Preemptive Disaster Planning

Allen Melton and Jason Trahan

How would your company respond if your manufacturing plant were flooded? Or hit by a tornado? Or damaged by fire? Your likely response would be to discuss your company's business continuity plan (BCP) for these events … but what about the financial recovery?

Many large food manufacturers have business continuity plans that detail procedures for ensuring employee safety, salvaging supplies and inventory and restoring operations should disaster strike. But such plans often do not include established protocols for proving losses caused by the disaster. A lack of those protocols could delay or impede the claims preparation process for potential recovery under an insurance policy. Various obstacles can hinder a company's efforts to support a loss, so planning ahead by knowing the appropriate documentation, how to retrieve it and then how to communicate that information with your insurer can often be the difference between negotiating and litigating a complex insurance claim.

Appropriate documentation

Insurance claims are based on facts – property damaged, expenses incurred, profits lost. Proof in the form of documentation is required to support those facts. It is critical that the BCP consider communications to key organizational leads, such as finance, sales and marketing and operations, to make sure documentation supporting those facts is captured appropriately and communicated to risk management, or to whoever within the organization is responsible for the claim.

But even before getting to the documentation, it is important to first explain your business to the insurers in the context of the loss. Nobody knows your manufacturing business better than you, so it is imperative that you help insurers understand. Explain how you make money, so you can then explain how you have lost it. Being able to help your insurer understand the entire loss circumstance, in the context of the supporting documentation, will help you effectively communicate your claim to insurers.

After your insurer understands how your business works, it is time to provide the proof you will need to recover your losses. The type of documentation required depends on the components of the claim. For physical damage, such as to finished goods, the current sales values of the damaged products and their associated selling expenses will likely be required, whereas standard costs and production price variance data will likely be necessary for work-in-process and raw material losses.

Out-of-pocket costs such as production outsourcing and incremental product testing are likely more straightforward to document, using specific vendor invoices to support them. However, the various categories of incremental operating costs can be harder to document. These could include production inefficiencies, incremental R&D costs due to delayed product launches or cost savings initiatives and incremental sales or marketing costs. A holistic view of how your organization is impacted by a loss will enable you to determine what documentation will be needed to support the financial loss calculation, so you can direct the organization accordingly.

Capturing proof

When disaster strikes, food manufacturers often react quickly to contain the damage, protect property and re-establish operations. Many of the costs incurred to do so may be recoverable through an insurance policy, provided that those costs are appropriately documented and supported in the claim. When property has been damaged or compromised and the pressure is high to resume business quickly, those in the trenches can forget to track and document what could be recoverable expenses.

When faced with an insurance claim, you need to consider all aspects of loss that your organization is incurring. Looking beyond just the physical damage from a loss, you could also be incurring costs at the distribution, sales, marketing and research and development levels. After a loss, notify the organization that any impacts altering "business as usual" need to be captured, reported to risk management and evaluated for potential insurance recovery. The capture of proper documentation is essential to recovery.

Let's take the example of a storm-damaged facility where you will need to dispose of products and materials due to water damage. It is important to demonstrate to the insurers that the disposed product is in fact damaged. In this example, the water could contain bacteria or other foreign substances, possibly damaging the

finished goods. The quality assurance procedures utilized to determine whether the product is useable should be thoroughly documented just as they would be during a non-loss situation, even though you might be overwhelmed with the volume of quality assurance needed. Whether disposing of one pallet or a thousand, your quality assurance procedures need to be consistently applied and documented.

Even repairs to the structure itself may not be as straightforward to document as initially thought. Many manufacturing facilities are older buildings exempt from subsequent code changes—until they are damaged and need to be reconstructed. Code upgrades could require increased construction costs and longer reconstruction timelines. Detailing to insurers the difference between reconstruction changes due to codes, as well as those from upgrades, is a critical step. To support the claim, you should document details regarding what you are doing to the facility and why you are doing it. If the insurer understands your reconstruction reasoning, recovery of your losses should be a smoother process.

Another example of incremental costs resulting from the facility damage might be in the area of incremental freight costs. While your facility is shut down for repairs, your distribution team is likely expediting freight as the product comes from other facilities or outsourced producers, in efforts to fill as many orders as possible on time. Logistics tracking can get complex very quickly and may be difficult to track if proper documentation is not maintained from the beginning. Flagging loss-related shipments or maintaining specific origin and destination information are both examples of ways to capture this incremental cost data for insurance claim purposes.

Effective communication

Communication is important throughout the claims process. You need to manage insurer expectations regarding claim documentation, cash advance requests and your expected timing for settlement. This is best done through the presentation of an initial loss estimate and then an agreed-upon schedule of meetings where updated loss estimates and documentation are provided and select claim items are resolved. After identifying, capturing and providing the appropriate claim documentation to insurers, you need a consistent dialog with insurers to discuss the information provided and to reach resolution in a methodical manner.

At the end of the day, while issues may arise that hinder your ability to document some claim items, preparation is critical to documenting and recovering what is due to your organization under your insurance policy. Establishing and communicating plans that detail the process of what documentation is needed and how it should be captured, and then communicating that documentation to insurers is essential to the success of settling your claim. If those responsible for executing the business continuity plan and those responsible for helping the organization prepare its claim are all aware of their responsibilities in advance, they will be able to incorporate that knowledge into their actions to both recover operations and document the claim following a loss.

The views expressed herein are those of the authors and do not necessarily reflect

the views of Ernst & Young LLP. Allen Melton is a partner at Ernst & Young LLP and is the Americas leader for Ernst & Young's Insurance Claims Services practice. Jason Trahan is a senior manager in Ernst & Young's Fraud Investigation & Dispute Services practice.

Source URL (retrieved on *07/22/2014 - 2:59pm*):
http://www.impomag.com/articles/2010/03/preemptive-disaster-planning?qt-digital_editions=0&qt-recent_content=1