

MEETING STAKEHOLDER EXPECTATIONS IN ONSHORE ENERGY

What needs to change to deliver claims service consistency?

Onshore energy insurance claims can be complicated, depending on the asset damaged at a facility, the complexity of the production process and the damaged asset's criticality to the production process. The majority of claims are settled without dispute, but there is a trend developing with large and complex claims that can leave the Insured with long periods of silence regarding affirmation of policy liability from their Insurers and simultaneously Insurers left feeling frustrated, in effect with their 'hands tied', as a result of the Insured not providing information material to the claim investigation.

The insurance market has proven time and again its ability to handle and settle the most complex property damage and business interruption losses. Most, if not all, industry professionals can reel off numerous examples of service that has delighted Insureds, helping them recover from debilitating events. With the ultimate ambition to consistently deliver this service experience, Integra Technical Services questioned Insurers, Brokers and Insureds to find out what needs to happen to make this possible.

Leo Dixon, Chief Operating Officer, Integra Technical Services explains "we asked questions in four areas: the policy clauses that most frequently cause difficult conversations

and polarise opinion; how to reduce conflict; and what the insurance market should 'start' and 'stop' doing to improve the claims service experienced by Insureds. The questions provoked excellent responses and material for several articles which we will address, but the burning issue is how we provide a claims service experience that Insureds can rely upon and which provides Insurers and Brokers with competitive differentiation."

For the purposes of our survey, the definition of Onshore Energy included the Oil and Gas, Power Generation and Mining sectors. Whilst the type and severity of losses can vary, respondents identified eight clauses that stood out (see

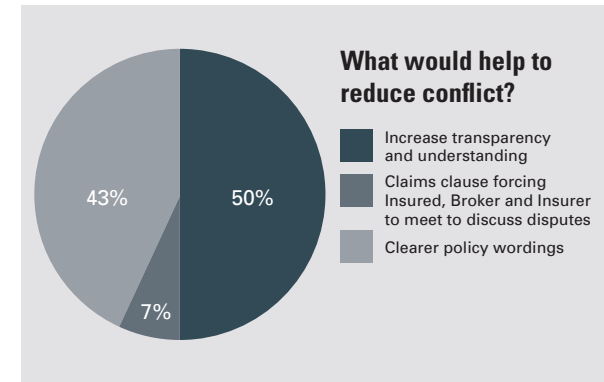
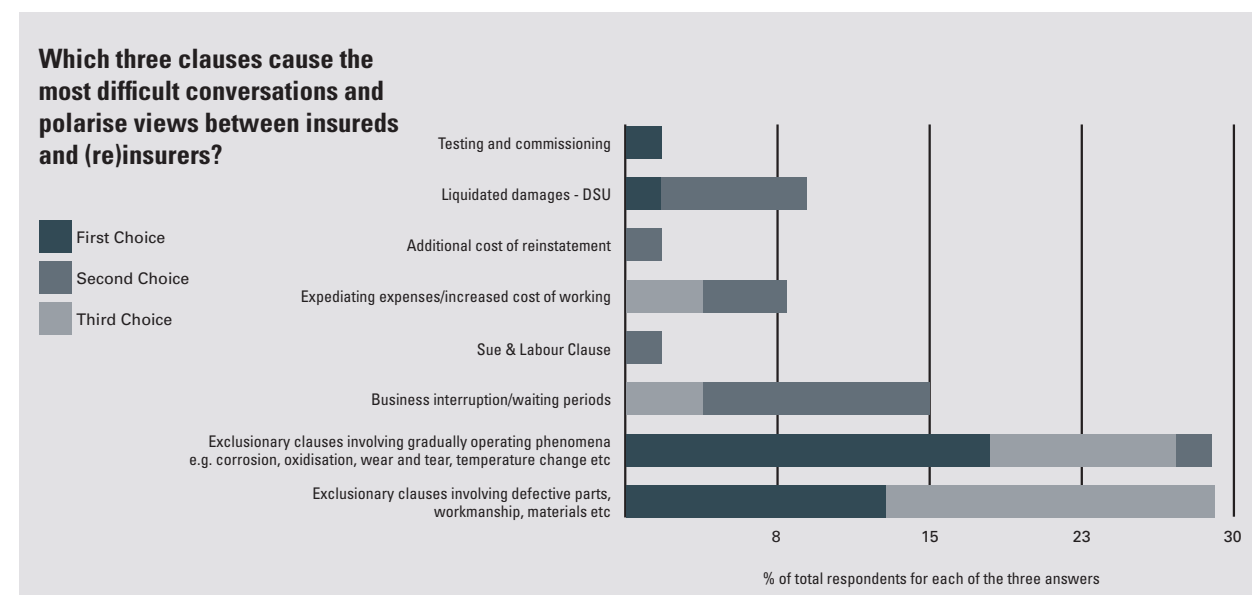


