



## **Industry Specialist Training: Manufacturing**

Topic 3

# **Business Interruption issues and implications**

## **Part 2**

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in partnership with **AXA Commercial**



# Introduction

- **Nick Thomas & Associates** in partnership with **AXA Commercial**
- Delivering practical technical training support to AXA Broker partners
- Today is the third topic of four in our focus on 'Manufacturing' sector
  - » Topic 1 – Property insurance issues and implications
  - » Topic 2 – Business interruption issues and implications [Part 1]
  - » **Topic 3 – Business interruption issues and implications [Part 2]**
  - » Topic 4 – Liability and Motor insurance issues and implications
- After each topic you can test your knowledge with a short quiz



# Agenda - Manufacturing

## Topic 3 – Business interruption insurance for manufacturers – Part 2

- Assessing an indemnity period
- Increased Cost of Working [ICOW] and Additional Increased Cost of Working [AICOW]
- Identifying key extensions and what issues to consider for each extension





## Assessing the Indemnity Period [IP]

- Absolute time limit on how long the policy can respond
- Starts running at occurrence of Damage, ends at end of effect on business or chosen period – whichever shorter
- Need to identify what is the correct IP – too short IPs reduce payments to client
- The client may want something shorter – for economy or business case reasons
- 12 months ‘standard’ – for serious loss it is unlikely to be sufficient
- Need to increase sum insured as IP increases





## Assessing the Indemnity Period

- Competence of management team
- Decision-making process
- Thinking/decision time
- Business continuity plans - tested
- Neighbouring locations/businesses
- Planning consents/enquiries
- Unions – agreement to overtime
- Shortage of construction workers
- Brexit delays – materials and workers





## Assessing the Indemnity Period

- Rented premises tenants have no control over rebuilding
- Environmental issues e.g. asbestos
- Lead time for replacement machinery
  - » are there any key machines that need to be made to order/have special requirements?
  - » foundations
  - » testing and re-commissioning
  - » relative size of client to machinery supplier
  - » availability of second-hand machinery
  - » location of machinery supplier – air, road or sea delivery
  - » Brexit delays







## Assessing the Indemnity Period

- Seasonality
- Raw material
  - » just in time – no buffer stock
  - » Brexit delays
- Re-training staff
- Re-gaining the anticipated level of custom/trade
  - » customer loyalty
  - » finding new customers
  - » procurement hoops
  - » long term contracts





## Increased Cost of Working [ICOW]

- Covered within Insurable Gross Profit item
  - » The additional expenditure **necessarily and reasonably incurred** for the **sole** purpose of avoiding or diminishing the reduction in turnover
- Subject to 'economic limit'
- Expenditure incurred £50,000
  - » loss avoided £200,000. Policy pays £50,000
- Expenditure incurred £100,000
  - » loss avoided £30,000. Policy pays only £30,000
- Benefit of expenditure must be within indemnity period







## Additional Increased Cost of Working [AICOW]

- No economic limit BUT still must be “reasonably and necessarily incurred”
- Benefits need to be within indemnity period of AICOW
- Loss adjusters like it – they can authorise expense and worry about “economic” later
- Important for any “just in time” business
- Some businesses may need a longer indemnity period for AICOW – costs could continue after resumption of activities (should never be shorter than GP indemnity period)





## Extensions

- Amend definition of Premises/Property to add additional locations (still has to be Damage)
- Note - territorial limits of policy apply to all extensions, unless amended in extension
- Loss of Insurable Gross Profit at insured due to damage at:
  - » suppliers
  - » customers
  - » third party premises
  - » prevention of access
  - » utilities





## Extensions

- Amend definition of Damage (but not Premises/Property)
- Loss of Insurable Gross Profit due to
  - » failure of supply/terminal ends
  - » non-damage denial of access
  - » contractual fines and damages
  - » murder, suicide and human (notifiable) disease
  - » engineering breakdown (may be separate policy)
- Change basis of settlement
  - » research & development expenditure
- Some are 'hybrid clauses' – do more than one thing – often in bespoke wording!







