consequences by spreading their risks more widely; planning for multiple material sources; managing inventory; and most importantly acknowledging vulnerabilities and proactively planning for contingencies. Protection against supply chain disruptions is an important component to operational harmony and ultimately stronger financial health.

