The Hanover Insurance Group®

Commercial Lines

Your guide to business income risk assessments for manufacturers

Every business has the risk of being interrupted and potentially shut down. That's why business income (BI) coverage is a key component of every business insurance program. It's a common coverage, but manufactures have unique circumstances that can impact business income. These can have a varied impact on operations, which can leave businesses underinsured if not reviewed regularly.

A business impact risk assessment (BIRA) is a worksheet that helps identify the critical operations that can have an impact on a manufacturer's production and helps to estimate how long it could take to return to full operational capability following a loss. Reviewing and updating a BIRA is a good starting point for both you and your client to better understand where their current business income risks are and adjust coverage accordingly.

Six questions to ask manufacturing clients to get you started

1. Is there a business continuity plan?

Companies with well-conceived business continuity plans in place will most likely recover more quickly from a loss.

2. How much of the business income is seasonal? Or comes from a key customer?

Some businesses have higher levels of production, sales and income during peak (3-month) seasons while others have key customers accounting for a majority of their sales volume. This can have a more drastic impact when they face a business income loss.

3. What are the repercussions if a critical piece of equipment goes down?

A manufacturer should have continuity alternatives (e.g. spare parts, temporary equipment rental, surplus inventory) in the event that a the loss of critical equipment disrupts throughput for an extended period of time. Alternatives should be addressed in a business continuity plan, and the extra expenses captured on the BIRA worksheet.

4. How long would it take to fully recover critical operations if 80% or more of the facility or equipment were damaged?

There are no standard rules for determining this duration, but keep in mind that in the event of a large natural catastrophe, limitations on labor, materials and infrastructure can slow the recovery process. Zoning changes enacted since the original facility was constructed could slow or derail plans to rebuild. Long equipment lead times should be considered as well.

On the other hand, some factors can accelerate recovery. Companies with well-conceived business continuity plans in place, for example, most likely will recover more quickly from a loss.

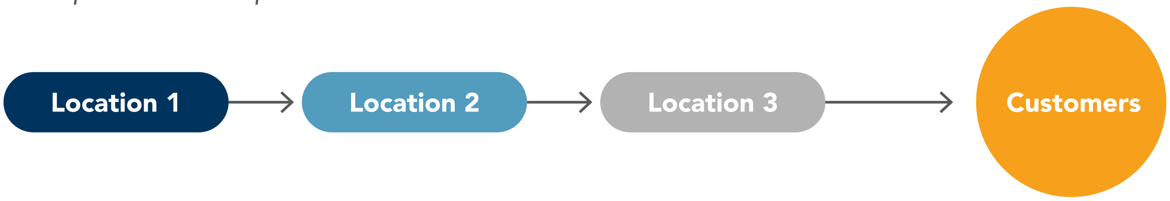
5. Would there be production challenges in the event of a relocation?

If a manufacturer can continue to operate at an alternative location while the permanent location is rebuilt, the impact of the loss event can be significantly reduced. However, some building features may impede the manufacturer's ability to relocate operations.

6. For businesses with multiple locations: how much would damage to one facility impact overall operations?

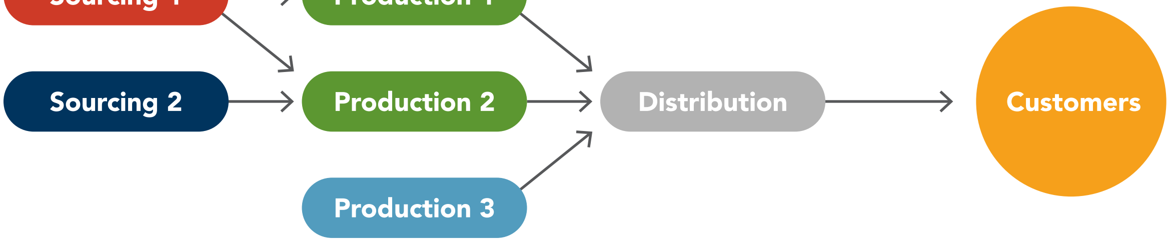
When working with multiple locations, all of the location limits, when totaled, should equal 100% of a manufacturers BI limit. However, where location interdependencies exist, the allocated limit for a single location may not reflect the total BI exposure. Consider these two examples:

Example 1—linear production



Here, all three locations are needed for production. From a BI exposure standpoint, each individual location may only represent 33% of the total BI exposure. However, the entire company's BI limit could potentially be exposed if any of these locations were to go down.

Example 2—interdependent production



In this example, the interdependency of an event occurring at an upstream sourcing location (red) can have a significant impact at the production facilities downstream (green) potentially impacting 66% of the company's throughput.

***Note:** Both of these examples could also apply to critical equipment within a manufacturing facility.*

Business income risk assessment—six initial questions to ask your clients

QUESTION	LOW IMPACT	MODERATE IMPACT	HIGH IMPACT	ADDITIONAL CONSIDERATIONS
Do you have a written business continuity plan?	Yes, developed to an industry standard	Written plan in place or in development	No plan, or no evidence of a plan in use	Review The Hanover's business income resource page for more information and guidance on business continuity planning.
Does the operation have a peak season? Or does it derive a significant amount of income from a key customer?	Less than 30% of annual output is generated through one customer or in a period of 3 months	30%–40% of annual output is generated through one customer or in a period of 3 months or less	40% or more of annual output is generated through one customer or in a period of 3 months or less	Peak season and key customer exposures will vary depending on manufacturer making it important production and sales exposures be documented.
What are the repercussions if a critical piece of equipment goes down?	Less than 25% impact to throughput Lead/restoration time less than 2 months	Less than 50% impact Lead/restoration time 2–4 months	50% or higher impact Lead/restoration time more than 4 months	Additional considerations should be made for: • Custom-made or nonstandard equipment • Highly complex or patented equipment with long lead or installation time • Impacts of foreign manufacture • Age/obsolescence of equipment
How long would it take to fully recover critical operations if 80% or more of your facility or equipment were damaged?	Less than 12 months	12 to 15 months	More than 15 months	Things to consider: • Natural catastrophe which limits necessities such as labor and/or materials • Zoning changes since original facility was built • Long equipment lead times
Are there any unique location, building or process features that would prevent relocating operations to another facility?	Viability established in the business continuity plan	No identified challenges	Significant challenges	Additional considerations should be made for: • Complexity of build, including any special structures • Availability of construction materials • Special location requirements and/or special permissions • Jurisdictional delays around permits and approvals • Proximity critical suppliers, customers or utilities
For businesses with multiple locations: how much would severe damage to one facility impact your overall operations?	Less than 20% of overall production	Less than 40% of overall production	40% or more of overall production	When dealing with multiple locations, all of the location limits, when totaled, should equal 100% of a manufacturer's BI limit.

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