Q1 2013

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Delay in Start Up Cover: A New Hope?

Mention the words ‘Delay in Start Up’ and many believe it is just ‘Business Interruption’ cover for construction projects—and, at its simplest level, the many aren’t wrong! However there is a myriad of subtle differences in the application of Delay in Start Up cover when compared to Business Interruption. For a start, a project is not necessarily delayed because of a loss, and if this loss occurs early enough along a projects critical path, some of the time lost can be recovered. Outside of North America, the many tend to believe that a project can only be ‘Delayed’ once—it is either on time or not and so the deductible tends to be applied as a single aggregate rather than on a more typical each and every occurrence BI basis. Next we have the more concerning issues that for many years some underwriters believe the policy responds in a manner this writer finds rather disingenuous—once the policy is triggered, it is gone and reinstatement is required regardless of whether the client has utilised the full Indemnity Period or Limit he has originally purchased. Following this, there is often a complicated negotiation over how to extend/reinstate the policy if there has been, or worse still, may have been an indemnifiable loss. There is of course not enough room on these pages to discuss these issues in detail but nor was this the intent.

The point to be made here is more one of the green shoots of progress being made on this entire product as a market. Just over a year ago, the London Engineering Group invited underwriters, brokers, engineers, loss adjusters and forensic accountants to a meeting on the subject of DSU. The agenda was generally open, but ideally to ascertain if it is still the product underwriters wish to offer and clients wish to purchase, whether it works, if as a product it needs to be re-examined etc. The consensus was of course more discussion was required and greater clarity and understanding of the product itself was of benefit to all. IMIA (International Association of Engineering Insurers) also expressed interest and became involved and a joint working party of LEG, IMIA, brokers et al was formed.

Fast forward... many, many meetings.

LEG and IMIA have now released jointly produced papers which are available from us by request or from the IMIA website. The papers are intentionally very basic. DSU (or more to the point, the mechanics and detail of this product) simply needs to be better understood by all parties. The aim was to start at the beginning with the basics and encourage dialogue between clients and their brokers to iron out any ambiguity as early as possible. The paper is aimed perhaps more at CEO’s or CFO’s who may not be full time insurance professionals but of course need to understand the risk transfer protection their companies are purchasing. A few of those insurance professionals who should know but were afraid to ask may well pick up a point or two which is no bad thing either.

Perhaps most pertinent going forward, is that, amongst other things, Underwriters are forming the opinion that they wish to understand the composition of the Sum Insured to a greater degree, and they need to attempt to understand where a project is on the date of loss relative to the critical path. There is nothing wrong in this. Munich Re are publicly concerned at the quantum and frequency of DSU claims in the current climate. They have seen some alarming loss trends in this product which they are of course eager to share with all (Editor: to justify price and deductible increases per chance?).

Is any of this altering the buyer’s position today? Well, no, not yet, but do expect to be asked increasingly for more information, for more understanding of the composition of the financial models, and for a greater transparency on where the project progress stands versus the planned progress—a complicated feat when you consider the Contractor may not wish to tell the principal at all given times for fear of incurring financial penalties.

There will be more from LEG / IMIA in due course. The following subjects are firmly on the radar:

1. how to extend / reinstate DSU when there has been or may be an indemnifiable claim, and
2. how to accurately track the critical path.

The working party seem at this time to find consensus and common goals for the benefit of all; to ensure that the product does not strike back!

Source:
www.imia.com
www.londonengineeringgroup.com
Cyber Security — Increasing Concerns for Power Industry

The world’s most valuable company Saudi Aramco’s network was attacked by a custom virus on August 15th, damaging about 30,000 desktop hard drives and preventing them from operating. “The aim was to stop pumping oil and gas to domestic and international markets”, said Abdullah al-Saadan, who headed the inquiry team.

As it is “in the interest of the investigation not to reveal any results” Aon believes it’s useful to reiterate key observations and recommendations made:

- “If it can happen to them, it can happen to anyone” Saudi Aramco operates in a high-threat environment and has good security defenses.
- “Attacks which purposely destroy data and computers systems are rare” This attack is a good example of a ‘black swan’—an unlikely event with potentially high impact. However, ‘copycat’ attacks are possible and should be considered in an organization’s planning.
- Administrators appeared to have effective controls in place These controls prevented this attack from gaining access to server and domain administrative accounts. Their apparent success at ‘defense in depth’ sets a target that other organizations should emulate.
- A good major incident response plan is critical for any organization The incident response plan should be based upon effective communication and management decision making processes. A tabletop exercise may be a good idea to help gauge your organization’s ability to handle a similar attack.
- Emerging Threats to critical Infrastructures This incident doesn’t stand on its own. The European Network and Information Security Agency (ENISA) recently published a report comprising over 120 recent reports from security industry, networks of excellence, standardization bodies and other interdependent institutes. According to this report the ‘Top 5 Threat Trends’ in critical infrastructure is:

