Business Interruption – Indemnity Periods

A disruption to an organisation can result in an extended interruption to normal business operations, often leading to a reduction in turnover.

A Business Interruption Policy aims to restore an organisation to the financial position it would have occupied had the insured disruption not occurred, subject to the maximum indemnity period.

Selecting an appropriate maximum indemnity period (MIP) is critical to ensuring sufficient time for rebuilding, reinstatement and recovery.

This Loss Prevention Standard outlines the key factors organisations should consider when determining an appropriate maximum indemnity period.

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Introduction

The purpose of a business interruption policy is to restore the Insured to the position they would have enjoyed had it not been for an insured disruptive event, until full recovery is achieved or the MIP expires, whichever occurs first.

The MIP should be sufficient to cover the duration of a reasonable worst-case disruption.

This should include the time required to rebuild damaged premises, reinstate operations, implement any necessary recovery activities and regain customers, enabling the organisation to return to the position it occupied prior to the disruptive event.

An inadequate MIP may result in losses continuing beyond the expiry of the policy's indemnity period, with any uninsured costs being borne by the Insured.

Important: The responsibility for deciding the MIP under a business interruption policy rests with the organisation. However, advice and guidance should be sought from your broker and insurer when choosing the most appropriate cover.

Note: This Loss Prevention Standard relates to business interruption and is focussed on loss prevention and related risk management guidance. It is not intended to address liability/general liability exposures. The presumption is that all local regulatory territory requirements, and compliance with national/local building regulations, codes, or standards take precedence and have, or will be, met. In territories where local authorities have jurisdiction, compliance with applicable laws and regulations is assumed as a minimum requirement. The recommendations in this document are intended to supplement, not replace, local requirements.

Understanding the Risks

Selecting a MIP that supports business recovery to pre-interruption levels is critical, with many organisations underestimating the time it will take to recover and re-establish their market position. This can have serious consequences, including:

- **Uninsured Losses.** Without an appropriate MIP, losses can continue before a business has resumed operations or is trading at pre-interruption levels.
- **Increased Costs.** Significant increased costs of working may continue and be borne by the insured if the selected MIP is too short.
- **Reputational Damage.** Failure to supply products or services can damage customer confidence and harm long-term business relationships. Customers may seek alternative suppliers, potentially resulting in permanent loss of business.

Indemnity Period Definitions

It is important to understand how a MIP is defined by the Business Interruption Policy:

Indemnity Period. The period during which business results are affected due to the damage, beginning with the date of the damage and ending not later than the MIP.

Maximum Indemnity Period. The number of months stated in a policy schedule (unless amended in any additional contingency).

In practice, this means the insurance policy will cover the business interruption losses starting on the day the interruption occurs and ending at the expiry of the MIP.

For example, should the interruption occur on 1 June:
- With a 12-month MIP, the policy will cover the business interruption losses incurred up to 31 May of the following year, but not beyond that date.
- With an 18-month MIP, the insurance will cover the business interruption losses incurred up to 30 November of the following year, but not beyond that date.

Optional extensions to a standard business interruption policy, such as the specified suppliers or committed costs extensions, may have shorter MIPs and, if so, this will be stated in the policy schedule.

Choosing the MIP

Whilst 12 months is the minimum period typically available, it is rarely sufficient to fully recover operations to pre-interruption levels.

Buildings may need to be reinstated following planning, design and approval processes. Equipment may require a period of commissioning. Raw materials and labour need to be sourced, and customer relationships re-established.

The MIP should be long enough for the business to fully recover to the same financial position they would have enjoyed had the loss never occurred.

Factors which can impact business recovery include, but are not limited to:

Reinstating the Premises. In many cases, organisations will want or need to reinstate or repair the premises at the same location. The premises may be owned, or be conducive to business activities due to their nature, location, facilities, etc. Even for rented properties, contracts may stipulate that the tenant must return to the property providing the premises are rebuilt within a given timescale.

The time it takes to rebuild or repair a property is affected by a wide range of factors, including:
- Age.
- Size.
- Complexity.
- Construction materials and methods.
- Listed status.
- Location (centre of a city, remote, isolated site, etc.)
- Style of building (terraced, semi-detached or detached)
- Any trade-specific requirements (e.g. hygiene requirements for food production, freshwater supplies, etc.)

Other factors that may increase rebuilding time include:
- Decontamination and site clearance.
- The design process for the new building.
- Current building regulations.
- Availability of materials.
- Approval from local planning departments or authorities.
- Any environmental requirements – even properties built only 10 years ago may have to meet new standards for carbon neutrality or having rainwater harvesting or retention to reduce the flooding risk.
- Overcoming local objections.
- Availability of suitable contractors.
- Access issues to the property.
- Issues arising if the site of the loss is considered a crime scene.

Trading from Alternative or Temporary Premises. Some occupancies, for example, small offices, storage depots or small industrial units, may be able to relocate to alternative or temporary premises with relative simplicity. Within a relatively short period of time of the loss occurring, e.g., three to six months, trading operations can be fully re-established and generating income whilst the original property is being rebuilt.

For other occupancies, alternative or temporary premises are not practical. These might include:
- Food or pharmaceutical production, which require licensed hygienic premises,
- Industrial facilities with complex utility requirements or machinery configurations - it can take as long to fit-out a new property as it does to rebuild the original premises.
- Similarly, hotels and multiplex cinemas cannot easily trade from temporary premises.

