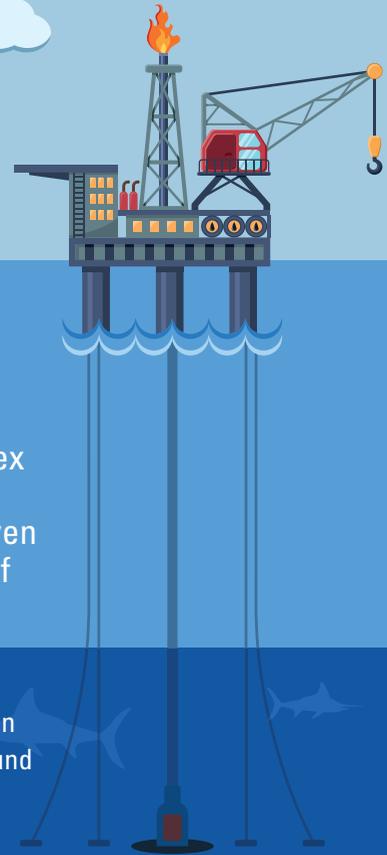


UPSTREAM ENERGY IN FOCUS



A technical root cause analysis is often undertaken in large or complex loss scenarios to determine how an insurance policy should respond. This can present some unique challenges in Upstream Energy and, even once the cause has been established, necessitates careful analysis of policy wordings.

Having recently joined Integra Technical Services to lead their Offshore Energy Team, Sam Foster set up a discussion to consider whether the current causation investigation process was working and explore if insurance policies require clearer definitions around issues such as corrosion and what constitutes damage.

Root cause analysis - exploring improvements and best practice

When a Natural Catastrophe strikes, investigations into the cause of the loss or damage typically aren't required, however for the majority losses in the Upstream Energy an investigation into the root cause of the loss is essential for both the Insured and their Insurers. In some cases, cause is readily apparent so limited further work needs to be undertaken. In other cases much more involved root cause analysis is necessary to determine more precisely what caused the loss or damage, whether there is an admissible insurance claim and, if so, to what extent.

With Oil and Gas companies in the Upstream Energy Sector constantly pushing technological boundaries, operating in ever deeper waters and in more remote and hostile environments,

conducting a root cause analysis can be inherently challenging; for example, requiring specialist vessels and being dependent upon the right weather conditions to inspect the damaged equipment.

This brings complexity, cost and delay to the claims handling process, with no guarantee that the insurance claim will be recoverable. It's easy to see why Insurers and Insureds aren't enamoured at the thought of potentially spending millions of dollars to undertake a root cause analysis, especially when, for Insureds, there's no guarantee those costs will be recovered or the claim itself indemnified.

Appoint a single expert

Michael van Bergen, Claims Consultant, Marsh, suggests "those losses where the Insured and Insurers appoint multiple experts can often become more contentious and add extra layers

of complexity, especially when you consider multiple parties investigating proprietary information and assets, with varying scopes of work and agendas, and where we need them to, at least, come to complementary conclusions."

Whilst there might be a good argument for all parties to agree at the outset to be bound by the decision of a single expert, Jonathan Blackstaffe, Oil Rig Technical Lead, AIG warns "this option can cause nervousness that the root cause analysis will not meet your expectation and you will not be comfortable with the integrity of the investigation."

Appointing a single expert would not always be appropriate. Insurers may, for example, have opposing views to those drawn by the Insured or be reluctant to share cost, when in their consideration the loss seems highly likely not to be covered. However, Alan Long, Executive

Director Natural Resources, Willis Towers Watson believes “that working with the Insured’s own investigation findings would most certainly reduce the frequency and amount spent by Insurers undertaking root cause analysis and ultimately stop unnecessary and frustrating delays in the claims management process.”

Sam Foster, Regional Manager Middle East & Africa and Offshore Energy Lead, Integra Technical Services, believes “having a single expert in certain scenarios can be helpful, as it brings speed and clarity to the process. Insurance Brokers can play a key role by encouraging the Insured to get the Loss Adjuster involved in the investigation as early as possible and ensuring that the Insured makes the process as transparent as possible.”

When the Loss Adjuster can agree the claims strategy before key decisions are taken, it allows them to play a pivotal role between the Insured and Insurer - agreeing the scope of the root cause analysis, potentially organising for costs to be shared and working in partnership with the Insured to assess potential engineering experts. Michael considers “this streamlines the whole claims process and lessens the work for the client, meaning they are less inclined to become frustrated by the claims process. The alternative is that the Insurers are always playing catch up and if they don’t agree with the work carried out they are left with little choice but to appoint their own experts, which can delay the claim by months, or even years.”