<table>
<thead>
<tr>
<th>Threat</th>
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<tr>
<td>1. Drive-by exploits Injections and drive-by downloads will be a serious threat to components of Critical Infrastructures (insurable risk: ⬇)</td>
<td>✅</td>
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<tr>
<td>2. Worms/Trojans The increasing trend in creation of trojans will affect components of Critical Infrastructures (insurable risk: ⬇)</td>
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<td>3. Code Injection Cross site scripting will play a significant role, especially in web applications involved in Critical Infrastructures (insurable risk: ⬇)</td>
<td>✅</td>
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<td>4. Exploit kits Tools to identify and abuse exploits found in most common infrastructure elements, both web and client systems (insurable risk: ⬇)</td>
<td>✅</td>
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<tr>
<td>5. Denial of service Is considered as an effective technique to attack critical systems and achieve impact with relatively low capabilities, e.g. through Hacktivists (insurable risk: ⬇)</td>
<td>✅</td>
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Good behaviors lead to good outcomes

“All agree that the [Aramco] attack could have been much worse if it had targeted the production infrastructure, similar to the Stuxnet attack, which in turn could have triggered worldwide price increase of oil and secondary economic repercussions”. Generally, there are four ways to deal with risks (see image). Within the Power Industry though, a board has only two options really; reserve against contingency and/or transfer (residual) risk by purchasing cyber (liability) coverage.
Call to Action: Integrated Risk Management & Risk Transfer Assessment

Companies are telling us their dependency on IT risks has grown. Meanwhile, the Costs and Income associated with IT Risks are typically uninsured. This imbalance calls for action.

Our key message therefore is all about preparing your organization for getting oversight and insight. Being prepared proves you’re serious about your company’s (security) mission and vision to the outside world as well as it will enable you to mitigate (financial) losses better.

Aon’s risk management and insurance brokerage capabilities provide integrated solutions for the Power Industry.

- Perform a gap analysis on your insurance coverage. Growing IT risks and associated costs for Power Industry are insurable
- Assess transfer of (residual) risk. The scope of cyber cover has improved— including but not limited to threats/risks above

Products now common across Europe—with paying claims and premium levels at a reasonable level (considering increasing risks and improving cover)

Sources:
http://www.alarabiya.net/articles/2012/12/09/254162.html
http://www.dexasystems.com/blog/2012/08/Lessons-Learned-from-Saudi-Aramco-Incident
www.enisa.europa.eu
http://en.wikipedia.org/wiki/Stuxnet
http://www.cyber50.org/blog/shamoon-wiper

Aon Publishes Nuclear Property Insurance Paper

Mounting losses in this sector and recent market responses are requiring risk managers and their brokers to re-evaluate the position of the nuclear insurance, mutuals and pools seeking adequate, long-term and stable risk transfer capacity.

This paper examines some of the insurance options available to nuclear power plant operators globally.

Hamish Roberts says: “This is a great team contribution and achievement. Nuclear expertise within Aon has that unique feature to be completely decentralized and spread over several continents. Notwithstanding the distance and time differences our nuclear experts are able to provide high quality and timely services and advices to our nuclear clients and prospects. This document is another example of their skill and commitment in a fast evolving nuclear world.”
Insurance Reality behind the Tohoku Earthquake Claim

1. Introduction

Tohoku 11th March 2011: an earthquake with magnitude 9.0 on the open Richter scale and the ensuing tsunami would cause world’s biggest devastation following a single event. The human toll is huge: 15,850 people killed, 3,200 missing. An entire region is destroyed.

TEPCO’s nuclear plant of Fukushima Daiichi was also severely hit by a 15m high sea wave causing most of the auxiliaries of the plant to fall out. Four out of six reactors were affected by cooling issues leading the cores to be largely melted in the first days and thus causing world’s second largest release of radioactive material. Hundred thousand people are evacuated outside the restriction zones established by the Japanese authorities.

Direct losses i.e. victims’ compensation and nuclear clean-up cost could amount as much as USD 275 Bn over the next 10 years and with an estimated USD 265Bn indirect losses. But how was the insurance market affected? Did the nuclear insurance protection and compensation scheme work? Although it is likely to be the costliest natural catastrophe ever, the impact on the private insurance industry will probably not surpass that of hurricane Sandy (2012) or Katrina (2006).

