

Loss Prevention Standards – Cross Classes

# Supply Chain Risk Management

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With many organisations having global supply chains, assessing each link for resilience is vital, to ensure that companies can continually supply to their customers.

# Supply Chain Risk Management



## Brief History of Supply Chains

Supply chains have been around for as long as trading has existed, with many businesses being dependent on other organisations for the supply of stock, machinery, equipment, services, etc.

World events often see acceleration of development in certain areas, necessitated by what event has happened. The end of World War II signified a large increase in mechanisation, material handling and warehouse design. The mid-1950s saw advances in container transportation by road, and the 1980s saw development of personal computers and rapid technology advances.



The widespread **recognition of the term 'supply chain'** has come primarily as a result of the globalisation of manufacturing since the mid-1990s. Computer technology has improved communications, ordering and stock control, and the reach of supply chains around the globe.

## Some Statistics

The Business Continuity Institute (BCI) Supply Chain Resilience Report each year looks at impacts from incidents in the supply chain. These figures from the [2019](#) report demonstrate where businesses saw an interruption, but also that a large amount of companies had not assessed their supply chains at all:

- 48.9% interruption in supply chain, seen at Tier 1
- 24.9% interruption in supply chain, seen at Tier 2
- 12.2% interruption in supply chain, seen at Tier 3 and beyond

32.6% do not analyse their supply chain fully.

## Risks to the Supply Chain

- ECONOMIC – Take over, bankruptcy, failure of supplier at lower tier
- POLITICAL – Border closures, tariffs, **political unrest....BREXIT**
- LEGAL – Injunctions, forced closure
- SOCIAL – Strike, criminal activity, caught in **another's** dispute, arson
- ENVIROMENTAL – Pandemics, extreme weather, natural disaster, flood
- TECHNICAL – Cyber crime, IT failure, equipment breakdown, utility issues, transport, fire

## Insurance

Business Interruption (BI) Insurance may well require a review following a supply chain risk assessment. The insurance in place for BI will provide cover to the organisation for incidents causing an interruption at the **organisation's** premises. There may/will be a need to extend this cover under the Business Interruption section, to include any losses incurred as a result of an interruption, caused by an insurable peril, at the premises of a supplier. This can be done in two ways.

First by taking out an Unspecified Supplier Extension: this will provide cover as detailed above, but for an interruption at any, unspecified supplier.

Secondly, a Specified Supplier Extension: this will provide the same type of cover, but for a specified supplier to the business, named in the policy.

## LOSS PREVENTION STANDARDS

In **today's** business world, the loss of an important or key supplier, service provider or manufacturer in an **organisation's** supply chain, could be considerably more serious than an actual loss at their own premises. Assessing this exposure requires investigations into what would or could be lost if that supplier was:

- Unable to supply the organisation; and
- It was difficult to duplicate what they did, or what they supplied

These will be considered key suppliers, and they could be responsible for a sizeable portion of the income to the business, or a sole or critical supplier of a product or service. The sum insured for a specified supplier extension should be assessed in detail to ensure it is adequate. It should be re-visited regularly, to ensure the sum insured stays at a level that represents the income derived from that supplier. Even the smallest component; a packaging or printing element or a service provided could result in the exposure to the primary business being significant.

With an unspecified supplier extension, the sum insured will require an organisation to look at the likely financial impact on the business of the loss of any of the smaller suppliers they deal with. These unspecified suppliers would be responsible for less income to the business, and not a sole or critical supplier of a product, or supplier of an essential key product. These should be suppliers the organisation would have less trouble replacing with a similar alternative or where alternatives are in place but could still see a financial loss if an incident at their premises caused a loss of supply.

## Reputational Impact

Businesses should consider the impact the loss of a supplier will have on them from end to end. It should include the potential loss of customer goodwill, and damage to the **organisation's** reputation.

Customers will probably only see their 'immediate supplier' as the responsible party, if something such as a product or service is not available to them. It could be that an incident somewhere down a **company's** supply chain has halted production or delivery of products, components, etc., but the customer will see only the business they directly deal with (and their name), as letting them down. This is probably the name that will be mentioned and publicised, and this situation could be further worsened by involvement of social media, television, industry publications and newspapers.

