MARSH JLT SPECIALTY

QUARTERLY NEWSLETTER | APRIL 2020

Energy and Power Newsletter

Focus On: Decommissioning Security Solutions in the UK and Dutch North Sea

MARSH

We are pleased to provide our second Energy and Power Insurance Quarterly Newsletter of 2020.

During these difficult times, we want to make sure all our clients are kept as up to date as possible with developing issues in the Energy & Power insurance sector. In this edition, we specifically look at the evolving and transitioning Directors and Officers (D&O) market place, which we believe will be of interest and value to our Energy & Power clients.

In addition to this, and to our regular features, we have included a ‘focus on’ **Decommissioning Security Solutions in the UK and Dutch North Sea.**

In line with government restrictions and guidelines, many of our Marsh JLT Specialty colleagues around the world are working remotely for their health and wellbeing, as we know are many of our clients and insurers. Importantly however we continue to be fully operational, and are striving to continue to deliver the high standard of service or clients demand, and have come to expect from us.

Our thoughts are with you, your families and your businesses at this time.

We hope that readers will find this newsletter interesting and informative and would welcome any feedback you may have, which you can email to: john.cooper@marsh.com or pass on to any of your usual Marsh JLT Specialty contacts.

If you are reading this in hard copy, or have been forwarded it electronically, and would like to be added to our electronic mailing list, or you wish to unsubscribe, please email john.cooper@marsh.com

John Cooper ACII
Global Chief Client Officer
Marsh JLT Specialty | Energy & Power

Energy and Power Newsletter

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General State of the Market Overview

General Backdrop

The Energy and Power insurance sector was already going through a stage of transition prior to the current Coronavirus pandemic and resultant financial market impact, with contraction of capacity and substantial rate rises prevalent in varying degrees in Downstream, Power, Renewables and Casualty sub-sectors. The exception to this state of play was the Upstream class, which unlike the other Energy and Power classes had not seen a run of large losses erode or eliminate profitability, and the inevitable withdrawal of capacity that follows such a position.

The big question now is what impact will the COVID-19 have on the financial health of the insurance industry in general, and what knock on effect will that have on the Energy and Power insurance sector?

With the information available at this stage as to the duration of the event, we cannot currently answer this with any certainty, but it is already having global repercussions that we have not seen since 2008/9 and 2001, and there is a likelihood that we will see a substantial shift in insurance capacity and premiums.

General insurers (who provide significant amounts of capacity to the Energy and Power sector) may face not only from a still unknown quantum of claims that will no doubt result from the pandemic, but also from the impact on their own valuations, and the impact on their investments.

Partially due to the impact of the pandemic on demand, and partly due to a production war between OPEC and Russia, global oil prices have collapsed (oil prices fell over 60% in a few weeks pushing prices to their lowest levels in 18 years). This will not only have a significant bearing on oil and associated service sector companies, but it will also impact the available premium pot for Energy Insurers, with cancellation of drilling programmes and construction projects, and reduction in property and business interruption values all being likely outcomes.

The other big unknown is how long the current crisis will last, and how quickly industry and economies will bounce back, but in the meantime we should all be prepared for a period of turmoil in both the Energy and Power industry and the insurance industry that supports it.

As the current pandemic gathers pace, many markets are working remotely and implementing systems designed to support large numbers of people working from home. Many insurers have been geared up for remote working for some time but the challenges are not being underestimated. We are all focusing on keeping service standards high and ensuring our clients' needs are met. The travel freeze will provide benefits in terms of freeing up valuable time to complete marketing and process placements, and market briefings are being circulated electronically.

The markets have largely been supportive to client requests with the uncertainty surrounding the duration of the prevailing conditions - short term extensions may be considered but are not the ideal answer. Due to a myriad of technical underwriting difficulties in most sectors, pricing conditions and a general ramping up of workloads, most clients prefer an early approach to the market to ensure renewals are completed on time.

As a result of the current environment, we are now seeing new Coronavirus and other communicable diseases clauses and exclusions being generated by insurers. There is little consistency across market, probably as result of the haste in releasing such clauses. From the perspective of the clients and their brokers, such clauses require further consideration regarding the detail of the language to avoid potential difficulties and legal challenges in loss scenarios.

Further impacting specifically Downstream and Midstream renewals is the postponement or cancellation of most engineering survey visits which has a significant effect on underwriting assessments. However, meaningful value can still be created by doing desktop studies and virtual interviews (see Engineering in the Current Crisis later on in this edition). In addition to this, further challenges lie ahead for the introduction of loss adjusters to any claims scenario involving physical attendance at a loss site; it is important that clients and brokers manage this process to ensure there is clear communication and agreement with insurers so positions are not prejudiced.

Upstream Energy

For the Upstream sector, the savage downturn sweeping through the industry in mid-March 2020 is expected to exceed the trauma of the 1985, 1999 and 2014 oil price crashes.

Clients are having to deal with an abundance of issues; any one taken in isolation would be challenging but the combination will result in an existential crisis for some: Coronavirus, Saudi-Russia supply surges, the shock to the world economy, a loss of confidence by Wall Street / the banks / private equity in the oil and gas business model, climate change, renewables and electric cars are providing unprecedented trials for our clients.

Generally, the insurance market acted responsibly in the last rapid descent in the commodity price in late 2014.

It is likely that this time too, insurers will recognize the stress on their customers and reflect reductions in exposure with lower premiums. CAPEX dedicated to drilling wells will be reduced, reducing revenues will be used to calculate loss of production income numbers, and more laid up rigs will all drive significantly lower pricing. Other than for Gulf of Mexico windstorm, we today have the most capital and highest level of coverage in the history of the upstream market. In fact, in the new year we saw a healthy uptick in available capacity. However, the new premium base may not support current limits purchased so we are likely to eventually see reductions to current capacity levels.

Additionally, attritional losses have spiked in the sector. Over the last nine months three offshore blowouts with costs of USD 50 million plus have occurred and two onshore US shale blowouts occurred with redrilling authorisation of expenditure totalling circa USD 100 million. The result is that Control of Well as a class is unlikely to make money for underwriters this year. There has been a run of offshore drilling units having accidents, the most high profile being the dropping of a blowout preventer in Angola. This is therefore another class which may be in negative territory. Onshore North American risks have produced plenty of losses resulting in steeply increasing premiums levels and the offshore CAR sector is showing an above average number of loss advices.

However, incumbent leaders have generally been setting 2.5% rises on renewals. The surplus of capacity needed on most policies has meant most markets are continuing to compete for their preferred signed lines, with the addition of Convex to the market this year adding to this trend. On the larger USD 10 million plus premium accounts, we have in fact seen fierce competition for the leadership which in some cases resulted in like for like reductions being offered.

Although there is likely to be weakness in insurers' profitably, it is trumped by extreme circumstances impacting the oil patch. The insurance sector from 2014-2019 did not in any way suffer in the same way the oil and gas industry did and this fortunate position should now be remembered by underwriters as insureds revisit the challenges of 2015-16. We therefore believe that in 2021 many companies will be under pressure to withdraw upstream capacity to manage potential volatility there due to the declining premium levels.

Downstream Energy

As we conclude first quarter 2020, rates have continued to move upwards. Notably clients renewing in this quarter had already seen upward rate movement in 2019 and as we progress into the second quarter, the rate movements will likely compound the pricing impact for the corresponding period last year. This is pushing insurers into the target levels of rate sustainability quicker than originally anticipated.

At this time, rating entry points for Downstream on established business are plus 30% but with some risks transacting considerably above that. Midstream business continues to be treated with a marginally lighter touch but this treatment depends on risk profile, whether the risk falls into the Upstream market, the Downstream market or the Ports and Terminal market. Midstream risks that encompass fractionation will likely find their way into the Downstream market and be treated with more severity than those limited to storage and gathering systems, which can be accommodated within Upstream. Nevertheless, nothing is quite as simple as it seems and direction can easily be skewed by the likes of Nat Cat requirements, Lenders' requirements, retention appetite etc.

Whilst insurers concentrate on correcting rates there is also considerably more focus being brought into understanding clients' methodology of asset valuations and the volatility of their earnings. Insurers may no longer be as accepting of declared values at face value and a considerable swathe of the market will likely look to impose Business Interruption (BI) volatility clauses outside of clients whose revenues are fixed, based on tolling or 'take or pay' arrangements. Additional grants of coverage and respective sub limits are coming under pressure, and retentions are now back in play either to mitigate increased cost or to attract capacity.

As the market tightens up, coverage extensions such as Cyber resultant physical damage are being heavily trimmed in terms of scope. Singleton refiners are falling short on critical market mass and as a result are particularly challenged on both pricing and capacity. Capacity continues to leak and the market lost a valuable MGA insurer in January when their capacity provider withdrew across a number of classes. There has been real difficulty in achieving completion of some programs, which has required a combination of very clear thought and relentless marketing. Nevertheless, as rates accelerate the market is becoming a real opportunity for capacity that has either not previously participated in this space, or remained shelved for the last number of years, and it is likely that this opportunity will be seized upon in the near term. Meanwhile there has been acute sensitivity from insurers to any unplanned incidents with a number of potential losses in the first quarter particularly relating to refineries. Nevertheless, with the exception of two such incidents in the Far East and Southeast Asia the others appear to be negative optics more than actual substantive negative impacts to the market. As such, insurers are in a better place at this point of the calendar than they have been for some time.

On a final note, it should be recognised that although insurers within the Downstream and Midstream space have endured challenging times over the past three to four years, their customers have now entered into their most challenging period in memory, with market dynamics and investor sentiment moving against the hydrocarbon industry. It should also be recognised that this customer base does not have the luxury of diversity afforded to insurers writing multiline classes of business.

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Power

We are amidst a sustained market correction in the Power and Renewable sector with the market pulling most of the levers at their disposal such as narrowing problematic coverage (for example, catastrophe coverage), a focus on deductibles (in an attempt to remove attritional losses), and a firming up of rates. We are seeing an average of 20% added across the portfolio for a clean renewal, and perhaps more for a troubled account with losses.

A good broker can help mitigate such increases by re-layering or restructuring a programme, but we forecast that this market correction will last for the remainder of the year and perhaps beyond, as carriers go through their own treaty renewals.

Traditional Power

As we continue into 2020, the positioning of the market remains as challenging as it has been for the past nine months. The restructuring of programmes is now commonplace, with many vertical placements being used to mitigate the impact of the hardening market conditions. The placement process is taking longer due to incumbent carriers reducing their shares and lead markets delaying the quoting stage to try to drive up their price. Road shows (now virtual), recent engineering reports and demonstrating the clients' commitment to continual improvement to risk management, are crucial in avoiding the worst for tough market conditions.

Straightforward renewals with a clean loss record and no natural catastrophe (CAT) exposures are, on average, experiencing increases of around 20%. Accounts that have CAT exposure or losses are taking more, along with the shortening of policy coverages and increasing deductible levels. Whilst a potential solution has been to seek market capacity internationally, the knock on effect from London is starting to see rates and terms align globally. We are also seeing the London markets restricting cyber coverage by replacing the NMA 2914 with the NMA 5400. Clients, particularly in the US, are pushing back as their local markets are still prepared to grant NMA 2914 coverage and London markets are at risk of losing orders locally.

Many markets will not consider new business if recent engineering reports are unavailable. Similarly, Underwriters will look to present to upper management on how they can justify writing new business in the absence of previous budgetary pressures. In some cases, even renewals require a referral to management, if certain criteria such as loss history or technical pricing are below pre agreed required levels. Buyers can also consider reducing the size of the limit they buy, to help keep down the premium level.