2. The international nuclear liability regime

Joe average is aware that states operating civil nuclear plants adhere to international conventions to framework the nuclear third party liability regime of their national nuclear operators.

In the fifties and early sixties most of the “nuclear” states adopted either national, either international conventions regimes.

To date 3 international conventions are ruling the matter:

3. The 1997 Convention on Supplementary Compensation for Nuclear Damage (CSC) Not yet in force as only 4 contracting and 15 signatory states to date.

These 3 conventions form the cornerstone of the international nuclear liability regime by setting the basic principles that are now widely recognized and accepted:

- Strict liability of the nuclear operator or nuclear transporter;
- Exclusive liability of the nuclear operator or nuclear transporter;
- Limited liability in the amount;
- Compulsory financial security of the liability by way of insurance, fund, bond, guarantee…
- Limitation of liability in time;
- Exclusive jurisdiction of the limits of the state in whose territory the incident occurred;
- Uniformity of applicable law and equal treatment of all victims.

3. The Japanese nuclear liability regime

Fostered by the Hiroshima and Nagasaki bombings and conscious that no civil nuclear program would have been adopted by the public opinion, Japan has opted for its own national third party legislation of which the headlines are:

- The nuclear operator is strictly and exclusively liable for nuclear damages;
- The nuclear operators’ liability is unlimited;
- Liability must be secured for JPY 120Bn by private insurers (± EUR 1Bn – USD 1,3Bn);
- Possibility for operators to sign “assistance” agreements with the Japanese Government for the unsecured part (exclusions and limits in excess);
- Operators liability exemption and transfer to the government for damage due to a ‘grave natural disaster of an exceptional character or due to an insurrection;
- Limitation of declaration of damage (3 years after knowledge of the damage and person liable);
- Triple claims declaration method: to the operator, to a local court or to the Dispute Reconciliation Committee.
4. TEPCO’s insurance and victim/damage indemnification

TEPCO, following the Japanese legislation at the time of the loss, had secured its nuclear third party liability by an insurance policy issued by the Japan Atomic Energy Insurance Pool (JAEIP - Japan’s 23 leading insurance companies) for the compulsory limit of JPY 120Bn.

The exclusion of “grave natural disaster of an exceptional character” has been invoked rapidly by JAEIP to decline any claim and thus protecting its members and its reinsurance schemes with the other national pools, mutuals and direct reinsurers. The annual premium was said to be approximately USD 3M.

Would this exclusion mean that victims were set aside of any indemnification by TEPCO? Surely not!

The Compensation Act and the guidelines of the Reconciliation Committee were two mechanism helping TEPCO to, efficiently and voluntary, settle disputes over compensation of nuclear damage. By the end of 2012, TEPCO had received approx. 260,000 individual request and approx. 120,000 applications from corporations and sole proprietors. Almost 80 % of all the cases were already settled by end of 2012. As TEPCO could not bear the entire financial weight of the indemnification, the Japanese government started making provisional payments to the victims acquiring a right to claim compensation to TEPCO. Finally, in summer 2012, TEPCO was placed under temporary state control by the acquisition of JPY 1 trillion of their preferred shares. In the meantime, the bonds issued by the Japanese government total JPY 5 trillion (EUR 55Bn).

5. Global impact on insurance market

Due to the widespread exclusions or limitations for earthquake, tsunami and contamination by radioactive material, one can wonder if such national and international catastrophe can impact the global insurance and reinsurance markets. It did severely hit the Japanese household market in many ways. The international property and casualty (re)insurance markets were also hit but in different ways.


As mentioned earlier JAEIP declined, by reason of contractual exclusion, any claim from TEPCO. TEPCO was also informed by the JAEIP that they would not renew TEPCO’s nuclear liability insurance for 2012, putting a serious threat on the entire decommissioning work of the Fukushima reactors. Initially, TEPCO thought to put USD 1,3Bn (JPY 120Bn) escrow with the Japanese government to cater with it but this was another financial limitation in TEPCO’s available cash.

Finally in January 2012, TEPCO deposited a JPY 120Bn insurance coverage from a private sector insurer with a rumoured USD 30M annual premium (x10). The consequence is important. It means that some important insurance capacity has been found outside the traditional pooling system. The backside of it is also that it can be seen as higher premium is not an obstacle to obtain a nuclear liability protection. Legitimately other countries may expect significant increases of their nuclear liability premium (even with the pools).