This demonstrates how important it is to fully understand where products and services come from, where the issues could arise in the supply chain, and to ensure that adequate resilience is built into the process.

Even if a **business'** Tier 1 (immediate) supplier is a large multi-national company, they may still get key supply, parts, raw materials, etc, from a number of much smaller companies further down the supply chain, **who don't** have their approach to risk management; their manufacturing resilience; their level of management diligence; their own company standards and desire for such things as protections and detections.

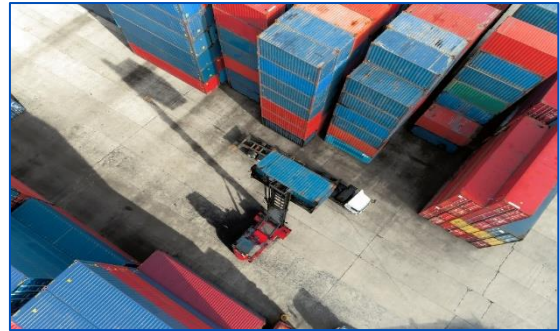
With an integrated supply chain, the component, process, service or product is contracted out to a partner, but the inherent risk to the final end-product is only as robust as the weakest link in that chain. If the approach to risk management by each partner down or across the supply chain is different, then the exposure felt by all parties is that created by the poorest risk within the chain.

## Mitigating Actions

Completing a supply chain risk assessment may highlight areas of concern, and this should suggest actions to be taken immediately to protect, for example, key processes or contracts, or actions to put things in place ready to be invoked/actioned at a time of emergency.

The list below details some of those probable activities:

**Diversification** – Doing something different, if a product or process is not available. A **business’ machinery or current processes** may suit a different product to protect its income.



**Stockpiling** – Perhaps key products, materials, ingredients, can be stored to provide a safety ‘buffer’ stock, to enable time to source alternatives, should an interruption occur.

**Contracts and Service Level Agreement’s** – Contracting service levels and penalties for failure can force suppliers to build in resilience, to minimise or avoid interruptions.

**Substitution** – If a product or service is unavailable, can the business supply customers with a viable alternative?

**Duplication** – Providing multiple sources of key supplies helps protect against the loss of one of the suppliers. The key is to understand if the provision is exactly the same, if there are any differences and what impact one supplier has, and if the others can make this up?

**Rationalisation of Product Range** – Can the business reduce its range of products in the event of an incident affecting its supply? What is the basic level of products the business can still operate with? Lower earning lines may be removed to protect delivery of more important/profitable or reputationally important product lines.

**Product or Process Redesign** – Can either the product or the process be changed (Management of Change) to lessen the impact of products, parts, ingredients, services, etc. not being available?

**Localised Sourcing** – Establishing suppliers closer to the principle site in need could result in better communication, a stronger relationship, an earlier notice that there could be a problem or any potential challenges with logistics. It could make it easier to re-stock, or to provide help.

**Supplier Selection** – **Selecting suppliers shouldn’t just be about the product**, it must also consider their resilience. What are the physical arrangements of their site(s); what is their approach to risk management; is their Business Continuity Plan (BCP) suitable, up to date and tested?

**Supplier Development** – Sharing best practice, developing closer links, creating joint employee training programmes, etc., can build relationship, as well as see products dealt with in a more consistent way. It can also **raise a company’s level of importance with their key suppliers’ own business portfolio**.

**Monitor Suppliers and Chain** – Assessing the supply chain is hugely important, but monitoring it is also key. There could be changes happening that affect a business with their supplier, their processes, their own suppliers, or licencing, etc., e.g. Brexit - the 31<sup>st</sup> December 2020 marks the end of the Brexit transition period, and the immediate period after this date will undoubtedly pose a number of additional challenges for many UK organisations.

Being aware of these and other issues gives a business a chance to consider how these could impact on them.

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## Business Continuity Planning

Business Continuity Planning and Management is key to coping with incidents and recovering the business afterwards. This should include any impact an incident has at a supplier, especially a key one to the business.