Our recommendation is to enter preliminary discussions with markets as soon as prudent to avoid last minute rushed negotiations. Insurers are taking significantly more time to review schedules and they may delay quoting until very close to inception, often resulting in frustration for brokers and clients. Above all, clients should be prepared for a change in terms.

Renewables

The Renewables market has undergone a significant period of hardening and market adjustment during the first quarter. The market has struggled consistently for a number of years and subsequently insurers are under increasing pressure to return to profitability this year.

Terms and conditions have changed significantly across all asset types along with increased pricing for both renewing operational risks and new construction risks. High CAT-exposed projects have seen particular focus from the market, with CAT cover becoming very limited and premiums increasing because of the recent rise in extreme weather events. Meanwhile, new CAT perils, such as hail and wildfire, are being specifically identified by insurers and subjected to increased deductibles and pricing. Hail cover, in particular, is proving challenging and clients with projects in areas with likely hail exposure should begin renewal discussions as early as possible.

In the Offshore Wind space, as developers seek to enter new territories, over the past few years many have identified East Asia (specifically Japan, China and Taiwan) as an area of great opportunity. Rapid expansion in this region has meant that many insurers are encountering issues around aggregation due to the CAT exposure, specifically typhoon and earthquake. We expect that this issue will intensify as increasing amounts of projects continue to be constructed in the region. Meanwhile, as Europe continues to establish itself as the global hub of offshore wind, the US clearly presents the next significant future growth area for the Offshore Wind industry.

Other notable areas of focus for insurers have been out-of-warranty wind turbines, which have incurred both increased deductibles and limited defects cover, and biomass projects, which have seen an unprecedented retraction in capacity leading to a sudden increase in pricing and retention levels.

Insurers have also looked to include a 'micro-cracking' exclusion clause on Solar PV placements due to recent market losses as a result of this exposure.

In order to mitigate the effects of this market shift, we suggest that clients begin their discussions with ample time before renewal to ensure the best possible result. Clients with significant CAT exposure, equipment moving out of warranty or prototypical technology should be particularly aware of this and it will be important for clients with these risk profiles to prepare for a change in terms. Given the variety of stakeholders involved in many of these projects, such as lenders and financiers, it is important to manage expectations and prepare all stakeholders (both internal and external) for this adjustment.

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Energy Casualty

US energy casualty continues to harden, with some syndicates (especially those who write US general casualty) looking for 20% plus in terms of rate. The pure offshore/marine writers are more content with 10-15%, but the highest common factor often wins.

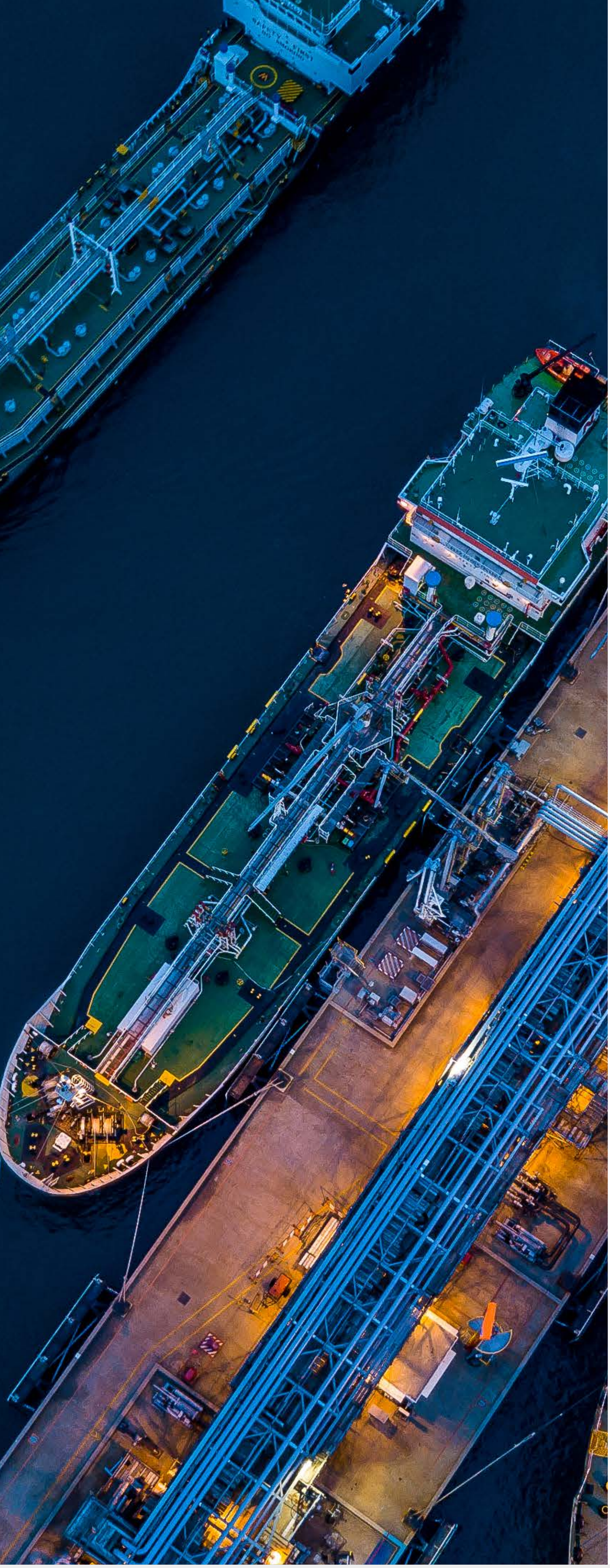
The absence of a London lead umbrella continues to be keenly felt by our clients, with the US markets not filling that vacuum as readily as previously expected.

Canadian risks are proving more and more challenging with Lloyd's looking for a 25% PRI (Price Rise Index) increase from the International Casualty books of syndicates, which in theory should be on top of exposure increases, for capacity approval and business planning. The Canadian domestic market is coming into play more than it had previously, but this is not an endless resource for retailers to fill gaps with.

International (non-US and non-Canada) continues to be the most distressed and altered from expiry sector. Reductions in capacity as well as changing internal protocols within some carriers mean that rises can be unpredictable and inconsistent.

As a very rough rule of thumb, an integrated up and downstream quota share programme in layers might have previously expected the USD 100mm excess of USD 400mm (assuming a tower limit of USD 500mm) to go at between USD 1,000 and USD 2,000 per million - now that would be between USD 3,000 and USD 4,000 per million.

Insurers are prepared to walk away, as they look set to meet income targets for the year.



Marine Exposures

As we head into the second quarter, the problems facing the Marine Insurance market continue. Reduced capacity and enhanced scrutiny of risk are now commonplace with risk selection being key. Many underwriters are insisting on their pricing levels to commit capacity and we are also seeing a challenge to the traditional lead and follow tradition within the subscription market, with some following capacity not supporting lead terms, instead opting to quote their own terms for their capacity.

There is good news however, for those Hull accounts with excellent records, as these can still attract favourable terms. Underwriters want to ensure they retain their key accounts, but outside of those stellar accounts, those with average to poor records are certainly seeing significant premium increases and restrictions to coverage.

The review of the Lloyd's syndicates continues, with most carriers having to re-submit their plans to ensure they are staying on track. Most carriers are also mindful of claims deterioration in the 2019 year of account, which is yet again looking like an overall loss-making year.

The cargo market, which has seen the most dramatic reduction in capacity, has now been hit with another large loss, at a computer factory. Whilst it is still too early to predict, the numbers being suggested will have a significant impact on this book in the coming months.

The marine liability market remains steady however we are now starting to see rises becoming commonplace due to adverse claims being reported.

The cargo market, which has seen the most dramatic reduction in capacity, has now been hit with another large loss, at a computer factory.

Middle East Market Update

The mix between international carriers, indigenous market and managing agents has always sustained a dynamic market in the Middle East. The growth of the market from 2010 to 2017 was the result of a broadening remit for the domestic cedants as they transitioned to writing international portfolios coupled with the growing number of branch office openings from international markets. It is not surprising that a market where Specialty classes are so dominant would see some significant changes in line with the volatility we are seeing globally.

The hub of international carriers based in Dubai's International Financial Centre has always been fluid with new market entrants and departures and a general restructuring of appetites and authorities. This process of change has been highlighted by the recent decisions of two major carriers to realign their regional and/or product line strategies.

- **AIG –** following a prolonged period of speculation AIG have confirmed the reorganization of their Specialty lines around two hubs; London and North America. With this decision the Energy, Power and Construction lines currently underwritten from their Dubai office will move back to London effective 1st May 2020. It's likely that a member of their regional team will remain in the office to handle the run-off until 1st May 2021. AIG's Dubai office will remain open for General Property, Casualty and Financial Lines.
- **Allianz –** whilst they re-domiciled their Energy underwriting back to London in 2017 Allianz had continued to be a market leader in Power, Construction and Casualty. Earlier this month Allianz decided to close their Dubai operation and will cease underwriting on 1st May 2020 with the office closure planned before the end of the year.

Following a similar move from Swiss Re in 2019 the common perception of the regional market is that it is in decline, however the complex mix of carriers trading from the region ensures that it is robust enough to withstand even the most major international carrier departures. Certainly we see the changes in the region mostly as a reflection of the continued volatility in the specialty markets – particularly Energy.

The increased focus on costs in such an environment inevitably leads to consolidation and retrenchment back to headquarters. The profile of the indigenous carriers continues to develop and whilst international carriers come and go, the regionally headquartered markets remain the defining feature. Carriers such as Oman Insurance, ADNIC, Emirates and Orient continue to play a significant part on Energy and Power risks both within the region and into broader Afro-Asia. In Qatar, QIC and Al Koot having considerable Energy appetite and in Kuwait, Al Ahleia and Kuwait Re provide useful support capacity. All of the aforementioned, whilst limited in their geographical scope outside of MENA, can offer capacity across the oil and gas value chain and into power generation and construction.

Added to this regional capacity are relatively new Managing Agents such as Arma (with Hiscox paper) and Aspire (part owned by Oilfields and with a consortium of Chinese backers) both of whom bring new capacity to the region in so much as their backers cannot be readily accessed directly – similar to the established Elseco who took over Lloyd's-backed outfit Malakite in 2019.

From the shrinking pool of international carriers, market cornerstones like Liberty and Zurich have prevailed and are complemented by new entrants like Berkshire Hathaway Specialty and Korean Re who continue to grow.

In the current climate of uncertainty, it is unwise to make any projections but the status quo in the Middle East, despite the recent changes, sustains a broad and diverse selection of carriers for our clients to consider.

Recent Quotes

The following are 'sound bites' taken from speeches, statements or articles by prominent market figures about the insurance market and whilst we have tried not to take their words out of context, the excerpt may not be the entire speech or article.

Pat Regan, QBE CEO

"The impact of the recent Australian bushfires is genuinely apocalyptic. I question whether any insurance company genuinely understands the full impact climate change will have on its portfolio. It's hard to be absolutely sure; it's probably foolish to say you are absolutely sure. The insurance sector will play a key role in helping to provide climate change solutions. I do think we have got almost an obligation to play a significant role in helping grow renewable energy across the world."

Speaking at the Insider London conference in January 2020

Andrew Horton, Beazley CEO

"The London market has experience of dealing with claims inflation and should be prepared to respond to step changes in liability claims patterns. A couple of years ago nobody mentioned social inflation in their earnings, whereas in the last quarter it was a major theme. I find it slightly odd that we are calling claims inflation – which happens on a regular basis – 'social inflation'. In casualty books you tend to see step changes in claims and we should be thinking about that."