chart). Kevin Miller, Major Loss Claims Adjuster at AIG felt that "a high number of losses in this sector have turned on the clauses that came top in the survey."

Jonathan Haysom, Senior Partner at JLT Specialty agreed but believes that disagreements between Insureds and Insurers are becoming more commonplace. "Perhaps there is a dynamic that correlates with the market conditions and the way it encourages practices that get more competitive deals, but which can exaggerate the problem".

MARKET CONDITIONS

Without question the continued prevalence of the soft insurance market and abundance of underwriting capacity has put pressure on underwriting margins. In the Energy sector this has been compounded by lower oil prices which has led to reductions in insurance values and premiums.

These conditions can enable opportunistic behaviour with positive and negative implications for the Insured's claims service experience. The increased use of 'Offslips', new entrants that are perhaps less experienced in the sector and policy wording enhancements.

Leo explains "we have seen 'Offslip' insurers that underwrite a small part of a risk but are CAPs in their own right,

slowing down the decision making process of other Leading Insurers. Some even go as far as appointing their own experts for their 'Offslip' resulting in multiple Adjuster (and sometimes multiple Lawyer) appointments."

According to Jonathan "we are seeing Insurers entering new markets to help them grow and to replace lost premium income. Competition is helpful to securing more cost effective cover, but it does not come without risk as some markets don't necessarily have the track record or history of handling complex onshore energy claims."

Prescriptive policy wordings would help to breed common understanding and interpretations and it's easy to see why this might make sense to the uneducated observer. But this would stifle competition and choke the market innovation that clients increasingly demand to meet their evolving risk management requirements.

BEING CLEAR ABOUT POLICY INTENT

Brokers and Insurers diligently draft and agree new wordings but these can sometimes introduce 'grey areas'.

Leo explains "uncertainty can come from additional words being inserted into phenomena clauses without clearly defining what they mean, for example, 'abnormal corrosion', 'accelerated corrosion' or 'unusual corrosion'. We've also seen business interruption policies where it is not crystal clear whether the waiting periods apply to the production loss or sales loss. The production loss is immediate whereas the sales loss can be 30 or more days after the event has occurred. Immediately this creates a measurement issue with different parties having their preference as to which loss they'd like it to be."

It's not difficult to see why half of those surveyed would like to see more transparency and agreement with the interpretation of the policy. Pre-loss workshops and claims

scenario stress testing to establish how the policy would respond, delivering tangible clarity to the wording and proving invaluable when a loss occurs.

Whilst many Insurers and Brokers run workshops with a number of their clients, the investment of time and resource required by all the parties (Insurers, Brokers, Insured and often the appointed Loss Adjuster) is possibly the single reason why they are not as widespread as they should be.

We have noticed that if the Insured's Risk Manager has experienced a complex loss during their career or seen how these can help with theirs and their Insurer's understanding of the wording, then they are more likely to invest the time that is needed to make a successful pre-loss workshop. High profile events can also trigger Risk Managers into action, probably as a result of their board of directors raising questions amid a realisation of the importance of quickly confirming to investors and other stakeholders that their insurance will respond in the event they suffer a similar type of major loss.

Kevin agreed "Insureds want confirmation as early as possible that their claim is insured and we strive to meet that requirement. We introduced the AIG Claims Payment Commitment to assist our Insureds with financial obligations they face following a claim and an additional benefit is that this encourages quicker coverage decisions. One of the things AIG has pioneered is claims workshops that look at pre-loss scenarios and promote discussion about policy intent."