Narrow the RCA scope

Controlling the scope of the expert review has time and again been seen to speed up the claims resolution. Without clear instruction, experts can go into molecular levels of detail, searching for deeper reasoning as to the cause of the loss or damage when it is not needed.

There can, also, be a tension between what Insurers’ Risk Engineers want to see in a root cause analysis and what those handling the claim need, to confirm how the policy will respond.

Charles Bush, Head of Property, Energy & Construction claims, Zurich Insurance concurs “where the policy is ‘All Risks’, we should just be trying to establish whether any exclusions apply. Once you can confirm the claim is covered then the claims process should move along to considering the scope of damage and what the policy is going to indemnify the Insured for.”

When an incident occurs, the Insured’s own processes invariably trigger an investigation to identify lessons learned and actions for the future. Alan would like to see “the Loss Adjuster working with the Insured’s own incident investigation, bringing their expertise to the team and ensuring that an area of the report is devoted to the Insured’s views on the likely cause and the necessary requirements of Insurers, with that part of the report shared so that Insurers can determine policy liability.”

If the Original Equipment Manufacturer is involved it is virtually impossible to be part of their causal analysis as they keep their ‘intellectual property’ away from the commercial insurance market. Sam considers that “this can be further complicated by the requirement for the Loss Adjuster to sign Non-Disclosure Agreements to even read the root cause analysis report produced, which can handcuff the Loss Adjuster from reporting to their principals.”

Pragmatism

With subsea infrastructure installed in depths of over 10,000 feet (3km) of water, where the pressure is around 4,400 psi / 300 bar, recovering damaged equipment

in order to determine the proximate cause of the failure can sometimes neither be technically nor commercially viable. Mobilising expensive vessels and equipment with experts having to remain on board during the investigation can quickly escalate costs. The Insured could potentially be committing a sum of money that could be equal to or more than the potential claims recovery or, if their policy includes a Claims Preparation Clause, it could significantly increase Insurers’ exposure to the loss.

In these circumstances, it’s important to take a pragmatic approach and this often means all claims stakeholders sitting down and working through the options. Sam suggests “in our experience the Insurers, Insurance Broker and Insured are usually keen to come to an agreement that prevents prolonging the claim and damaging long term relationships. Protocols for this can be put in place before the event, which have been shown to significantly improve the claims process”.

Charles adds, “Like some of the other Insurers, Zurich advocates pre-loss workshops with their Insureds and involving Insurance Brokers and Loss Adjusters to work through hypothetical claims scenarios. We find they build trust and allow open discussion and agreement as to what the different parties will do and how they will behave when faced with such decisions.”

Many would rightly question whether this commercially driven approach is sufficiently robust when you have a USD50 or USD100 million loss. Charles is of the opinion that “these workshops are a start, and are clearly not going to provide all the answers. The only way to be completely confident would be to fundamentally restructure the insurance policy, such that there was no longer the scope to debate policy clauses and definitions.

04 INSPIRATION

Toward a claims protocol?

Root cause analysis remains hugely challenging because ultimately the concluding five lines of a 50 page report defines whether a client has a claim or not. Sam believes “a market wide protocol that confirms how root cause analysis should be carried out would be a major step forward. The aim would be to engage all the various types of stakeholder to produce best practice guidance to streamline the root cause analysis process and make it better for the Insured and Insurers,”

Fresh from the inaugural Mining Insurance Group Conference (MIG) (pages 20 and 21), Leo Dixon, Chief Operating Officer, Integra Technical Services points out that “The Mining Sector looked to the Lillehammer Terms of Engagement (LTOE) to help them draw up a Claims Protocol. Ultimately the MIG Board sanctioned a Claims Protocol that tackles this issue and others in the claims process that had historically caused disputes. In doing so the MIG Claims Protocol goes further than LTOE, in that it goes beyond what is expected of the Loss Adjuster, providing guidelines for each of the claims stakeholders (Insureds, Insurers, Insurance Brokers and Loss Adjusters) to collectively navigate and resolve the potentially difficult issues that polarise opinion and that, ultimately, can have a negative effect on relationships and brands.”