Courtesy of 123RF
2. Business Interruption and Contingent Business Interruption
The financial and organizational consequences of this catastrophe on the Japanese and worldwide industry were evident. Business Interruption (BI) in the local market is either very restricted (exclusions) either not taken. Foreign insurers in Japan offers BI coverage for large multinational corporations but it is very likely that many claims have been dismissed due to general earthquake, tsunami restrictions or exclusions.

Many corporations with mature Risk Management approaches and sophisticated insurance wordings have filled Contingent Business Interruption (CBI) claims to their insurers. The “just-in-time” supply processes for critical parts and the big hit suffered by a.o. the automotive parts, electronics, semiconductors have partially disrupted downstream manufacturer’s activities in many countries. The insurance industry is very quiet, for not to say silent about these impacts… We are assuming they could totalise well over USD 1Bn cumulated losses.

3. Marine and Aviation
The Tohoku event will most probably provide one of the most important marine reinsurance losses ever impacting hull and machinery, cargo and wreck removal covers. The total hull losses in the tsunami are valued USD 300M with at least ten ocean-going vessels considered total loss. In addition 90 ocean-going vessels and thousand of smaller fishing vessels were stranded inland. Most of the latest were not covered by an insurance policy.

Marine cargo losses are also believed to be important as thousands containers were damaged, washed away or inundated in the Sendai port and other regional harbours. Same fate applied to many other products (raw materials, semi-finished products, finished products, food…) whilst in transport or transit.

The impact on the aviation insurance industry (mainly Japanese Aviation Insurance Pool) is very limited. No large aircrafts have been damaged in Sendai airport and only 2 Boeings have been lightly damaged in Tokyo International airport. Seventeen smaller aircrafts didn’t survived the wave in Sendai.

4. International Facultative Reinsurance placements
The Fac Reinsurance placement affected by this claims are limited with the notable exception of East Japan Railway Company and TEPCO (for its non-nuclear generating and transmission assets).

5. Local Japanese market
a. Food, agriculture, fishing industries, consumers: These industries are organized in regulated cooperatives. Insurance coverage/packages for the members are very often negotiated by the cooperative and include very frequently the earthquake coverage although limited to a fraction of the Total Sum Insured (eg. 50 % or 25 %). Consequential damages (loss of income) are usually not covered. Most of those schemes are reinsured for large part in the global reinsurance markets. The impact here is very hard to establish.

b. Household: Earthquake cover can only bought as an additional cover to a standard fire policy. It is believed that only 25 % of Japanese households are covered by this additional cover which is ceded 100 % to the Japanese Earthquake Reinsurance Company (JER – USD 30Bn reserves) up to JPY 115bn (USD 1,48Bn). Above this threshold there is a 50/50 sharing mechanism between the Japanese government and participating non-life insurers. The Tohoku earthquake and tsunami have destroyed 129,225 buildings (totally collapsed), with a further 254,204 buildings ‘half collapsed’, and another 691,766 buildings partially damaged.

c. Auto: Minimal impact (although over 200.000 cars and trucks have suffered partial or total damages) as individuals and corporations rarely purchase the separate natural hazard insurance coverage.

d. Life: Also for life insurance the facts and figures are telling us that the insurance impact might be lower than expected. First at all, the age profile of the casualties points out that approx. 65 % of the casualties were older than 60 years and 45 % older than 70 years. Secondly, although payouts will be carried out on the life and groups (life) policies and death compensations on personal accident covers, insurers are expecting that some compensation will never been claimed by default of any claimant (no direct heirs).

5. Conclusion
Many factors ranging from the complex Japanese insurance structure, over the particular Nuclear Liability and Compensation Scheme to the particular sociological distribution of the claims have mitigated the impact on the global insurance industry. Best estimates foresee the total bill not to exceed USD 35Bn. This number can now tentatively being broken down as follows: residential earthquake losses amounts USD12 Bn, other Japanese non-life coverages amounts USD7.5 Bn gross of reinsurance, international non-life impact amounts USD 2.5Bn net, cooperative claims totaled USD 11Bn and another USD 28Bn comes from life insurance claims.

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News from the Global Power Network

In London

David Waters
Client Service Advisor

“David, tell us more about your past experiences?
I have been in the insurance industry for 14 years sharing my experience on both the Underwriting and Intermediary side where I have been an Accounts handler and Data Analyst. I hold the CII Certificate in Insurance and am on schedule to pass the CII Diploma in 2013.