# Suppliers

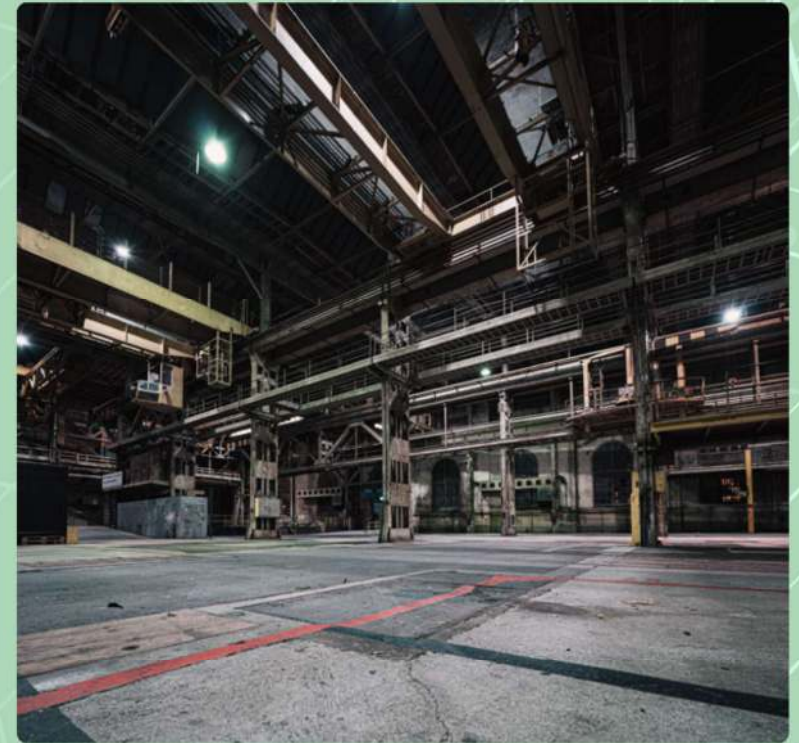
- Any supplier could be a worse risk than the client
  - » unnamed suppliers – overall limit or low limit any one supplier
  - » named suppliers – specific limit
  - » overseas suppliers – need to be specified and territorial limits amended, often reduced perils covered
- Client may have a dependency on a raw material supplied – identify these (may not be main raw material)
- The supplier may take longer to recover from damage than the client
- Need accurate information to assess the correct cover and indemnity period – can be difficult to obtain





## Customers

- Adds premises of named or unnamed customer
- Sole customer dependence and customer has limited premises
- Very easy to identify, but...
- Ensure the actual dependent premises is listed - not the sales office but the production site
- Consider if IP enough (often shorter than main IP)
- Consider limit
- Underwriting information may be difficult for a small supplier to a major customer to obtain





## Third party premises

- Adds premises owned by third parties but used by insured to generate turnover
- Also called contract sites extension
- Outworkers or outsourced operations – ask what, where, when, consider:
  - » specialist treatment - common in many industries
  - » contract sites
  - » patterns, moulds
- Check IP







## Prevention of access (POA)

- Adds property in vicinity of insured's premises to definition of insured property
- Property in vicinity still needs to be Damaged, cover is for loss of turnover due to resulting hindrance e.g.
  - » drifting smoke from nearby fire making it impossible to work in the premises (food manufacturing)
- What is located in the vicinity of the premises?
- Vicinity is often defined – perhaps a mile radius. Is this enough?
- Check IP





# Utilities

- Adds premises of utility providers - electricity, gas, water, steam, communications
- Has to be Damage as insured by MD
- Check if ISPs used (some insurers cover these as utilities, some as suppliers)
- Assess risk / need for cover
  - » resilience / outages
  - » mitigation – e.g. back-up / temporary generators
- Loss limits required
- May be waiting / franchise period
- IP usually short – check it is sufficient





## Failure to supply/terminal ends

- Adds failure to receive utility supply as insured peril (contingency) excluding
  - » deliberate withdrawal of services
  - » failure caused by strikes etc
  - » satellite failure
  - » caused by drought or weather conditions (damage caused by weather is covered)
- At terminal ends / point where service enters insureds premises / meters / stopcock
- Must have for manufacturing dependent on continuing power (e.g. furnaces), water etc
- Own IP
- Always a waiting / franchise period
- Usually not satellite failures – but may be possible for larger risks