Speaking at the Insider London conference in January 2020

Richard Trubshaw, Managing Agency Partners (MAP) active underwriter

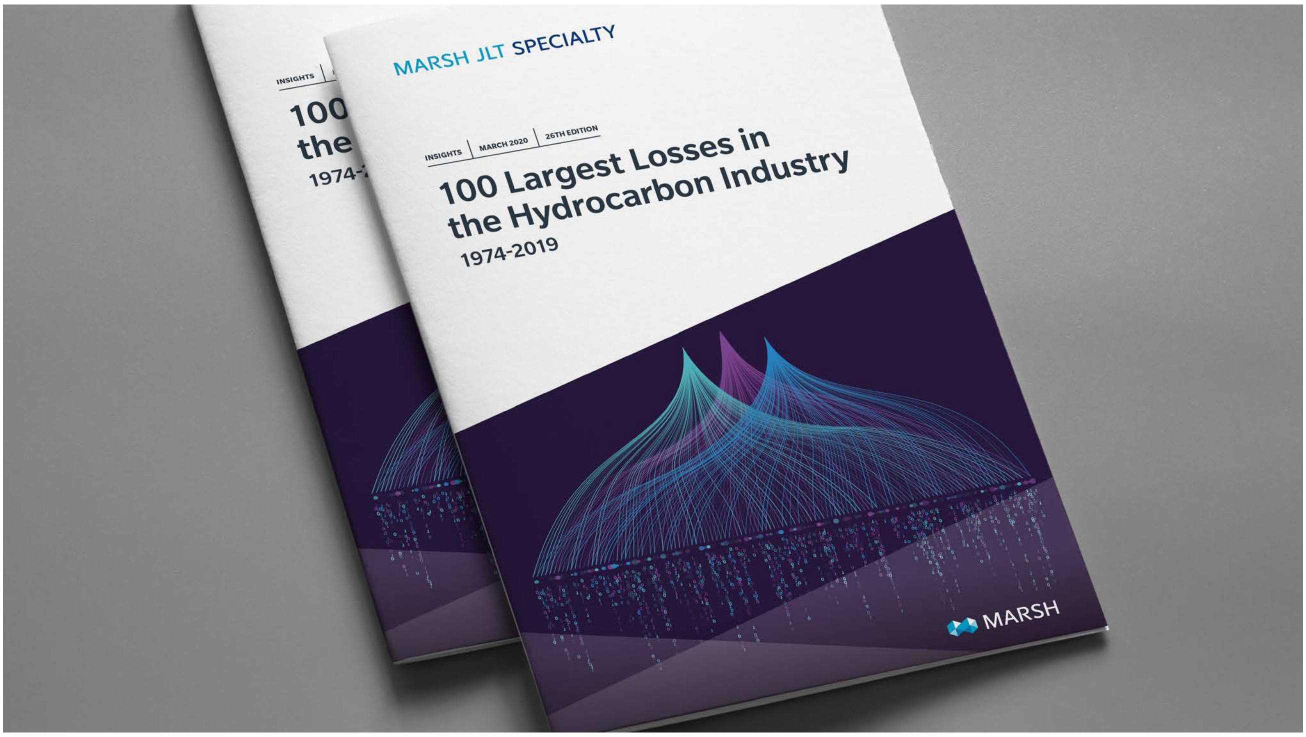
"The worst-performing syndicates in Lloyd's have pushed the market further into downturn by pandering to brokers, and improvements are now only being driven by the more disciplined carriers in the market. The fourth quartile have really fuelled the downturn in the market by prostituting themselves to brokers and have only seen improvements because more responsible carriers have stepped in and repriced the business. The last thing Lloyd's needs is for them to start wooing the brokers again. While Lloyd's is alive to the market impact of some of these weakest players, its management appears to not fully recognise the damage done by some members of another cohort. There's a slightly rogue second quartile that needs to be policed. They are trying to lead everything and outburn rivals through internal reinsurance. Both categories are the antithesis of the traditional Lloyd's subscription market - neither of them are playing ball. Lloyd's must maintain market discipline or risk exterminating the nascent rating upturn. Hopefully they understand that the market is only improving because capacity has been restrained: should the handbrake be released, then too many businesses will carry on regardless and the market improvement would be still-born. Almost 90 percent of the market is foreign-owned and you don't have that alignment of interest that we epitomise. You don't have that concentration of culture, of people, of ownership – not just financial ownership but responsibility for your actions."

In an interview with Insurance Insider in March 2020

The quotes referenced above are included herein to provide readers with a broad overview and insight into what is currently being said in the marketplace, however the inclusion of such does not mean Marsh JLT Specialty, Marsh, or Marsh & McLennan Company endorse or agree with any of the foregoing.

Market Moves / People in the News

- **Mike Kolodner** has joined Marsh JLT Specialty as our Renewable Energy Leader for US. He will join from Nuclear Energy Insurance Limited (NEIL) mid-April and will be based out of the Philadelphia office.
- **Sarah Baldys** will rejoin Marsh from NEIL.
- **Jon Hancock** Lloyd's Performance Management Director, is to leave the corporation and join AIG as their CEO of international general insurance operations. John Neal, Lloyd's CEO, is to step into the role of interim Performance Management Director.
- **Sarah Stephens** has been appointment of Head of Cyber, International, for Marsh JLT Specialty. Sarah will continue to be based in London and will assume the additional responsibility of the newly created role in addition to her current responsibilities as cyber, media and technology leader within the UK FINPRO practice.
- **Lee Ackerman** who left Liberty when they closed their energy general liability book, has been employed by Apollo where he will be working as senior underwriter in their US casualty team.
- **Daisy Thompson** who left Liberty when they closed their energy general liability book, has been employed by Hiscox.
- **Dervla Lynchahuan** has left Kiln's casualty team to join Convex.
- **Raoul Carlos** Arch Insurance's international onshore energy head, has moved to MGA Castel Underwriting Agencies, recently acquired by Arch.
- **Hannah Hutton** has assumed management of the onshore energy business at Arch, reporting to Jake Gibbs, who has been promoted to head of marine & energy.
- **Jane Hayes** has been appointed underwriting director at the Lloyd's Market Association (LMA). She joins from Zurich Insurance, where she was chief underwriting officer for Europe, the Middle East and Africa.
- **Julian James** has been named Sompo International's leader of London market and international operations.
- **Julian Samuel** has joined MS Amlin as head of natural resources.
- **Andy Lane,** ex Tokio, Skuld and Markel equipment underwriter has joined Berkshire Hathaway Specialty Insurance.
- **Peter Bilsby,** ex-CEO of Talbot Group has left his position as head of global specialty at AIG. He will be replaced, on an interim basis, by global head of energy and construction Gordon Brown.
- **Nick Salter** has joined Bowring Marsh as its new head of mining & metals, strengthening the team and bringing a wealth of expertise. Nick joins from Price Forbes where he established and led their mining and metals team.
- **Greg Hendrick,** Axa XL CEO has left the firm with immediate effect. He is replaced by Chubb's Scott Gunter, who was senior vice president at Chubb and president of their North American commercial insurance unit.
- **Mike Southgate,** formerly with Canopius has joined Hiscox as divisional head of marine and energy.
- **Peter O'Neill** has been promoted to UK head of downstream energy and power at Axa XL, replacing Peter Welton who was promoted to UK head of energy last October.
- **Fergus Fergusson** has joined Hamilton Insurance Group from Aspen Insurance to be their head of excess casualty at its Lloyd's and its Dublin-based company market business.
- **Marc Sullivan** has joined International General Insurance (IGI) as the downstream energy class underwriter in its London office. He joins from Barbican Insurance Group.
- **Rory Kane** is joining Argenta Singapore, he was previously at Asia Capital Re (ACR).



26th Edition of 100 Largest Losses in the Hydrocarbon Industry

The 26th edition of Marsh JLT Specialty's 100 Largest Losses in the Hydrocarbon Industry report was released in March.

The publication continues to summarise the 100 largest property damage losses from the hydrocarbon extraction, transport, and processing industry since 1974 reflecting on the industry's history, identifying key issues and trends from large losses, and considering whether the industry is making progress in relation to plant safety.

Issued every two years by Marsh JLT Specialty, this year's report reconsiders:

- What lessons can the industry learn from the last two years?
- Is history repeating itself 30 years on?
- Does the age of a plant really matter?
- How to turn uncertainty into opportunity through organisational resilience.
- A loss-by-loss profile of each of the 100 largest losses.

Did you know?

- In the last two years, four of the new losses were among the 20-largest losses experienced to date.
- Refineries accounts for 50% of new additions in the report to the largest losses.
- The onshore oil and gas sector has experienced more property damage losses in excess of USD100 million per annum.

For a copy of the report please visit marsh.com or contact your Marsh JLT Specialty Account Executive.

What's New?

New Products and Market Developments

The Lloyd's Market Association (LMA) have issued a Coronavirus Exclusion (LMA5391) excluding any claim in any way caused by, or resulting from, COVID-19 or SARS-CoV-2; including any fear or threat of such. To what extent this is likely to imposed by the market on energy and power polices is to be seen, but your Marsh JLT Specialty Account Executive will discuss this with you prior to accepting it on any policy, should it be required by insurers.

Lloyd's has now closed its underwriting room in line with UK Government advice to avoid all non-essential contact. In an announcement, Lloyd's said "following our successful resilience test on March 13, we are confident that our emergency trading protocols will enable the market to continue trading during the closure and we will review this decision on a weekly basis." The test was the first time the room had shut in Lloyd's 334-year history.

In response to Lloyd's and the FCA 'Silent Cyber' mandates, insurers have issued a series of new Cyber clauses. For upstream, the status quo is maintained by the Joint Rig committee clause (JR 2019-14) that replaces CL 380 by using the same language as CL 380 plus simply affirming that whilst 'malicious' cyber-attacks are excluded, non-malicious cyber events are not. However, for downstream a new clause (LMA 5400) that that some insurers have said they want to replace NMA 2914/5 (the previous market standard clause providing malicious and non-malicious write back for resulting fire and explosion) only writes back accidental cyber events and still excludes deliberate cyber acts. Our continued view is resultant fire (and broader perils where on offer) resulting from both malicious/deliberate and non-malicious acts should be covered by 'All Risks' policies, and we continue to promote the use of NMA 2914/5 or will look to amend LMA 5400 accordingly.

The London Joint Liability Committee (JLC) have updated their London umbrella/claims made policy forms (occurrence claims made versions) for 2019. The occurrence version is now JL 2019/006 (19 Dec 2019) and the claims made version is now JL 2019/006 (19 Dec 2019). The JLC said in a circular that the changes were following the Deepwater Horizon Case. The main change is they are amending the joint venture scaling of limit clause from "liability of the insured" to scale, to "ultimate net loss" to scale. In a Deepwater Horizon defence costs claim, the court decided "liability of the insured" did not include defence costs and therefore should not scale to the insured's interest (where the existing ultimate net loss definition they are now using instead, specifically includes defence costs and going forward will therefore scale in the same way as indemnity does). The JLC also said in their circular that it anticipates that further work will be done in 2020.

Marine Hull has been chosen as a pilot class for Lloyd's proposed new lead and follow model (where only certain syndicates will qualify to lead certain business). There will be an LMA consultation on the plans.

The Corporation of Lloyd's has announced it will buy a 40% stake in e-trading platform PPL.