I started my career as a Reinsurance Technician processing reinsurance recoveries at the Lloyd’s Syndicate Faraday. I then joined Advent Solutions in 2003 handling accounts with high volume insurance products where I gained experience in report writing and Data Analysis. I became involved in the renewable insurance sector in 2009 when I joined the Underwriting Agency GCube who focuses on renewable energy risks. My role at GCube began as an Accounts Handler dealing with premium and claims transactions and it quickly developed into management information reporting which helped analyse business performance. I went on to specialise in reporting and eventually assumed responsibility for most other reporting output and data quality monitoring.

Why did you join the Global Renewable Team at Aon?
I was already aware of the strong presence and technical expertise that Aon have in the Renewable sector so when I heard there was a vacancy I was delighted to take up the opportunity to join an innovative and dynamic team. I joined the team at the beginning of March 2013 as a Client Service Advisor reporting to Tom Sexton. I bring with me a number of transferable skills being familiar with London market slips, the types of renewable insurance products, and claims commonly seen in renewable risks. I am sure this knowledge will be a sound platform for integration into the team at Aon.”

“We are very pleased to welcome David to our team. He has unique skills around technical data analysis that enhances our ability to manage our statistical benchmarking data, and his experience in working for a renewable energy underwriting agency provides us with invaluable underwriting capabilities to support our own market facility. In the short time he has been with us he has already proved his worth, and we are looking forward to further integrating him into our renewable energy network.”

Tom Sexton – Head of Renewables, GBC

Hugh McManus
Client Manager

Hugh, please tell us about your background?
For the past 22 years I have been involved in Construction & Engineering insurance, coming initially from a claims background. This has given me a full perspective on the services we as a broker offer, and of our clients’ needs, in order to ensure a successful construction project. Having previously worked for Sedgwick, JLT and Aon, I joined AJ Gallaghers, and then RFIB Group, where I assisted in establishing new Construction & Engineering insurance Divisions.

In this time, I gained significant experience in the production, placement, broking and servicing of annual and project specific construction & engineering covers for contractors, principals and major projects, both in the UK and internationally. In addition, this has helped me develop a detailed knowledge of the UK and international insurance and reinsurance markets.

So this is your second term at Aon – What made you come “home”?
I rejoined Aon in April 2011, to assume the role of Client Director for the UK’s largest housebuilding contractor, and also work within the Projects and Contractors team.

When I was approached by Darren to join his team in February 2013, I had no hesitation in accepting, and I now look forward to transferring my skills and experience to the Power Construction team going forward.

Finally, what do you believe the London market can offer our clients today?
It is fair to say that London has lost some pure pricing edge in recent years, with the emergence of markets in the Far East and Middle East. However, with the increasing technical complexity of power projects, together with the growing requirement for ‘A’+ rated security, London underwriters are well placed to fully offer their group’s capacity in the most comprehensive manner. At Aon in London, we are of course best placed to coordinate a global marketing approach for our clients – I believe it is the future of London and more importantly, the best for our clients.

“We are delighted that Hugh has joined our team within Aon. He brings further strength and depth to our Power team with his 20+ year knowledge of construction project idiosyncrasies”

Darren Marshall – Head of Power Construction, Power GBC
In Sweden

We are very pleased to announce the hiring of two new Associates in the Aon Stockholm Office. David Lindqvist and Olof Mångs will work closely with Global Broking Centre in order to strengthen the relationship with major Nordic power companies. Following earlier success in attracting the growing renewable energy sector this will also form an important part of the Business Plan. David and Olof are joining from previous positions at Willis. With their experience from both conventional power as well as renewable they are well positioned to develop the Swedish power portfolio.

In Turkey

Yucel joined Aon Turkey to lead AGRC activities and to support developing Aon’s energy insurances share in Turkey. He studied BSc. in Mathematics in Turkey and then he started his career with Tupras (Turkish Refinery Company) and then worked for Unilever. He then went to Canada to study Msc. in Statistics and MBA in Vancouver. After graduate studies, he worked for BC Hydro in Vancouver for 9 years, initially as Treasury Manager and then as Enterprise Risk Manager. Yucel returned to Istanbul in 2009 where he joined Enerjisa as their Risk Management and Insurance Manager to develop and manage the company’s risk management and insurance programs. Yucel is CPA from Washington State U.S.A and CIA from Canada and certified risk manager from GARP. After his ~ 15 years experience in the energy sector with large integrated power utilities in the areas of treasury and risk management, he decided to move to Aon Turkey to further develop Aon’s Turkeys market share in risk consulting and energy insurances areas.

David Lindqvist
Director
Aon Sweden AB

Olof Mångs
Senior Account Executive
Aon Sweden AB

Yucel Cakmur
Senior Director
Aon Turkey