Sub-contracting. Where alternative or temporary premises cannot be established, the scale of the interruption can often be mitigated by sub-contracting work to third-party suppliers. In some cases, this may not be acceptable to the organisation, particularly when intellectual property, such as recipes or manufacturing processes, would need to be shared with competitors.

Machinery Replacement. Some organisations use highly specialised or bespoke equipment which can be expensive to replace, built to order, or have a long lead time for replacement. Multiple orders to replace several machines could take considerably longer than a single machine order.

Older machinery can also present additional challenges. Replacement parts, whether new or refurbished, may be difficult to obtain, particularly where equipment is obsolete or the original manufacturer is no longer trading. In some cases, suitable alternatives may need to be sourced, adapted, or custom manufactured, resulting in further delays.

Additional time may need to be factored in to install, commission and run-in machinery, and some industries may require validation periods and consistent product quality runs before normal production can recommence.

In addition, machinery replacement often depends on the affected premises being reinstated to a suitable condition and delays in repairing the building envelope or restoring essential services can delay the installation and commissioning of equipment. For example, unresolved issues relating to watertightness, environmental controls, security, or utility supplies may prevent machinery from being brought back into operation, resulting in further disruption.

Customers. The loss of customers following a disruptive event can have a significant impact on the recovery of a business and may extend the period required to return to pre-loss levels of turnover. This is particularly relevant where a business is heavily dependent on one customer, or a small number of customers, that account for a substantial proportion of its revenue.

During a prolonged interruption, customers may seek alternative suppliers to meet their needs and once new supply arrangements have been established, may be reluctant to return immediately. In some cases, customers may have entered into longer-term contractual arrangements with competitors, making it difficult to regain lost market share.

Marketplace. Recovery is also impacted by the number of competitors an organisation has and how easily customers can switch to alternative suppliers.

- An organisation may recover relatively quickly if it has few competitors or operates in a specialist market where competitors would struggle to increase production easily.
- It will take considerably longer to recover from or replace lost business if there are many competitors and customers can easily move their business elsewhere.

Suppliers. Raw materials damaged during the interruption event may have long lead times for replacement, particularly where large inventories are required. Transportation times for equipment manufactured overseas can also cause delays.

A loss event at a critical supplier's premises may result in inadequate availability of products, components or raw materials, and impact production or essential services.

Validation, Certification and Quality Assurance. Some organisations may require additional time after the buildings have been reinstated, and operations restored to obtain the licences, quality assurance approvals or meet customer compliance requirements. This is particularly important in sectors such as food, pharmaceuticals and other regulated industries where quality and safety are critical. Any delays in achieving these requirements can extend the required recovery period.

Seasonality. Some organisations or sectors are subject to seasonal peaks:

- Christmas, in particular, accounts for a significant amount of retail, food and beverage sales. A loss event in the run-up to the Christmas trading period would have a far bigger impact than one occurring at any other time of the year.

Contact Information

United Kingdom

Please visit Aviva Risk Management Solutions or email us at riskadvice@aviva.com. To speak to one of our advisors, call 0345 366 6666.*

*The cost of calls to 03 prefixed numbers are charged at national call rates (charges may vary dependent on your network provider) and are usually included in inclusive minute plans from landlines and mobiles. For our joint protection telephone calls may be recorded and/or monitored.

Canada

Please visit Aviva Risk Management Solutions | Aviva Canada or email us at arms.canada@aviva.com

Ireland

Please visit Insurance Risk Management | Business Risk Management Insurance - Aviva Ireland or Email us at armsireland@aviva.com

Specialist Partner Services

Aviva have created a network of Specialist Partners to complement our in-house capabilities and to enable our policyholders to benefit from a wide range of risk management solutions at preferential rates and terms. Together, we provide solutions to help with the significant challenges of modern-day risk management.
Note: These partner relationships are wholly for the benefit of our policyholders with no income to Aviva.

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For more information please visit: Aviva Risk Management Solutions - Specialist Partners

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For more information please visit: Insurance Risk Management | Business Risk Management Insurance - Aviva Ireland

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For more information please visit: Our Specialist Partner Network | Aviva Canada

Standards, Sources and Useful Links

Canada
- The Business Continuity Institute - Canada

Ireland
- The Business Continuity Institute - Republic of Ireland

United Kingdom
- The Business Continuity Institute

Additional Information

Loss Prevention Standards

These documents set out best practice recommendations to help reduce the likelihood and impact of losses.

Relevant Aviva Loss Prevention Standards include:

- **Business Continuity - Seven Steps to Continuity**
- **Business Continuity - Step 1: Roles & Responsibilities**
- **Business Continuity - Step 2: Incident Management Plan**
- **Business Continuity - Step 3: Communications Plan**
- **Business Continuity - Step 4: Business Impact Analysis and Risk Assessment**
- **Business Continuity - Step 5: Solutions Design and Implementation**
- **Business Continuity - Step 6: Policy**
- **Business Continuity - Step 7: Test and Exercise Plan**
- **Supply Chain Risk Management**
- **Business Interruption - Committed Costs**
- **Business Interruption - Specified Suppliers Extension**
- **Business Interruption - Rebuilding Period and Valuation**

Please visit Loss Prevention Standards to view the full library.

Aviva Risks Training Solutions (United Kingdom Only)

Aviva Risk Training Solutions, delivered through our Specialist Partner, SafetyCulture, provide free, bite-sized learning modules exclusively for Aviva policyholders.

Please visit Aviva Risk Training Solutions for further guidance.

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