Lloyd's has announced it has established a working group to explore reviving a framework (previously devised in the late 1990s) to host captives as part of the capital element of the Future at Lloyd's strategy. The working group is headed by John Keen, Lloyd's development manager for managing agents. The Corporation has also brought in consultants from the captive space to assist with the work. Captives with Lloyd's paper would benefit from the corporation's extensive global licenses and could potentially save significant sums in 'fronting' fees.

The UK Government back Terrorism backstop Pool Re is to become a government entity. Pool Re's transfer to the central government subsector through HM Treasury (HMT) – is retroactive back to its formation in 1993. It has until now been a member-owned entity that ultimately benefits from a state guarantee, for which it pays. The change in the mutual's status will follow a one-year transition period. Pool Re called the Office for National Statistics (ONS) action a "statistical matter that does not have any direct implications in areas such as ownership, legal status, or management structure". On announcing the change, the ONS said it may also review the status of Flood Re and Pool Re Nuclear.

Lloyd's announced their 2019 results in March.

The key takeaways were as follows:

- GBP2.5 billion pre-tax profit for 2019, (following two years of losses).
- An overall underwriting loss for the year (102.1% combined ratio).
- The combined ratio for 2019 saw a 2.4 point improvement year-on-year, predominantly driven by lower major claims year-on-year, which accounted for 7.0 points of the combined ratio, versus 11.6 points in 2018.
- 2019 was third consecutive year in which investment income supported pre-tax profit. In 2019, GBP3.0 billion of investment income offset an underwriting loss of GBP500 million – bringing the market back to pre-tax profitability after two years of losses.

Specific to the energy industry:

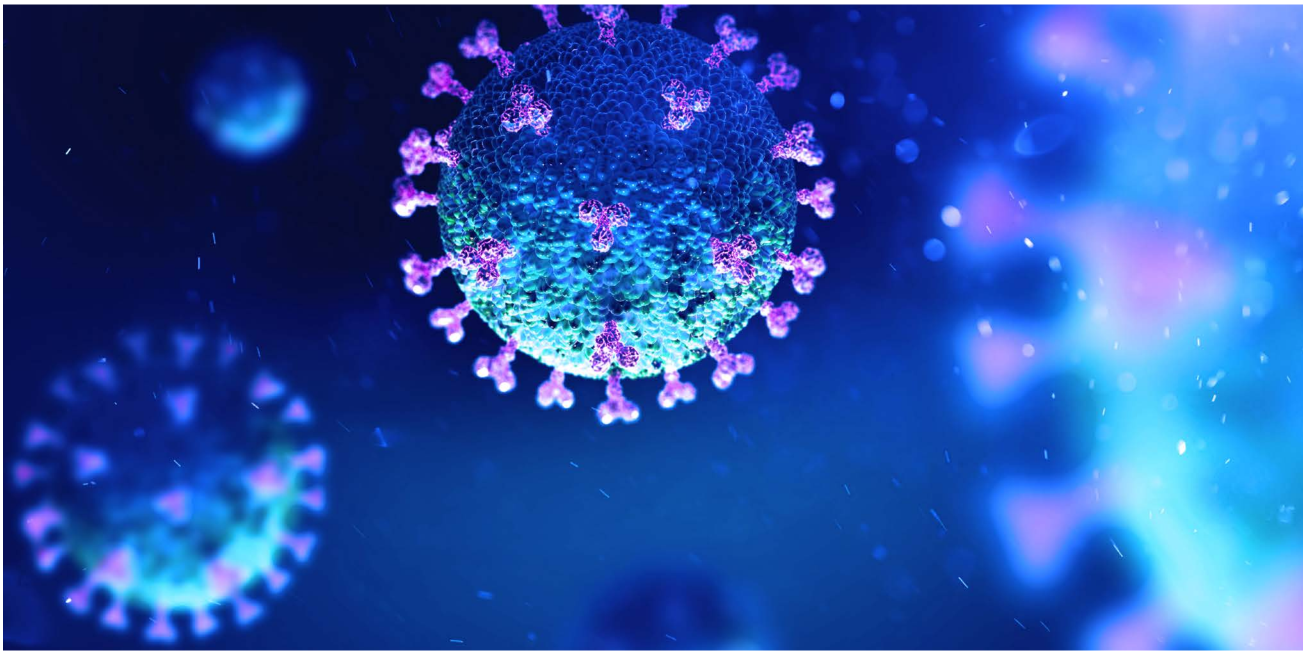
- Pre-tax profit of GBP27 million (over 75% fall from 2018's GBP113 million).
- Underwriting result 107.5% (worse than 2018 result of 105.6%).
- Combined ratio deteriorated by 9.9 points to 97.3%.
- Reserve releases bolstered underwriting profitability by 10.2 points, 8 points lower than in 2018.
- Gross written premium was GBP1.5 billion, up 6.8% from 2018 (GBP1.44 billion)

The commentary Lloyd's provided in respect to energy included:

The direction of travel in the pricing environment across all energy lines has had a positive impact on results through 2019. Continued large loss activity in the downstream lines through 2018 and 2019, specifically in the US refining sector, has driven increases in downstream property and liability rates. From a whole of industry perspective, this has been balanced somewhat by benign large and catastrophic loss activity in upstream lines, which is the largest part of the overall energy account, in terms of risk count, written premium and exposure.

The prior year movement was a release of 10.2% (2018: 18.2%). The energy line of business has seen continued prior year reserve releases over 2019. This line contains a mix of contracts that give rise to claims that are settled on both a short-term and long-term time horizon. Both the short-term and long-term lines have performed broadly in line with expectations, with the short-term lines benefiting from releases on older catastrophe losses. Given that the energy portfolio is also exposed to isolated large losses, large margins for uncertainty tend to be held and released in benign years. For long-term contracts, these margins can be held for a number of years. Reductions in claims estimates for these large losses and the release of unused margin is expected to drive releases at a market level.

In downstream energy, both property and liability, the market is has enhanced underwriting discipline and price increases are gathering momentum as underwriters react to adverse large loss experience in the last few years. Steps are also being taken to implement tighter terms and conditions, in light of losses and volatility in claims values. Upstream energy remains in a state of relative stability in terms of pricing, conditions and underwriting appetite. This is mainly driven by an absence of large losses, coupled with a benign wind season in areas of high energy asset exposure accumulations, such as in the Gulf of Mexico. While there has been a trend of increasing limits of indemnity in the sector, due to the increasing magnitude of some of the offshore complexes, there is adequate capacity in the market to accommodate these large placements.



Briefly

Due to the outbreak of COVID-19, Marsh JLT Specialty made the decision to postpone its 2020 Energy Industry Conference (EIC), which was to be held in Dubai last month, until early 2021. Revised dates will be released in near future however the insights and risk engineering research which was to be launched around the EIC will be published over the coming months.

The 2020 Global Risks Report, published by the World Economic Forum with support from Marsh & McLennan is now available from the below link. The 15th edition of the report draws on feedback from nearly 800 global experts and decision-makers who are asked to rank their concerns in terms of likelihood and impact. This year's report highlights important threads across the global risk landscape: intensifying confrontations, both between and within countries, as well as a heightened sense of urgency and emergency around some critical global problems. The full report can be downloaded from: http://www.mmc.com/insights/publications/2020/Jan/the-global-risks-report-2020.html

The ICC International Maritime Bureau (IMB) has reported that 2019 saw a fall in the amount of piracy and armed robbery at sea, whilst there was an "unprecedented" increase in kidnappings, mainly in the Gulf of Guinea. There were 162 incidents of piracy and armed robbery reported, down from to 201 incidents in 2018. Of the reported incidents there were four hijacked vessels, 11 vessels fired upon, 17 attempted attacks and 130 vessels boarded. The Gulf of Guinea saw a more than a 50% increase in kidnappings in 2019, with a large increase during Q4. The number of crew kidnapped increased from 78 in 2018 to 121 in 2019. The IMB said that the Gulf of Guinea now accounted for more than 90% of global crew kidnappings. There were no reported incidents of piracy or armed robbery in Somalia, but the IMB piracy reporting centre continued to advise that vessels and crews remain cautious when travelling through the region. The report noted that "Somali pirates continue to possess the capacity to carry out attacks in the Somali basin and wider Indian Ocean". The full report can be downloaded from: https://www.standard-club.com/media/3229418/icc-2019_annual_piracy_report.pdf

The 2020 Allianz Risk Barometer has reported that cyber incidents rank as the top peril for companies globally for the first time after receiving 39% of responses from more than 2,700 risk management experts in over 100 countries and territories – the largest number of respondents ever. Seven years ago cyber risk ranked only 15th with just 6% of responses. After seven years at the top, business interruption (BI) drops to second position (37%). However, the trend for larger more complex BI losses – from both traditional causes, such as fires and natural catastrophes, as well as newer causes, such as technical issues with digital supply chains and platforms or even civil unrest, continues unabated. Businesses are more concerned about changes in legislation and regulation (third with 27%) than a year ago with this risk appearing in the top three for the first time. Natural catastrophes dropped out of the top three global risks for the first time (fourth with 21%). Climate change (seventh at 17%) rose to its highest-ever position. Loss of reputation or brand value is another peril to rise year-on-year (eighth, 15%). New technologies, such as artificial intelligence, was ninth (13%), whilst macroeconomic developments was a new entry in the top 10 risks for 2020 (tenth, 11%), driven by corporate fears over a global recession and debt accumulation, particularly in the US and China. The full report can be downloaded from: https://www.agcs.allianz.com/news-and-insights/reports/allianz-risk-barometer.html

Munich Re have reported that in 2019, 820 natural catastrophes caused overall losses of USD150 billion, broadly in line with Munich Re's 30-year average. Of these USD52 billion were insured. The wildfire season in California was less severe than in the record loss years of 2017 and 2018, after a wet winter eased summer drought conditions. This resulted in USD800 million in insured losses for California wildfire last year, although that this did not change the sharply rising long-term trend for wildfire losses in the US. In Australia, however, the bushfire season in 2019 was "very severe". A combination of high temperatures, dry air and large amounts of flammable fuel due to a lack of rain during the cooler season meant the bushfire season began early in September, with fires in Queensland and later New South Wales, Victoria, South Australia, Western Australia and Tasmania. North America saw three major hurricanes in 2019, close to the long-term average of 2.7, although the 18 named storms forming in the Atlantic last year was higher than the average of 12. The largest named storm, the category 5-strength Hurricane Dorian, caused catastrophic damage in the Bahamas but only grazed the US, resulting in around USD4 billion in insured losses overall. US thunderstorm season brought slightly more tornadoes than the long-term average, while severe flooding in the Midwest and other areas along the Mississippi triggered by snowmelt and thunderstorms caused around USD14 billion in insured losses last year.

The International Group of P&I Clubs 2019 annual report quotes statistics that continue to point towards a significant decrease in the number of large oil spills (more than 700 tonnes) over the past few decades.

