# The supply chain challenge

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**Last year's petrol crisis in the UK together with multiple media reports of looming shortages has focused the attention of companies on the robustness of their supply chain and how to safeguard this faced with a prolonged period of potential disruption resulting from COVID-19 and Brexit.**

Traditionally, companies have been able to use both supplier's extension and customer's extension policies to safeguard both their upstream and downstream supply chains. However, the disadvantage of this type of insurance is that it is triggered by physical damage, typically those types of physical damage specified in the property damage BI policy of an insured. Furthermore, it is often only the immediate supplier who is specified which, in an age of ever lengthening and more complex supply chains, is of limited use.

As the current supply chain issues in both the UK and Europe are caused by factors other than physical damage, this type of traditional supply chain insurance would not respond to any resultant business interruption loss. Instead, Insurers have been offering bespoke supply chain insurance policies whereby no physical damage is required to trigger the policy. So far so good but due to the multiple possible causes of supply chain issues, both the insurer and the insured will need to satisfy themselves that the policy wording is totally clear on coverage to avoid lengthy and potentially costly disputes in the event of any claim by the Insured.


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Let's look at some examples arising from current issues in the UK; the recent petrol shortages were caused not by any physical damage or shortage of petrol at refineries but by a shortage of HGV drivers. It is unlikely that there were large numbers of petrol stations which suffered a loss as when they did have petrol, daily sales were sometimes as high as 400% of normal sales compensating them for periods when they were forced to close because of running out of fuel. However, some petrol stations may have suffered a loss due to multiple deliveries being missed. If such stations had supply chain insurance, this would need to specify logistical or transportation problems as an insured risk – merely specifying supplying refineries may not be sufficient to ensure coverage.

Another current situation is where pig farmers were forced to slaughter animals on site as there was no capacity at abattoirs due to a shortage of butchers. The farmers suffered a significant reduction in sales revenue as the meat from the slaughtered animals could only be used for pet food – not human consumption – as slaughter had taken place outside of a licensed abattoir. Once again, a normal supplier extension policy would not provide coverage as the abattoir had not suffered any physical damage. The farmer would need a more general supply chain insurance which would need to specify shortage of labour at a supplier and would also need to specify individual abattoirs as suppliers of services.

At the end of last year, there were reports of the container port at Felixstowe turning away container ships as they were operating at capacity and did not have space to take on additional containers. The problem was apparently caused by a shortage of HGV drivers to move the containers, restrictions at ports because of COVID-19 and a surge in imports. Once again, there was no physical damage suffered to trigger a supplier's extension policy but even if that was the case, it is questionable as to whether the port at Felixstowe would be a specified supplier. As a result of the situation at Felixstowe, it is likely that hundreds of wholesalers and their retailer customers suffered a decline in revenue in the run-up to Christmas due to the non-availability of products. Policies will only respond to such losses if there is a specific reference to container port capacity problems therein – general terms relating to transportation problems may not be sufficiently watertight to avoid months of arguments over coverage.

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**The lessons for Insureds are relatively clear. They need to take whatever steps they can, both in a business and insurance context, to minimise the risk of supply problems. These include but are not limited to:**

Using multiple suppliers where possible to spread the risk of supplier problems.

Increasing inventory levels (but remembering to check that increased levels do not breach coverage limits) to have a large “buffer” stock.

For suppliers and customers extension policies, specify not just the immediate supplier / customer but multi-level suppliers and customers.

Increasing customer base to minimise the risk to the business of one customer being unable to accept products / fulfil contract.

Considering employing own drivers and having own transportation fleet to minimise reliance on third party transporters.

For general supply chain policies, specify as many potential problems as possible and ensure that “invisible” elements of supply chain (e.g., hauliers, ports, specialist labour etc.) are considered and that potential problems with these are also covered.

It seems certain that in an age where sophisticated and complex computer programmes have increased reliance on “just in time” stock solutions, supply chain issues will continue to cause significant problems even before factoring in the potential complications of Brexit and COVID-19. Companies will need to take whatever steps they can to reduce and ultimately insure against supply chain risks whereas Insurers must provide total clarity as to coverage in their supply chain policies and produce Policies fit for purpose.

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