## Non-damage POA

- Access prevented/hindered but no Damage
- Many different versions of the wordings (one of reasons for FCA court case) e.g.
  - » closure due to terrorist threat – no damage
  - » closure due to enforcement action of local authority





## Fines and Damages

- Contractual penalties not covered under ICOW as paid because of contract, not to avoid a reduction in turnover
- Non-contractual penalties – may be paid if economic (often they are not) – insurers may resist
- AICOW – non-economic non-contractual payments if reasonably and necessarily incurred and benefit within IP
- Cover is for fines or damages for breach of contract caused by Damage at the insured's premises
- Should cover both:
  - » losses incurred in not fulfilling contracts outwards
  - » losses incurred by breach of contract through not being able to accept goods or services inwards
- Check if any contracts with such conditions – watch force majeure wordings



## Murder, suicide, disease

- Human notifiable disease as listed only (especially after FCA test case)
- Will probably be limited to outbreak at own premises in future
- Should be extended to cover closure under food safety legislation – necessary for food manufacturers
- Check IP – especially if seasonal







# Engineering breakdown

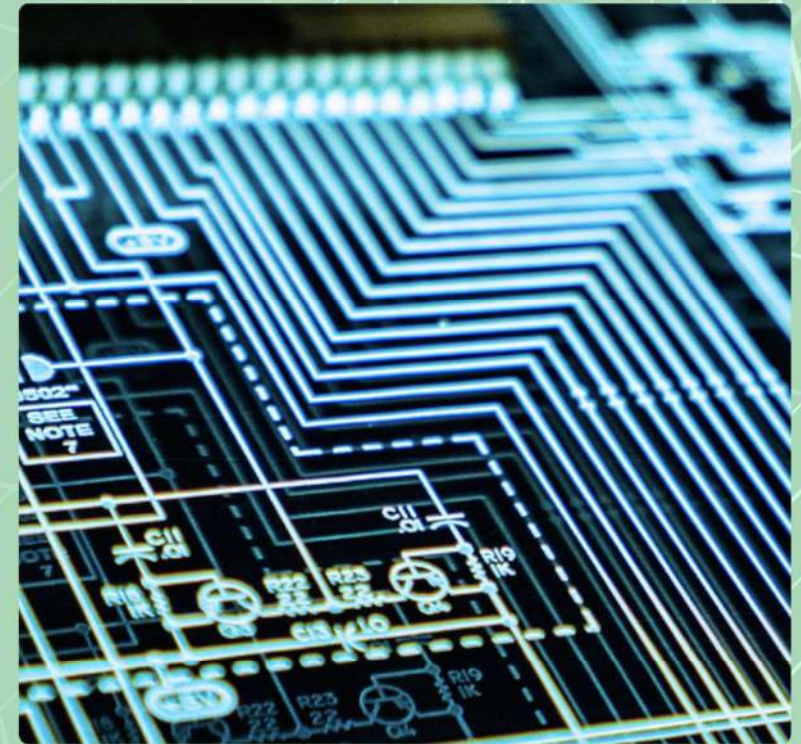
- Engineering perils e.g.
  - » breakdown of key machine
  - » explosion or collapse of production steam boiler/ equipment
  - » operational error causing damage to machinery
  - » deterioration in stock by freezer breakdown
- Identify bottlenecks in production/key machines
- IP needs to be sufficient to include obtaining replacement machine, testing, commissioning, re-training
- Discuss need with client – can often identify key areas not considered





## Research and Development [R&D]

- Most major clients maintain R&D unit
- They develop new products / new ways of making existing products
  - » common but not always called R&D e.g. recipe development team for food manufacturing
- If the unit is destroyed, all the work has to be re-written/re-done
- Not covered in standard policy– no reduction in turnover within IP
- Need to add a separate first loss item





## Summary and what next?

- Sum up
- This module also includes a short quiz so you can test your knowledge on Business Interruption issues
- Next session in our focus on 'Manufacturing' section:  
**'Liability and Motor insurance issues and implications'**
- Thank you





# Thank you

Industry Specialist Training: Manufacturing –  
Topic 3: Business Interruption (Part 2)