The full report can be downloaded from: https://static.mycoracle.com/igpi_website/media/article_attachments/24179_IGPI_2019_Annual_Review_web_14mb.pdf

Oil Insurance Limited (OIL), the Bermuda based energy industry mutual, has decided it was prudent and in the best interests of the company and its shareholders to not declare a dividend in March but to reconsider the topic at the July board meeting, and to defer consideration of increasing its per occurrence limit into next year. OIL said its board reached these decisions based on the recent deterioration of its capital position and the uncertainty around the developments over the short term. OIL's financial performance in 2019 was the company's second best since the company commenced operations in 1972. This was largely a result of the exceptional returns earned on OIL's investment portfolio. In the absence of COVID-19, OIL said its capital position could have allowed the board to consider declaring a dividend and potentially increase limits for 2021. Unfortunately, the drastic downturn of the financial markets over the past few weeks has more than exhausted the investment gains OIL earned during 2019. Furthermore, their capital model indicates, that while they remain financially sound at this time, the company no longer has unencumbered available capital to support additional limits and/or declare a dividend. The OIL board also carefully considered the need to maintain adequate levels of capital to satisfy the requirements of rating agencies in order to protect OIL's current ratings. OIL said because of the above decisions, OIL remains financially healthy with more than adequate liquidity to meet their obligations.

Legal Roundup

The English Court of Appeal confirmed that defects in passage planning, as well as charts that had not been fully updated, rendered a vessel unseaworthy.

A vessel grounded whilst leaving the port of Xiamen, China. Shortly after dropping off the pilot, the vessel's master navigated out of the recognised dredged channel marked by lit buoys, resulting in the vessel grounding.

The grounding site was within an area identified as a Former Mined Area. Although there was no longer any direct threat to surface craft due to mines, mariners were warned that the former presence of those mines inhibited hydrographic surveying, giving rise to a risk of uncharted shoals.

The vessel was subsequently refloated by professional salvors under a Lloyd's open form salvage contract. Following an underwater inspection, little or no damage was found. The vessel proceeded on her voyage to Hong Kong and then Europe.

The vessels owners funded the salvage operation in the first instance and declared general average to recover the majority of the salvors' remuneration (together with other elements of general average expenditure said to have been incurred) from cargo interests.

Some cargo interests chose not to pay, alleging that there was actionable fault on the part of the vessel owners, which would give them a complete defence to the general average claim.

At first instance, the court held that the passage plan was defective because it failed to record a warning, required by a Notice to Mariners, that depths shown on the chart outside the fairway were unreliable and waters were shallower than recorded on the chart.

On that basis, the court held that the defects in the vessel's passage plan and the relevant working chart rendered the vessel unseaworthy at the commencement of the voyage.

The vessel owners did not dispute that the vessel ran aground because of defective passage planning but appealed on the following grounds:

1. The defective passage plan was the product of an "error in navigation" in that the master and second officer were acting in capacity of navigator rather than carrier when preparing that plan prior to the commencement of the voyage and
2. They did not fail to exercise due diligence as required by Article III Rule 1 of the Hague Rules in that they delegated the task of preparing a proper passage plan to the master and crew.

The owners argued that passage planning could not render a vessel unseaworthy because it involved no more than the recording of a navigational decision. Owners said that a ship could only be unseaworthy if there was a defect affecting an "attribute" of the ship.

The Court of Appeal consisted of three experienced shipping judges who rejected that argument. The Court held that it was clear on the authorities that errors in navigation or management could render a vessel unseaworthy if they occurred prior to the commencement of the voyage.

The owners also argued that, even if the ship was unseaworthy, there was no relevant failure to exercise due diligence. Relying on the references in cases such as The Happy Ranger [2006] 1 Lloyd's Rep 649 to the carrier's "orbit" of responsibility, the owners argued that navigation was outside their "orbit" because it was a matter solely for the master and crew.

That argument was rejected by the Appeal Court. It stated that, once the owners assumed responsibility for the cargo as carriers, all the acts of the master and crew in preparing the vessel for the voyage were performed as a carrier, even if they were acts of navigation before and at the commencement of the voyage. The owners were responsible for all such acts as a consequence of the non-delegable duty under Article III rule 1.

Texas federal grants summary judgment in favour of coverage, finding the policyholder provided sufficient notice to its insurer.

A Texas court found the policyholder's notice of a potential claim was effective when provided to the insurer's agent, even though it was not provided directly to the insurer itself.

The insured, acted as a broker for the sale of chemicals to an oil and gas company for use in fracking operations in west Texas. In 2017, the oil and gas company notified the chemical broker that the chemicals supplied were contaminated and had caused damages to pumps and valves, as well as downtime.

Shortly before the end of their 2016 policy period (which ended on April 1, 2017), the chemical broker notified its insurance agent, of a potential claim against it by the oil company. In turn, the insurance agent advised the potential claim to the wholesale insurance broker, who failed to send the notice of potential claim to the insurer.

A few days later, in early April 2017, the oil company sent a formal demand letter to the chemical broker claiming approximately USD1.54 million in damages due to the contaminated chemicals. The insurance agent sent the demand letter to the wholesale broker on April 6 and the wholesale broker forwarded the demand letter to insurers on April 7.

Insurers filed suit, seeking a declaration it had no duty to defend or indemnify their insured under the 2016 policy because the "claim" was not made until after the policy period expired; nor under the 2017 policy because the insured's knowledge a claim was likely before the inception of the 2017 policy period negated coverage.

The court first analysed the text of the discovery clause, holding it did not require notice of a potential claim directly to insurers; and notice through an agent was permissible. The court next analysed whether the wholesale broker was in fact the insurer's agent with authority to accept notice. The court highlighted while an insurance broker is generally considered an agent of the insured, there are circumstances in which an insurance broker can act as a dual agent for both the insured and the insurer. The court found in this case the wholesale broker was the insurer's agent.

As for whether accepting notice from an insured was within the wholesale broker's scope of authority, the court focused on the producer agreement's provision where the wholesale broker was contractually obligated to "immediately notify the company of all claims, suits and notices". The court held such language granted the wholesale broker authority to "receive" notices on the insurer's behalf and therefore also the implied authority to "accept" notices on insurer's behalf.

US Appeal Court affirms where underlying allegations lack fortuity and there is no occurrence, there is no obligation for insurers to defend.

A lumber supplier was sued by a commercial contractor that ordered fire retardant and treated lumber (FRT lumber) required by the projects' architects for several construction projects. The allegations in the underlying suit were that the supplier purposely substituted uncertified lumber.

The supplier's insurance company brought an action for a declaratory judgment that it had no duty to defend the underlying suits. The district court granted summary judgment to the insurance company holding that the insurance company had no duty to defend. The Seventh Circuit affirmed.

In affirming, the circuit court described the well-known provisions of a commercial general liability policy requiring the insurer to pay sums that the insured becomes legally obligated to pay as damages because of property damage caused by an occurrence, and defining an "occurrence" as "an accident." The court held that the underlying complaints did not trigger the duty to defend because they did not allege an occurrence. Quoting from several Illinois cases, the court noted that if an injury is the rational and probable consequence of the act or the natural and ordinary consequence of the act, then the act is not an accident. In analysing the underlying complaints, the court concluded that the allegations were inconsistent with shoddy workmanship or that the lumber shipped had a hidden defect resulting in damage that could not have been reasonably expected. Rather, said the court, the underlying complaints alleged that the supplier "deliberately shipped uncertified lumber despite knowing the consequences of doing so."

The court disregarded the negligent misrepresentation count in one of the complaints, stating that the label "negligent" is given little weight by courts and that courts focus on the actual allegations. Here, said the court, there was no unforeseen, sudden or unexpected event. There was no allegation that the supplier was negligent or failed to exercise reasonable care when it made its unilateral decision to ship uncertified lumber. Rather, the court found, the underlying complaints allege that the supplier did not exercise reasonable care by representing that it had the specific certified lumber requested by the contractor available for purchase, and by failing to notify the contractor that it supplied uncertified lumber.

Therefore, the court affirmed the district court's summary judgment in favour of the insurer finding that there was no duty to defend because the damage alleged was the natural and ordinary result of the supplier's deliberate decision to supply, and conceal that it supplied, uncertified lumber.

Quebec Superior court hands decision on interpreting a pollution insurance policy.

A distributor of petroleum products, purchased an oil storage depot, where business operations surrounding the oil storage depot continued until 2011, when the equipment was dismantled, putting an end to all operations. After the equipment was dismantled, and in accordance with the Environment Quality Act, the owner conducted an environmental assessment which revealed that the soil surrounding the oil storage depot was contaminated with heating oil and diesel fuel.

The owner subsequently sent a notice of claim to its insurers, requiring them to cover the "decontamination costs" pursuant to a "storage tank pollution and decontamination cost" insurance policy.

After investigating the premises, the insurers denied coverage on the grounds it had not been demonstrated that (i) the leak originated from a "storage tank system" or that (ii) this leak had occurred during the "period of insurance," as required the policy.

The policy stated that "The **insurer** shall pay on behalf of the **insured** the **decontamination costs** that the **insured** becomes legally bound to pay following a **leakage** originating from a **storage tank system** provided that the **release** was first reported in writing during the **period of insurance** or during the **extended reporting period,** if applicable. The **polluting conditions** must have begun on or after the retroactive date specified"

The owner retained an expert to prepare an environmental report to define the contaminated areas and verify whether the location where the old oil storage depot was situated was contaminated. In his report, the plaintiff's expert identified the contaminated areas, but was unable to pinpoint the sources of contamination.

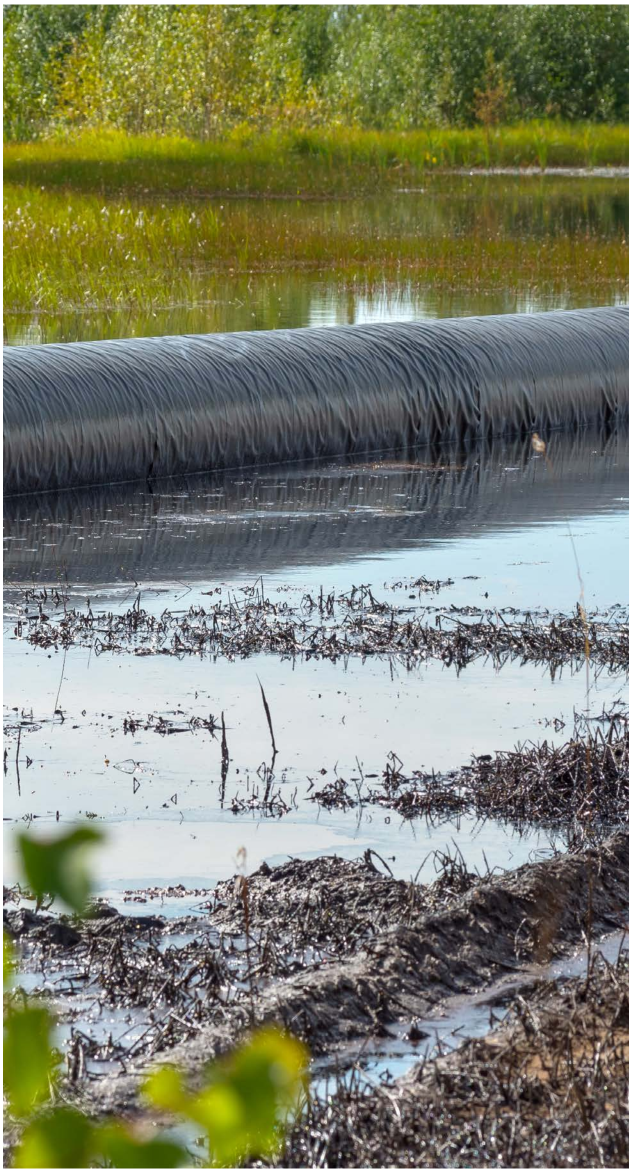
The insurers' expert, retained to determine the sources and time of the contamination of the previous oil storage depot, concluded that the source of contamination could not be determined and it would be reasonable to believe the contamination had occurred before 2001, given the fact that work had been performed on the previous oil storage depot equipment in 1997.