It is essential that consideration is given to this when building, maintaining and testing a BCP. For example, will the resources required by the recovery strategy be available, now that a certain supplier is out of business for the immediate future? Will a secondary supplier for the products or services affected need to be brought online quickly? Will the customers affected be prepared to wait, or will the company need to provide a viable alternative product? What could be impacted and for how long?

There will be many questions, depending on the type of business and the supply lost. Addressing as many threats to a business as possible, as part of the continuity planning and testing, will help to ensure that suitable preparations can be put in place ahead of time, in case of an actual incident in the future.

Another aspect of business continuity where suppliers and chains must be considered is validation. This is the part of business continuity management where the incident management and recovery strategy is tested, to ensure it will work in the event of a real interruption to the business. It is a good idea to involve key suppliers in this test, so the links between the different businesses and the proposed activities, would actually get the desired result within the required timeframe. This type of loss scenario test can be invaluable and involving suppliers will not only add to the relationship, but bring expertise to the test, in their specific field.

## Risk Assessing Suppliers and Supply Chains

The process of risk assessing and managing a supply chain can appear time consuming and complex. Looking at each supply the business requires, the suppliers who provide it, the resilience of their supply, and the viable alternatives, should something go wrong, can be a major undertaking.

However, this is essential in fully understanding the possible issues that could arise, and which may **affect a company's ability** to provide for its customers, and the financial impact this could have, should service levels drop, and customers go elsewhere.

Assessing the activities required to protect **an organisation's** ability to provide for their customers, and putting in place mitigating features, either now or for at some point in the future, should the worst happen, will help maintain service levels, customer base and market position.

Aviva, working with the RISC Authority, have produced a [Supply Chain Risk Assessment Tool](#). This is a web-based solution to help organisations manage and maintain their supply chain risks, which is available free of charge to Aviva clients on our [Risk Solutions website](#).

Interested businesses can register via the above link for their own toolkit, which can be made bespoke with the addition of the company logo. The toolkit has sections to provide supplier and contact details, and this includes:

- What items/services, etc. the supplier supplies to the business?
- What part of the business or product line this would affect if unavailable, and
- To what degree?

There is a set of questions regarding the resilience of the supply and from the answers provided a risk rating is calculated. This risk rating will be red, orange or green, in order of risk to the business; with red being the highest risk.



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This process should be followed with each supplier and the product or service they provide. The questions asked to build the risk rating can be discussed over the phone, or there is an in-built facility to email the questions from the tool to the supplier contact.

Saving each entry will populate a dashboard section which will show all supplies/suppliers, and this can be ordered to show the high risk rating entries at the top. These by their very nature should be the highest priorities to act on.

The dashboard will also show how many assessments (the question set) for each entry are complete or in progress, enabling monitoring of progress. Once a red/high rated aspect has been improved by a supplier, for example, supply duplicated, or BCP now in place, the rating can be changed to reflect the improvement of the risk and the reduced exposure to the primary business.

This process will help suppliers recognise weaknesses further along their own supply chain, with their own suppliers of goods or services, and also enable them to act on those.

There are resources and FAQ sections to help in the process and resolve queries. The facility is also arranged to export parts of the Toolkit to Microsoft Excel spreadsheets, for reporting, etc.

## Specialist Partner Solutions

Aviva Risk Management Solutions can offer access to a wide range of risk management products and services via our network of Specialist Partners who are reputable companies offering agreed discounted rates for Aviva customers.

For more information please visit:

[Aviva Risk Management Solutions – Specialist Partners](#)

## Sources and Useful Links

- [Business Continuity Institute](#)

## Additional Information

Relevant Loss Prevention Standards include:

- Business Continuity
- Business Continuity – Testing and Maintenance
- Business Impact Analysis
- Business Interruption – Indemnity Periods and Maximum Indemnity Periods

To find out more, please visit [Aviva Risk Management Solutions](#) or speak to one of our advisors.

Email us at [riskadvice@aviva.com](mailto:riskadvice@aviva.com) or call 0345 366 6666.\*

\*Calls may be recorded and/or monitored for our joint protection.

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