Testing & Commissioning

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Background

• Separate Construction and Operational markets

• Projects undertaken and insured in the Construction market

• Operational markets insure operating risk only
  – Not intended to cover project Testing & Commissioning (T&C)

• Construction insurers are reluctant to extend policy coverage for T&C period due to project delays, difficulties in reaching contractual milestones etc.

• Construction policy is often Property Damage (PD) only with no Delay in Start Up (DSU) coverage
  – Insureds keen to move to Operational insurance with full Business Interruption (BI) coverage
Background

• Historically, not properly defined when Operational coverage commenced and Construction coverage terminated

• Historically, losses occurred and there were disputes over which policy is most appropriate and where coverage sits
  – An unacceptable situation for everyone → clarity is essential
Development of the T&C clause

• Operational market sought to establish and clarify when they should consider themselves ‘on risk’

• Attempted to tie this to acceptable set of criteria that are ideally defined in the Engineering, Procurement & Construction (EPC) contract to trigger PD and BI coverage

• All EPC contracts are different however the T&C clause prescribed basic criteria that were generally clear in their definition and should be relatively easy to determine whether they have been fully satisfied

• The basic T&C clause requirements are:
  1. Completion of mechanical testing
  2. Testing & commissioning
  3. Performance testing (to 100% of design throughput, temperature and pressure) for a sustained period of 72 hours
  4. The Insured accepts the plant in writing without safety critical punch-list items being outstanding
Present position

• Clause works adequately in most situations

• Basic requirements are understood and accepted by Insureds, Brokers and Insurers

• Difficulties that have occurred since the introduction of the clause typically involve:
  – Inability to reach design throughput (eg. due to a lack of feedstock)
  – Phased handover brings added complications
  – Schedule delay in associated projects results in tie-ins and related work not being able to be completed in time producing unforeseen knock on effects to the project
  – Contractor arranged insurance rather than Principal controlled can produce communication difficulties meaning that problems are only disclosed late on

• If issues are present sometimes there is insufficient time to resolve these to the satisfaction of all parties producing potential gaps in coverage

• Coverage gaps or dislocation between policies may be in breach of Lenders requirements
Present position

• Most instances of difficulty have been satisfactorily resolved but often at the last minute and after extensive dialogue at a far from ideal critical time of commissioning

• Sometimes involving short notice risk surveys carried out during commissioning phase

• Best resolved with meaningful dialogue greatly assisted if Principal controlled construction policy with commonality of Insurers on the construction and operational placements

• Problems have occurred when the requirements of the clause have been misunderstood or when communication has broken down or not even been initiated

• These situations produced circumstances of conflict between policies but the problem is sometimes only apparent if there is a claim which leads to the T&C clause being found not to have been adhered to by which time its too late and coverage may be jeopardised through non-compliance
London Market Association (LMA)

• LMA of Onshore Energy underwriters group recently formed consisting of underwriters from leading companies and Lloyds markets with the mandate to discuss common issues

• The group decided to carry out a review of several topics including T&C with a view to streamlining this transition from Construction to Operational insurers avoiding any confusion that may exist at present

• Goal is to simplify the process for all parties

• The essential components and intent of the clause are unaltered, it is an evolution of the existing clause

• Clause amended to add clarity, it only formalises and streamlines existing market practice

• Intention is for the Insured to complete a standard questionnaire relating to specific major projects that are to be added to the Operational policy
New Clause & Framework Proposal Overview

• Intended to highlight potential difficulties in advance of potential handover so as to enable dialogue or have sufficient time to arrange survey

• The questionnaire is to be provided to project personnel well in advance of the T&C phase so expectations and information requirements are clear

• The questionnaire is designed to be easily completed by project personnel from their existing knowledge and understanding of the project

• Questionnaire meant to prompt thought over potential areas of concern to Insurers

• Questionnaire is also meant to be concise and helpful enabling Insurers and Brokers to obtain a full insight into the project without mandating a potentially disruptive risk survey

• Questionnaire can prompt dialogue and constructive review between all parties to ensure that there are no loose ends or any uncertainties
New Clause & Framework Proposal Overview

• In summary the questionnaire requests information on the following key elements:
  – Project Overview
  – Mechanical Completion
  – Testing & Commissioning
  – Safety Critical Equipment
  – Performance Testing
  – Official (Contractual) Acceptance
  – Mechanical Integrity, Process Safety and Reliability
Concluding remarks

- Clause can be found on the LMA website at:

  http://www.lmalloyds.com/Web/Wordings/LMA5197.aspx

- If widely accepted within the market translation into various languages would seem sensible

- Believe that this approach is the most constructive in brining together Construction and Operational Insurers to the mutual benefit of Insured, Broker and Insurers