The owner argued that its insurers (i) had failed to act in good faith, diligence and competence from the time the contract was made until it ended, (ii) should have further investigated the covered premises, both at the time the insurance contract was made and to justify the inapplicability of the policy and (iii) did not fulfil their duty of collaboration, diligence and transparency by failing to disclose the actual grounds for denial of coverage in response to the notice of claim.

The defendant insurance companies argued that they would be entitled to deny coverage since the owners failed to successfully demonstrate, on a balance of probabilities, (i) the existence of a leak within the meaning of the policy or (ii) the date of contamination, which would not trigger coverage under the policy, thereby denying coverage of the "decontamination costs" in question.

According to the Superior Court, the plaintiff, who carried the burden of proof, did not successfully establish that the contamination resulted from the leak from a "storage tank system" as opposed to one occurring in the context of the oil storage depot operations (human activities) and dismissed the owner's claims.

In addition, regarding the date of contamination, without evidence to determine the time when the "polluting conditions" had occurred, the Court could not conclude that the defendant insurance companies were bound to pay the decontamination expenses.



Demystifying Common Clauses

In this regular feature we take a look at common clauses found in energy insurance that are often not well understood and try to look at what their intentions are, and what they are designed to cover or exclude.

In this article we look at Operators Extra Expense or OEE

'Operators Extra Expense' (OEE) insurance is a commonly purchased insurance coverage in the energy sector, but what does it cover?

OEE covers three 'heads of cover' being control of well, redrilling expenses and pollution.

Shortly after the birth of the modern oil industry at Spindletop in the US in 1901, came the birth of the well control industry. In 1913, explosives were used for the first time to put out an oil well fire. In 1961 Paul 'Red' Adair and his crew controlled the 'Devil's Cigarette Lighter' in Algeria, landing Adair on the cover of Life magazine and elevating him to almost cult hero status, leading to the 1968 Hollywood film Hellfighters, starring John Wayne, on which Red Adair acted as a technical advisor.

Whilst well control history is well documented there appears to be no properly documented history of well control insurance. However, anecdotal evidence would suggest that specialized energy insurance coverages originated in the late 1940s in the London insurance market. Early energy insurance policies were limited to physical damage of land drilling rigs, which were insured as contractors' equipment in the same manner heavy construction machinery/equipment were insured.

Following the increased capital investment in the energy field after World War II, with oil and gas exploration extending from onshore to offshore areas, a requirement existed for new insurance products to protect the energy industry.

The challenge to provide this protection through insurance was taken up, mainly by the London insurance market, which went on to develop specialized policies to cover the energy industry.

Research would suggest that in the late 1940s and early 1950s, control of well coverage was available under a relatively simple Lloyd's of London standard form which covered "expenses entailed by the insured in regaining control of oil or gas well(s) being drilled which get out of control as a direct result of the drilling of wells insured hereunder until completion of (or abandonment), caused by a blowout."

Early policies covered control of well only, but over time these were extended to cover the additional costs to drill a replacement well (termed redrilling coverage) and clean-up costs, containment costs, and third party liabilities resulting from seepage and pollution emanating from the well.

A 'package' of these three coverages (control of well, redrill, and pollution) became known as Operators Extra Expense or OEE for short. It would appear that some of the early control of well insurance coverages did not include definitions for 'blowout' or 'well out of control' which inevitably resulted in legal disputes between some insureds and their insurers.

Insurers soon realised that without specific and tightly worded definitions the courts (especially in the US) would tend to interpret coverage in favour of the insured and thus provide coverage for expenses that insurers maintained amounted to no more than business expenses associated with the industry, rather than the result of a fortuitous event.

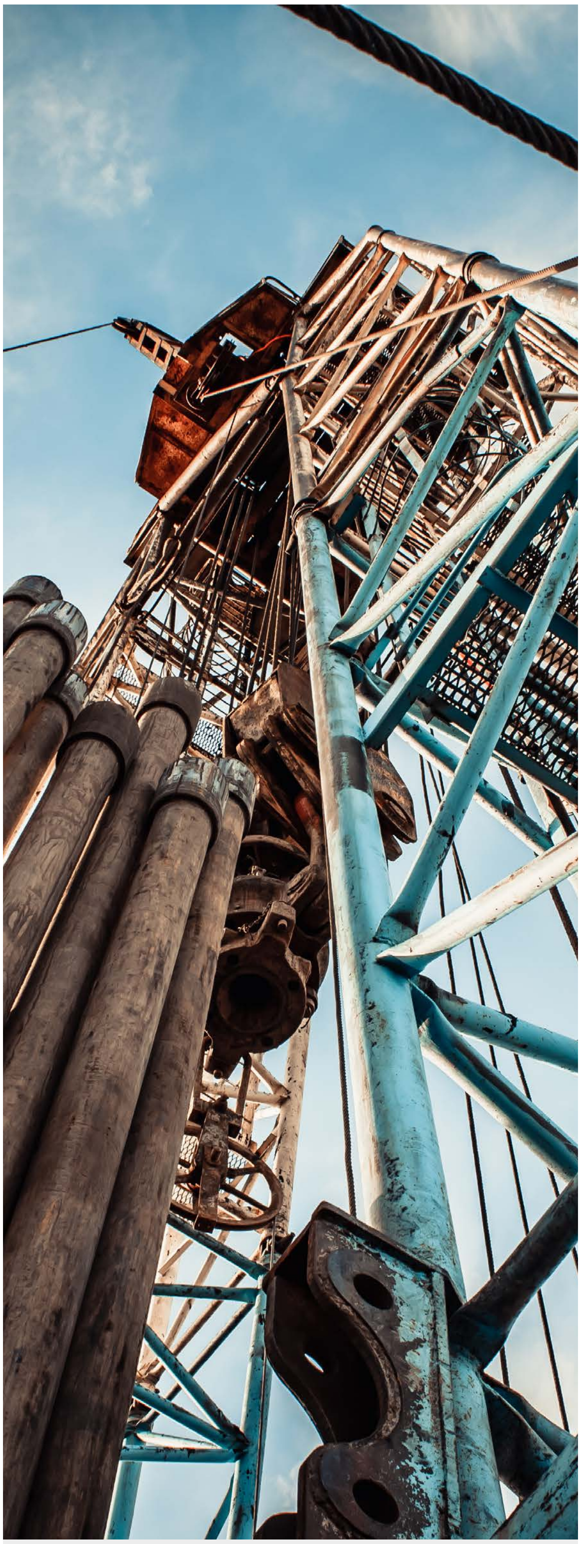
Examples of such 'normal costs of drilling a well' that insurers often ended up paying were operational costs to balance a well following a 'kick' (the first sign that a well is becoming over pressured and about to blow-out) or for loss of in-hole tools that had simply become 'stuck' in the bore hole.

Over the years various OEE wordings were devised by brokers and insurers, which aimed to cover additional expenses following a blowout, which was a defined term in the policy. However, various court cases led to expansive interpretations of wordings. So in the mid-1980s the market decided that the time had come for a revision of well control insurance wordings which ultimately led to the introduction of the Energy Exploration & Development (EED) 8/86 wording, which today is still the common standard control of well policy wording used in the London and worldwide insurance markets.

Unlike the previous OEE wordings, the EED form does not incorporate a blowout definition, but, instead, addresses the cover in terms of definitions for a 'well out of control', and a 'well brought under control'. One of the other main changes to the previous OEE wordings was to exclude "a flow in the wellbore, which can, within a reasonable period of time, be circulated or bled off through surface controls", which is designed to prevent the policy paying for the costs to control a 'kick' previously mentioned.

Although it was the underwriters' specific intention to exclude costs they were not intending to cover; some may contend that in tightening certain definitions and exclusions the market may have gone too far, leading to occasions where the restrictive policy language excludes a claim, even though additional expense has resulted as a direct consequence of a fortuity.

However, in spite of such exhaustive coverage overhauls, the insurance market has still struggled to make a consistent long-term profit from well control business. As such many underwriters will only write well control or OEE as a sort of 'loss leader' when part of a package of risks offered to them, including coverages (such as offshore physical damage) that are more attractive to them.



The above is provided as a general overview of some of the coverage often provided by the aforementioned clauses. This is not intended to be an extensive and exhaustive analysis of the insurance coverage provided by such clauses. The comments above are the opinion of the Marsh JLT Specialty only and should not be relied on as a definitive or legal interpretation. We would encourage you to read the terms and conditions of your particular policy and seek professional advice if in any doubt.

CONTACT US

If readers have particular clauses they would like us to consider including in this newsletter in the future, or have any comments on the above please contact john.cooper@marsh.com

Directors and Officers (D&O) Update

The D&O market has contracted fast and shows no sign of easing in 2020 or early 2021.

Local and international D&O markets have been contracting dramatically over the past 8 to 12 months, with regional differences slowly fading. London, a long term global market place for D&O insurance for international energy companies, with historically attractive capacity and innovative products, showed clear signs of changes as early as late 2018, early 2019. With D&O insurers reviewing their general appetite for the product line and centralising their underwriting oversight, the effects of the contraction can now be felt across Europe, North America and Australasia. Approximately USD1.3 billion of capacity has left the Lloyd's of London market since the second half of 2019 following market exits and portfolio run-offs, over USD70 million of which affecting directly D&O buyers.

Having faced an increase in claims frequency and severity for some years, insurers are counting their losses; many argue they have not made a profit in that class of insurance for almost 10 years. Investigations (internal/regulatory) and 'event driven' US securities claims in particular accounted for almost two thirds of all D&O insurance claims Marsh JLT Specialty saw in 2018. The trend continued in 2019 with pollution events as well as bribery and corruption allegations noticeable drivers for litigation in the energy sector. This trend is expected to continue with two COVID-19 related securities claims filed in the US since the start of the pandemic. Claims have also been more frequent outside the traditional hotspots countries (Europe, Australia and North America) and exploration and production risks and miners have been particularly affected following a series of high profile losses. Consequently, D&O insurers' appetite for the broader energy sector has reduced materially.

The market has considerably hardened across the board but companies with securities traded in the US and/or Australia, with financial or operational challenges or with claims, are feeling the brunt of the market hardening. The force of the contraction is furthered by historical D&O insurers being cautious of the sector and reducing their overall engagement whilst - in the wake of the 2018/19 Lloyd's review – the Lloyd's syndicates growth targets have also been curtailed significantly; in short capacity is contracting with all providers, putting further pressure on rates. Unfortunately, the global spread of Coronavirus, oil price and stock volatility, and the growing threat of a potential global economic crisis and a resulting surge of corporate bankruptcies, can only further unsettle insurers.

Stormy weather

1 Market capacity is contracting significantly across the board – all sub-segments of the energy sector are affected.

Active M&A activity amongst insurers over the past 2 years (AXA- XL- Catlin, HCC-Tokio Marine, AIG-Talbot, Hartford-Navigators etc.), recent market exits (MS Amlin, Channel 2015, Mitsui, AXIS, Neon Underwriting etc.) and a general trend towards capacity reduction have led to significant reduction in capacity available for large international buyers. Concurrently, there has been no new entrants to the D&O market, something of an oddity in the management liability space by past years' standards.

Our energy clients are particularly affected, primarily those with US or dual US/Australian listings. 2019 saw a general average limit reduction of 1.1%, whilst energy company's average limit purchased declined by 2.9% (Source: Marsh JLT Specialty). Geographical arbitrages are still possible across international markets but insurers have tightened up their underwriting process considerably and centralised their underwriting authority. Marsh JLT Specialty is able to leverage its network with direct access to the US, Bermuda and Asia, but capacity/rates there have always been more conservative and some of those insurers will not offer capacity without face to face meetings - a process that will be challenged by the current pandemic.