To agree a market wide approach to root cause analysis in the Upstream market would be challenging, not least because there is significant difference in the scope of investigation as between an incident on a fixed or floating object and one to subsea equipment that is fixed to or trenched under the seabed, but this may not be something that’s insurmountable with the support of the market and broking communities.



Jonathan Blackstaffe

Oil Rig Technical Lead, *AIG*



Charles Bush

Head of Property, Energy & Construction claims, *Zurich Insurance*



Leo Dixon

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Sam Foster

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Alan Long

Executive Director Natural Resources, *Willis Towers Watson*



Michael Van Bergen

Claims Consultant, *Marsh*

Reducing policy wording ambiguity

Upstream Energy Insurance Policies have traditionally tried to exclude losses arising from corrosion, but in recent times wordings have been drafted that refer to terms such as ‘accelerated corrosion’, ‘unexpected corrosion’, or ‘corrosion as a cause or a consequence’. Whilst the intent of these redrafts was to create clarity, if the newly introduced terms are not clearly defined, they can create further ambiguity, perhaps leading to claims outcomes not meeting Insured’s expectations.

Jonathan suggests “it’s actually often simple: did the corrosion get caused by something that’s covered or not? If the corrosion is a consequence of some covered loss then you pick it up and if it’s not you don’t. Charles agrees “I think corrosion is one of these things where people have a tendency to talk about it a lot but, in reality, I do not consider it to be as much of an issue. I remember Sam saying that everything corrodes at the speed it should corrode given the environment which it is in. So arguably is there such a thing as accelerated corrosion? I think the move to ‘expected vs unexpected’ corrosion is one way of addressing this, but I agree with Jonathan that corrosion is more often than not the consequence of something else that has happened and would, therefore, likely be covered under the policy.”

The trouble is that not all insurers approach the subject in the same manner. According to Michael “some insurers often look to deny claims involving corrosion entirely, from the outset, rather than putting some attention to understanding the potential fortuities upstream of the corrosion.”

One stream of thought that came out of the Lillehammer Energy Claims Conference in 2012 was to remove ambiguity by having an absolute corrosion exclusion and then offer the Insured the ability to buy back cover. Whilst many Insurers, Insurance Brokers, Insureds and Loss Adjusters would agree that this would be a sensible approach, with the continued soft insurance market there is little appetite to change policy wordings.

There are other similar discussions that arise in Upstream Energy loss scenarios, for example, relating to definitions of what constitutes damage. In Michael’s experience “more sophisticated insurers would conclude that it is the inability to use the insured property as intended or put another way, its loss of usefulness.” A good example for testing this interpretation is the ‘stuck pig’ in a pipeline loss scenario. Sam concludes that ‘in this circumstance there is quite often no damage to the pipe and no damage to the pig, but the pipeline cannot be used for its intended purpose, which can lead to further consequential losses for the Insured’. Are the costs to remove the pig recoverable under the material damage

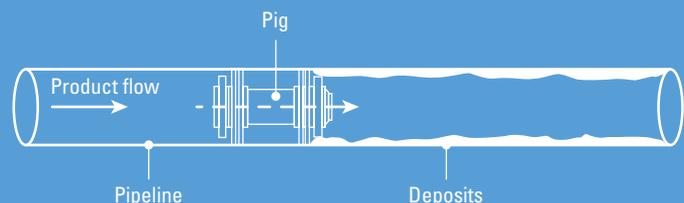
section of the policy, or, taking it to the extreme, are the costs to lay a new pipeline recoverable? If the Insured buys Loss of Production Income cover (LOPI), has the material damage proviso been satisfied in order to trigger the LOPI cover?

Ambiguity in policy wordings would seem to be a feature at least for the foreseeable future, especially as there is a case to be made that this often benefits Insurers, Insurance Brokers and Insureds alike. Besides, the very nature of Upstream Energy means that there will always be losses that are novel, and if these are large and complex enough, the wording will come under scrutiny.

This places an increased emphasis on the Loss Adjuster’s knowledge and experience. They need to be able to skilfully navigate the claim from ‘cradle to grave’ - from the damage assessment and root cause investigation, through the policy analysis and ultimately the audit and adjustment of the claim – working alongside a pragmatic Insurer whose first consideration is whether the loss triggers the policy, as opposed to how the claim can be denied.

Did you know?

Pipeline ‘pigging’ is undertaken for a number of reasons, for example: to remove unwanted materials, such as wax, from the line; to examine the pipeline from the inside; to plug or isolate certain areas of the line; or to apply chemicals to the inside of the pipeline.





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