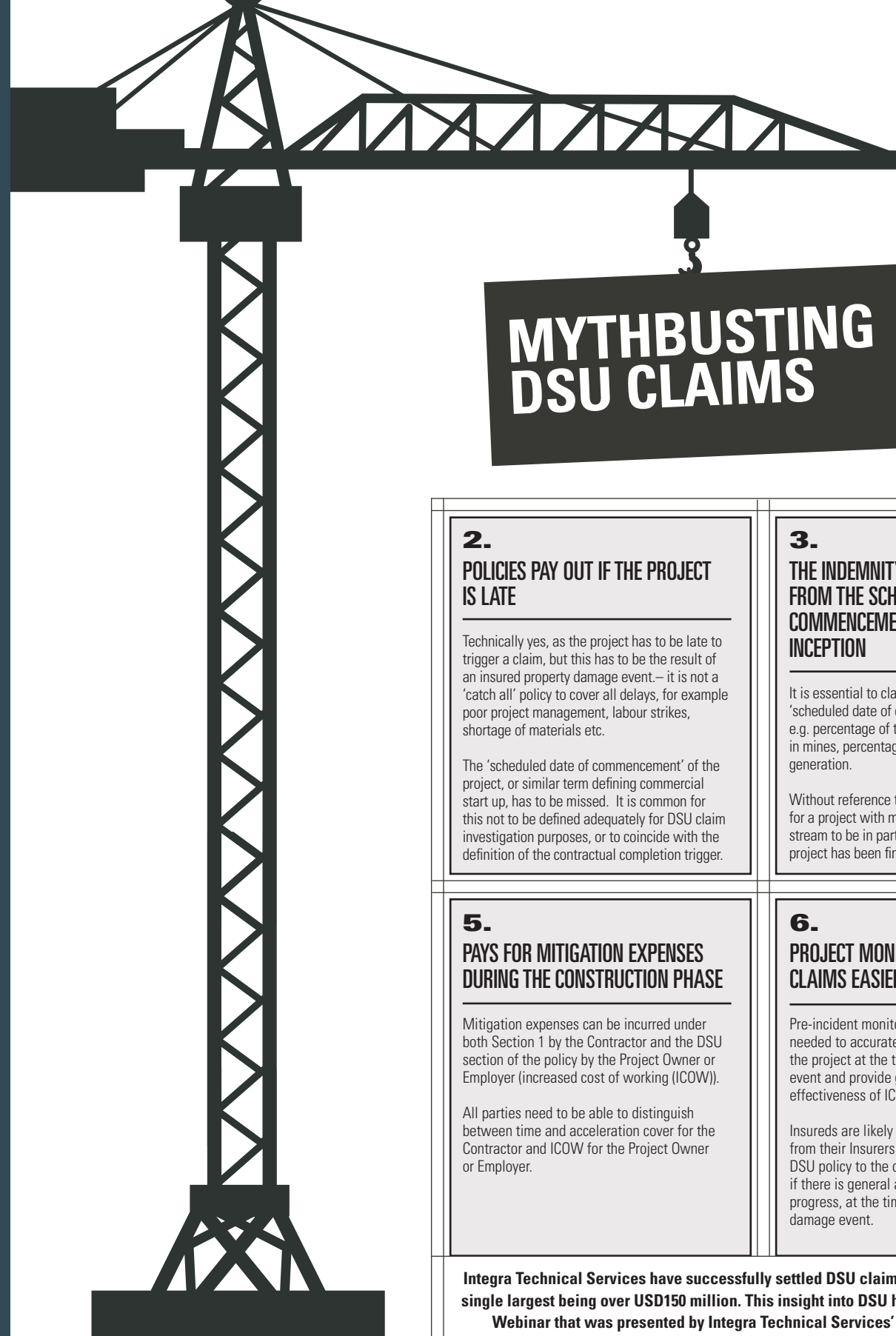
Steve Willis, Property Loss Control Insurance at ENGIE, mooted "whether policy renewal objectives should include the achievement of claims certainty for key production sites". Perhaps this suggests that Chief Financial Officers or boards of directors of client companies actually hold the key to making the next step change in improvement. Setting objectives which encourage Risk Managers, Brokers and Insurers to run more regular pre-loss workshops and policy intent discussions, which in turn help manage stakeholder claims expectations and ultimately create more of those claims service experiences that delight the insured.