We estimate the maximum market capacity for energy risks in the first quarter of 2020 to be in the region of USD300 million, a sharp decline from the almost USD900 million available at the peak of the soft market.

2 Rates are going up markedly across the sector with energy, power and mining risks particularly affected.

The harshest corrections are mostly seen by companies with (i) North American or Australia securities, (ii) claims activity, and/or (iii) distressed financial accounts in particular. Double to even triple digit percentage increases are now increasingly common and the trend continues to worsen; our public energy clients saw an average rate increase of 63.8% in 2019 (the increase was 87.8% in the last quarter of 2019 alone); in comparison, the rate movement for US listed companies (all industry sectors) was +112% in the last quarter of 2019 and we expect the first quarter of 2020 to show an average increase in excess of 100%. January and February 2020 have already delivered increases in excess of 300% for the most exposed risks.

3 Coverage generally remains broad by historical standards.

However, insurers are looking to curtail some elements of cover around investigations and securities or M&A related losses in particular. Bribery and corruption exclusions are more frequent and mining companies have to provide detailed tailing dam information to avoid blanket exclusions; whilst long-term agreements are no longer available. Corporate retentions are going up significantly for all types of claims with securities deductibles now routinely at a minimum USD5 million or above. Broad COVID-19 exclusions are also now being imposed by some insurers.

4 Underwriting information demands have increased significantly.

Strong reliance on publicly available information and in the UK, the insured’s duty of fair presentation and reasonable search; but underwriting discipline has tightened up materially, with financials, sanctions and cyber resilience yielding new/multiple questions. Operational and financial exposure to COVID-19 are now also a common area of focus for underwriters who are looking to understand short and medium financial impact and scrutinising management’s crisis management plan and earning guidance.

WEATHERING THE STORM

With contraction in full swing and insurers’ increasingly risk adverse, preparing thoroughly for a D&O renewal has become critical; below are quick pointers to best prepare:

- Start your renewal process early and prepare your internal stakeholders for the most challenging market conditions since the early years 2000. The market deterioration is very much ongoing. With most of the insurance market now working remotely and connecting from home, it is possible that some elements of the renewal process (documentation, invoicing, settlement) may be facing particular challenges or early teething issues.
- Reconsider your priorities for this line of insurance - discuss alternative programme structures and scope of cover (individuals vs. entity, headquarter cover vs. network), re-evaluate limit (desirable vs. achievable) and consider which insurers relationships can be leveraged upon. Marsh JLT Specialty can provide detailed data and benchmarking on rates movement to support your internal discussions.
- Differentiate your risk - dedicate time and resources to your D&O renewal: involve senior management, volunteer experts (finance, compliance, sanctions, ESG), pre-empt insurers questions (COVID-19), highlight what differentiates you from your peers.
- Be proactive - subjectivities abound, address them early on and, as much as possible, before renewal date. Insurers have grown increasingly nervous and impatient - they will use timing to their advantage.
- Budget for material costs increases - bar drastic changes in programmes structure, limit purchased or scope of cover, allowance for price changes should for part of budget setting.

Engaging early on with your adviser, informing senior management expectations, challenging historical purchase to revalidate ongoing priorities, will all make a material contribution to any D&O renewal.

Whilst the stormy market conditions of 2020 are widely expected to be felt well into 2021, a proactive engagement will make a material difference to both capacity renewable and rates.

Update from Marsh JLT Specialty Engineers: Engineering in the Current Crisis

We are now all acutely aware of the global impact of COVID-19, the safety and wellbeing of our clients and colleagues within the whole risk engineering community has to be our top priority. As risk engineers, the resultant travel bans and the understandable restrictions in relation to access to our clients' premises have been impactful with many surveys initially being postponed or cancelled.

The basic risk-engineering model has always heavily relied upon site visits and face-to-face meetings. However the placement of risks continues, markets still require information to support the process, and clients still want to leverage the experience and advice that expert risk engineers provide. At Marsh JLT Specialty we are hugely encouraged by how our clients, team and our risk-engineering colleagues at insurers have come together and adapted to these considerable challenges.

A number of alternative remote working strategies are taking shape. For example:

- Use of videoconferencing to conduct surveys and risk recommendation updates, at least until visits can be carried out safely. This is not without precedent as remote surveys have, for a number of years, been conducted in some difficult high-risk territories. Feedback from clients and markets has so far been supportive with most topics that appear on a normal survey agenda being addressed. The inability to conduct field visits is an obvious limitation.
- What have we learned about the process so far?
  - Test the video conferencing capabilities before lining up lots of people.
  - Preparation of the agenda and information well in advance is key.
  - Obtain information-for-review well before the video call and make sure it is fully reviewed well in advance of the call.
  - Include opportunities to validate key documents, inspection records, MOCs, etc.
  - Focus on questions and answers, and actively encourage participation from all participants.
  - Behave like it's a normal survey with opening and closing presentations and subject specific meetings protocols and procedures.
  - Use screen share functionality to go through any presentations and ensure all participants are viewing the same information.
  - Updates on recommendations should be supplemented by pictures and/or videos where possible.
- Anticipate issues that will likely be of importance to underwriters and be proactive in getting updates on key issues such as:
  - Turnaround plans.
  - Planned maintenance activities on high risk/key equipment.
  - Understanding deferments of inspection and maintenance activities, if any, with mitigation plans.
  - Specialist vendors' ability to support equipment overhauls and other key activities remotely (e.g. using webcam technology or other technology).
  - Business continuity plans.
- Work together with clients and markets to design contingency engineering plans specific to each client; one size does not fit all.
- Use of technologies such as webcams or other devices to stream video which will enable an element of field checking (e.g. permits, isolation standards, bypass status etc.) is currently being tested.

There are no doubt many more imaginative ways to execute the risk engineering process and satisfy the requirements of our clients and the markets; we encourage dialogue amongst all of the stakeholders to explore this further. Collaboration will drive innovation, and this crisis might well prove to be a catalyst for more permanent adaptations.

Pandemic Support

Disruptions to business can have a major impact on operations and ultimately earnings.

To ensure people engagement, operational resilience, supply chain robustness, and financial stability, it is important to understand and manage your stakeholder expectations in the event of a pandemic outbreak. This will ensure you have taken all possible precautions to protect your business and ensure it is operationally resilient to meet the rapidly changing environment whilst at the same highlighting to your stakeholders that you are prepared to meet this challenge.

There are four key areas where Marsh can offer support:

People: Human Resources Resilience

Develop a human capital resilience framework with policy, plans, and protocols which will support the management of direct and indirect impacts on employees.

Our analysis involves:

- Assessing the impact and contribution of jobs.
- Identifying the most critical jobs.
- Prioritising jobs for immediate shadowing and succession planning.

This will allow you to build a reserve bank of employees with multiple skills capability that will allow them, in the event of a pandemic, to step into and deliver key functional roles.

Operations: Contingency Preparation

Implement a pandemic plan as part of the fabric of your business continuity management (BCM) programme to ensure it meets the operational needs of your business.

We are able to work with clients and provide analysis which:

- Establishes resources required and develop pandemic recovery strategies.
- Develop pandemic communication protocols.
- Test and train the pandemic plans through the use of desk-top simulation scenarios.

This will ensure you have in place robust pandemic plans to address potential impacts to your operations that are easy-to-use and link to your existing BCM programme.

Supply Chain: Robust Scheduling

Identify which products/services are most 'at-risk' and determine what constitutes a key location/supply route.

Our analysis involves:

- Estimating recovery times, key dependencies and inter-dependencies.
- Determining stakeholders (internal/external).
- Considering supplier recover capabilities analysis and supporting mitigation plans.

This will determine where the vulnerabilities lie in your supply chain and what actions need to be taken to improve it robustness in the event of a pandemic.

Financial Revenue Stream Protection

Our experts can support clients to calculate the financial impact to operations and determine the activity costs required to manage a pandemic event.

The analysis involves:

- An 'activity delivery model' covering sales predictions, 'see through' gross margins, market share loss predictions etc.
- Identification of reinstatement times and actor 'refill' requirements.
- In-depth analysis of alternatives, additional cost of working, and per-location constraints.

This will highlight where revenue streams will be adversely affected by a pandemic event, and what mitigation actions should be considered.

Marsh JLT Specialty Training Courses: London

Marsh JLT Specialty run three different Chartered Insurance Institute (CII) accredited energy insurance and risk management training courses in London in 2020.

In light of the COVID-19 pandemic, Marsh JLT Specialty has taken the decision to cancel the intermediate level course previously scheduled from May 11-15. All registered delegates have been given the option to move their registration to the October 5-9, 2020 session of this course.

Delegate and colleague health and safety is of paramount importance to Marsh JLT Specialty and has been a significant factor in our decision. We are closely monitoring the situation for our courses scheduled for the remainder of 2020 currently scheduled as follows:

BEGINNER'S LEVEL

Energy Insurance Diploma Course

July 6-10, 2020

INTERMEDIATE LEVEL

Energy Insurance Risk Management Course

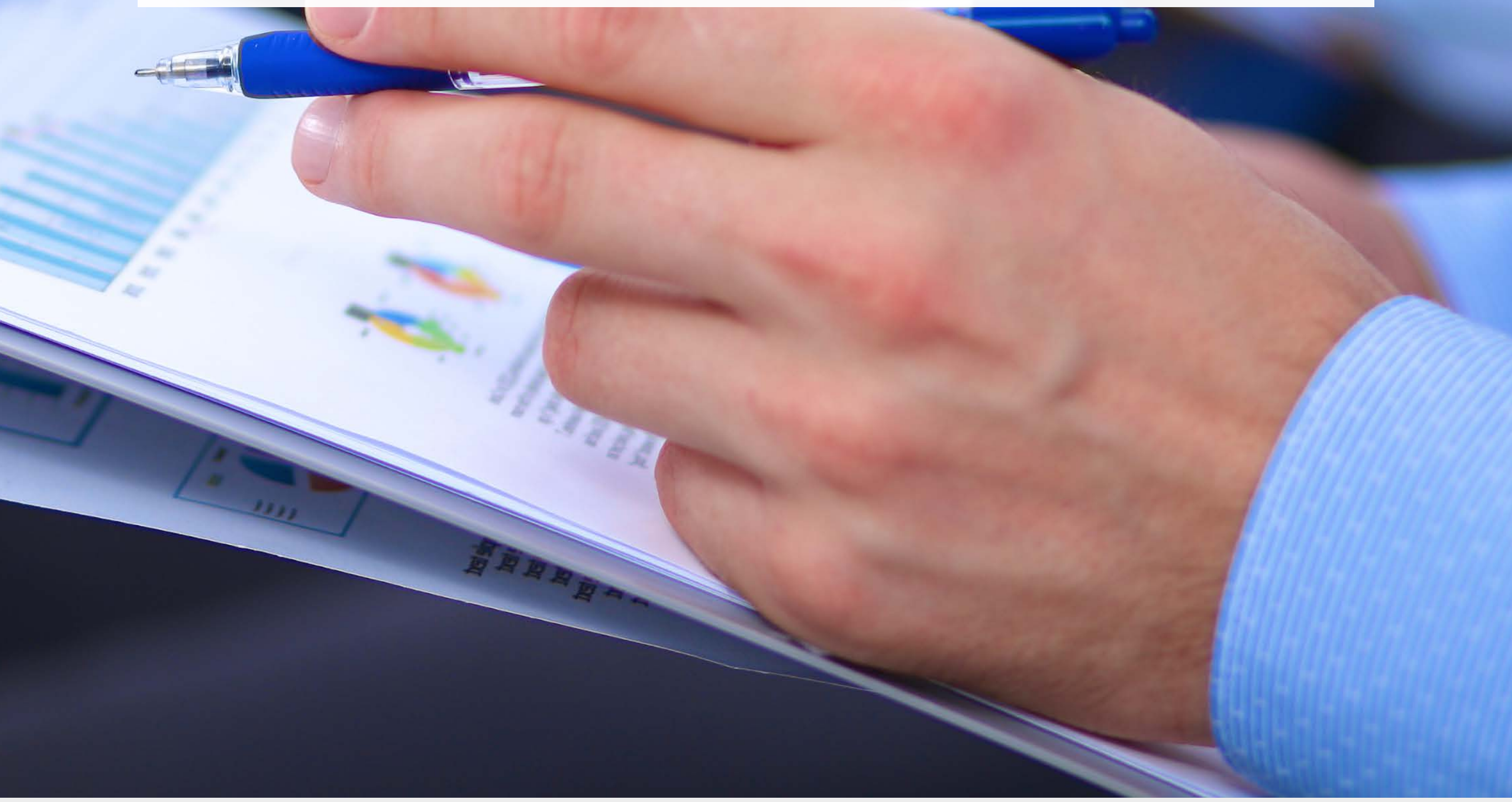
October 5-9, 2020

ADVANCED LEVEL

Advanced Risk Management Course

September 7-11, 2020

We stay firm in our commitment to provide some of the best in class, industry-relevant training to our clients, markets and colleagues both local and international. Questions regarding our London training courses should be directed to Sarah Verzola at sarah.verzola@marsh.com



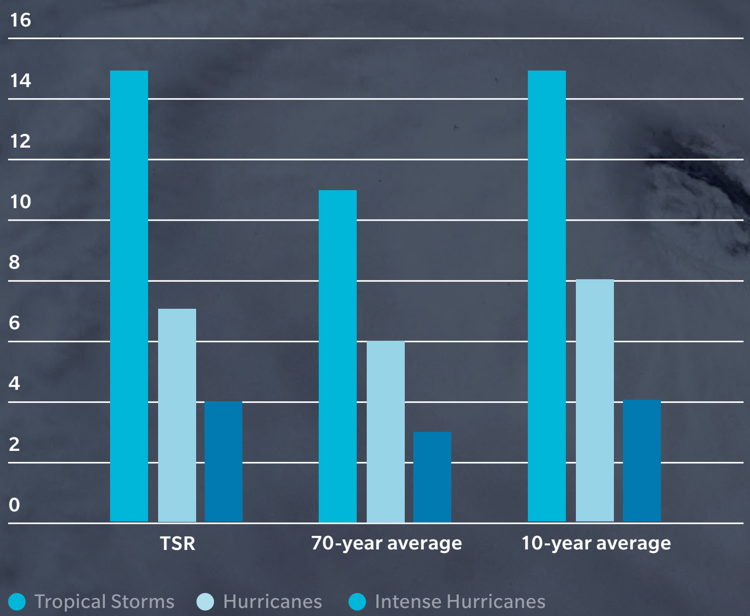
Atlantic Named Windstorm Forecasts

The Tropical Storm Risk (TSR) extended range forecast for North Atlantic hurricane activity in 2020 anticipates a season with activity close to the long-term norm.

The forecast spans the period from June 1 to November 30, 2020 and employs data through to the end of November 2019. Current and projected climate signals show an absence, of any climate forcing that will notably influence North Atlantic basin tropical cyclone activity in August-September 2020. TSR's main predictor at this extended lead (is the forecast July-September trade wind speed over the Caribbean Sea and tropical North Atlantic. This parameter influences cyclonic vorticity (the spinning up of storms) and vertical wind shear in the main hurricane track region. At present TSR anticipates that the July-September 2020 trade wind speed will be near to average – due in part to El Niño Southern Oscillation (ENSO) also expected to be near to average of TSR admit that the precision of their December outlooks for upcoming North Atlantic hurricane activity between 1980 and 2019 is low.

The chart plots TSR's forecast against the 70 year and 10 year averages.

FIGURE 1 | 2020 Atlantic Hurricane Season Activity/Forecasts



Focus on: Decommissioning Security Solutions in the UK and Dutch North Sea

The Opportunity

The insurance market issues various third party guarantees on behalf of exploration and production firms in the oil and gas sector. Many of these guarantees cover decommissioning obligations, both onshore and offshore and are referred to as surety bonds or surety guarantees issued by sureties or surety companies.

These surety guarantees are typically issued in favour of regulatory agencies, trustees, or other entities under joint development agreements (JDAs), or are issued in favour the sellers of assets being acquired. The oil and gas firm always maintains the primary responsibility to decommission the assets in question and the surety guarantee only comes into play under a default scenario (e.g. a failure to decommission assets as required and/or to maintain adequate decommissioning security).

The surety industry issues guarantees that generate USD15 billion in premium annually, and premium grows larger each year. Guarantees covering the decommissioning oil and gas assets represent one of the largest concentrations of exposure for the surety industry.

Surety companies evaluate risk and determine appetite, terms and conditions based on both financial metrics and the characteristics associated with the underlying assets being covered. There are surety markets with more favourable views of the sector, and those with more sophisticated underwriting techniques, that can serve oil and gas firms operating in mature fields such as the North Sea.

Marsh JLT Specialty has 270 surety colleagues globally, including colleagues with specific expertise in oil and gas base in Houston, London and Amsterdam. These colleagues work in close collaboration with colleagues in the Energy & Power practice; together, we bring the entirety of the market to our clients.

Background

Assets in the North Sea (UK and Dutch) are typically governed by Decommissioning Security Agreement (DSA), which sets the terms for the security each joint venture party are required to provide.

Historically, the level of security required for a company's decommissioning liability is based on the net present value (NPV) of the field. As the asset moves closer to the planned abandonment, each party submits decommissioning security based upon the anticipated decommissioning costs. The amount was set by operator and the security protected them against the "joint and several liability" provision of a non-operator becoming insolvent and unable to pay their share of abandonment cost.

Prior to 2000, most North Sea assets were operated by the "majors" and decommissioning security was not concern, as they could typically provide a parent company guarantee (PCG) if the external credit rating met the DSA requirements. However, beginning in or around the year 2000, it became more common for the "independents" to act as operators and as such a PCG was not typically an acceptable option to joint venture partners or by the regulatory authority.

Often, this left bank guarantees or letters of credit (LOCs) as the only form of acceptable security and in many cases, these LOCs needed to be cash-collateralised, either in part or in full.

As new DSA's are being formed, alternative forms of security are being accepted, with encouragement from the relevant authorities, to support investment in late-life UK Continental Shelf assets. With a continuing trend of majors exiting North Sea, it has created opportunities for independent/junior operators. This trend has resulted in the need for new approaches to satisfy decommissioning security requirements in a way that allows investment and the use of capital into CapEx and/or to fund further acquisitions.

Decommissioning Security

Traditionally, decommissioning security has typically taken two forms:

- Letter of Credit (LOCs) or Bank Guarantees (BGs).
- Parent Company Guarantee (PCG).

Generally speaking, the issuer of the LOC/BG or PCG must be "A rated" from an external ratings agency (S&P and/or Moody's). Historically, in some cases, the minimum rating was higher than "A".

Insurance Market Solutions: Surety Guarantees

Historically, some insurers supported the junior or start-up oil companies by offering surety guarantees that would 'sit-behind' the LOCs, freeing up cash that previously backed the LOCs. This approach was viewed as extremely valuable to these newer firms and start-ups.

However, these markets were relatively sparse and rarely provided sufficient capacity to release all of the existing cash collateral. In addition, the support was viewed as inconsistent, with each transaction being reviewed based on its own (perceived) merits.

Surety Guarantees: An Asset-Based Approach

Some surety markets have become more sophisticated with respect to their underwriting and what has historically been a heavily credit driven approach has evolved into one where asset value, and projected longevity and economic viability of the specific field(s) covered are taken into effect. An asset-based underwriting approach more closely resembles the asset-backed lending approach used by their banks. Some sureties employ oil and gas engineers, or other energy industry professionals, who evaluate assets and decommissioning activity.

This asset-based approach can be useful in situations where the financial condition of the company does not itself support the decommissioning surety guarantees. When the surety underwriter is convinced of the longevity of the asset(s), it may support surety guarantees based upon their evaluation of the asset's quality and their expectation that the asset(s) will survive an insolvency event.

The asset-based underwriting approach can be useful in certain situations, including in the North Sea, though it is not employed as often as ins some other regions given the maturity of North Sea fields.

Collateral Approaches

In certain situations, sureties may require a firm to post cash collateral over a period of time under what is often referred to as a "sinking fund" approach. Under this scenario, there is often a deposit collateral required, which builds over time as the assets approach end of useful life.

Information Required

Depending on the financial condition and asset portfolio, the following information is generally required by a surety underwriter:

- Financial statements (if not publicly available).
- Decommissioning site/field-level information.
- DSA wording.
- Decommissioning guarantee wording.

Supplemental information that is often required:

- Reserve report (third party).
- Investor presentation.

NPV fluctuates with commodity pricing so it is important to provide surety underwriters with "stress test" information, demonstrating the firm's ability to manage through a pricing downturn.

It is also imperative to present sureties with a comprehensive decommissioning plan, to include timing and sources of funding related to the required decommissioning costs.

An in-person between key financial and operational colleagues and the surety underwriters is highly encouraged.

Anticipated Cost

Depending on the individual merits of each firm's financial position and assets, the cost of obtaining a surety guarantee can often be competitive with LOC costs and in some cases, can be materially less.

In certain cases, the cost of a surety guarantee may be higher than a LOC. However, the release of cash collateral or the freeing up of bank lines via the reduction or release of LOCs, needs to be considered.

Under a PCG approach, there is often an internal charge that should be considered when comparing costs with surety pricing.

Experienced Resources

With over 270 specialists globally, placing over USD1 billion of premium into the market, Marsh JLT Specialty's Surety practice is the world's largest. Our clients benefit from surety expertise in not only the oil and gas industry, but more specifically in the North Sea (Dutch and UK).

Our market leverage and innovative approach ensure that clients receive the most competitive terms and conditions available, with full access to the market, including new capacity as it become available.

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INTRODUCING MARSH JLT SPECIALTY

We are specialists who are committed to delivering consulting, placement, account management and claims solutions to clients who require specialist advice and support. We consider problems from every angle and challenge the status quo with entrepreneurial ideas and solutions.

With unparalleled breadth, our Marsh JLT Specialty global team is united by a determination to bring the most experienced and relevant specialist resources to our clients, regardless of where in the world they are located. This approach means our local specialists work seamlessly with global experts, together creating and delivering tailor-made risk and insurance solutions which address each client's unique challenges.

Our service offering is enhanced with insight-driven advice supported by tailored data, analytic and consultancy capabilities to support clients in making important decisions about their complex risks.

Exceptional service combined with transparency, integrity, and accessibility underpins our partnerships with clients.

Note: All references to pricing and pricing movements in this report should be considered averages, unless otherwise noted. Also, as data is refined over time, it is possible that adjustments will be made to figures from prior quarters.

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