PROJECT MANAGING THE CLAIMS PROCESS

One of the more interesting improvement suggestions was to "run individual major loss claims as if they were projects in their own right with critical timelines, commitments and objectives.

This is not unique and there are odd examples in the market but perhaps it should be examined in more depth to understand the practicalities. This is particularly relevant to sectors such as onshore energy where clients are familiar with project management principles.

Whilst this would not solve policy interpretation or coverage issues, it would bring transparency to the process and ensure that the consequences of failure to deliver on agreed action points was visible to the stakeholders.



MYTHBUSTING DSU CLAIMS

1. INSURERS RARELY PAY DSU CLAIMS

Claims are paid as Integra Technical Services and Insurers can testify. However, and for different reasons, the settlement does not always meet the Insured's expectations, for example:

1. Insured vs uninsured delay;
2. Problems ascertaining the critical path;
3. Deductible period (time or monetary) and there maybe multiple deductibles if further periods of cover have been purchased;
4. Defects clauses and concurrency of critical path for the repair of defects or improvement to the original design;
5. Indemnity payments not due until the indemnity period starts, even if the delay happens early in the life of the project.

2. POLICIES PAY OUT IF THE PROJECT IS LATE

Technically yes, as the project has to be late to trigger a claim, but this has to be the result of an insured property damage event. – it is not a 'catch all' policy to cover all delays, for example poor project management, labour strikes, shortage of materials etc.

The 'scheduled date of commencement' of the project, or similar term defining commercial start up, has to be missed. It is common for this not to be defined adequately for DSU claim investigation purposes, or to coincide with the definition of the contractual completion trigger.

3. THE INDEMNITY PERIOD STARTS FROM THE SCHEDULED DATE OF COMMENCEMENT INCLUDED AT INCEPTION

It is essential to clarify what determines the 'scheduled date of commencement' e.g. percentage of throughput of materials in mines, percentage of efficiency of power generation.

Without reference to production it is possible for a project with more than one revenue stream to be in partial production before the project has been finally completed.

4. INSURERS CAN OFFSET LIQUIDATED DAMAGES (LDs) AGAINST THE DSU CLAIM

LD claims are rarely straightforward and usually contested. If the Project Owner is receiving LDs under the contract, then there would be a degree of double insurance or cover in place.

As a consequence, we see LDs often forming part of a negotiated settlement, depending upon the DSU policy language (Debt Service or Gross Profit) and the contractual terms.

5. PAYS FOR MITIGATION EXPENSES DURING THE CONSTRUCTION PHASE

Mitigation expenses can be incurred under both Section 1 by the Contractor and the DSU section of the policy by the Project Owner or Employer (increased cost of working (ICOW)).

All parties need to be able to distinguish between time and acceleration cover for the Contractor and ICOW for the Project Owner or Employer.

6. PROJECT MONITORING MAKES CLAIMS EASIER

Pre-incident monitoring can reduce the time needed to accurately determine the status of the project at the time of a physical damage event and provide greater certainty about the effectiveness of ICOW expenditure.

Insureds are likely to get earlier feedback from their Insurers on the application of the DSU policy to the delay they have experienced if there is general agreement as to the progress, at the time of an insured physical damage event.

7. COVERS ALL THE LOSSES THAT OCCUR DURING THE INDEMNITY PERIOD

DSU policies cover losses which are correctly indemnifiable. If there are number of indemnifiable losses in the project period and the project is not completed until after the 'scheduled date of commencement', then the DSU claim is the cumulative effect of all of the adjusted indemnifiable losses on the project.

As such there can be only one DSU claim per project, unless further cover is purchased to provide additional periods of indemnity.

Integra Technical Services have successfully settled DSU claims with a combined settlement value in excess of USD500 million, with the single largest being over USD150 million. This insight into DSU has been taken from a Zurich Global Corporate UK Construction Insurance Webinar that was presented by Integra Technical Services' Adam Humphrey and Zurich Global Corporate UK's Jonathan Sargent.