



CONSTRUCTIVE VIEW

JLT'S CONSTRUCTION INSURANCE WHITE PAPER ISSUE 2

Months	1	2	3	4	5	6	7
Design	█						
Delivery		█					
Foundations			█				
Erect Building				█	█		
Erect Machinery						█	
Testing							█
Storage Silos							█

Claims Example

In the event of a claim under the DSU insurance, insurers will only reimburse the principal to the extent that they have actually suffered a loss. Forensic accountants may be used by insurers to assess the actual loss sustained by the insured and will take into account seasonal and market fluctuations in the business performance.

Final claim settlements will also be subject to the deduction of any concurrent and/or uninsured delays and the application of the policy time excess.



DELAY IN START UP INSURANCE

The second of JLT's series of white papers introduces the basic principles of delay in start-up (DSU) insurance and the factors taken into consideration by insurers when assessing a DSU claim

INTRODUCTION

If damage occurs to a project, from an insured peril, the cost to repair the damage would be met under the projects material damage insurance. However, costs incurred by a principal following any resultant delay in completion to the project would not be covered. DSU insurance protects principals from the financial consequences of such delays.

HISTORY

Having grown steadily in popularity since first emerging in the 1980's, demand for DSU insurance has risen significantly in the last decade.

Part of this rise can be attributed to governments increasingly seeking to involve the private sector in the development of social infrastructure projects through PFI/PPP contracts where financiers on the project insist on DSU insurance to protect their interests.

The global economic downturn has also contributed to this rise as it has increased risk aversion in the global capital markets. With unpredictable weather patterns and operational

hazards increasing the chance of a project being delayed, project owners are increasingly using DSU insurance to mitigate the financial impact of delays to their projects.

KEY TERMINOLOGY

Insured

The entity that is likely to suffer a financial loss if completion of a project is delayed. Project owners typically purchase DSU insurance although contractors can also be an insured if they have entered into a concession contract with the project owner.

Indemnity Period

The agreed duration that the DSU insurance will provide cover for. This period commences from the SCOD and should be sufficient to cover the maximum rebuild period envisaged following indemnifiable loss or damage to the project - usually a catastrophic event occurring during the final stages of the project.

Sum Insured

The agreed limit payable under the DSU insurance. The sum insured should

represent the greatest financial loss that can be incurred during the indemnity period.

Excess

The agreed element of a delay to a project that is self-insured. The policy excess is usually measured in time rather than a fixed monetary amount. Therefore, no loss is paid for delays until the total delay exceeds the time excess. Thereafter all delays are paid in full.

SCOD

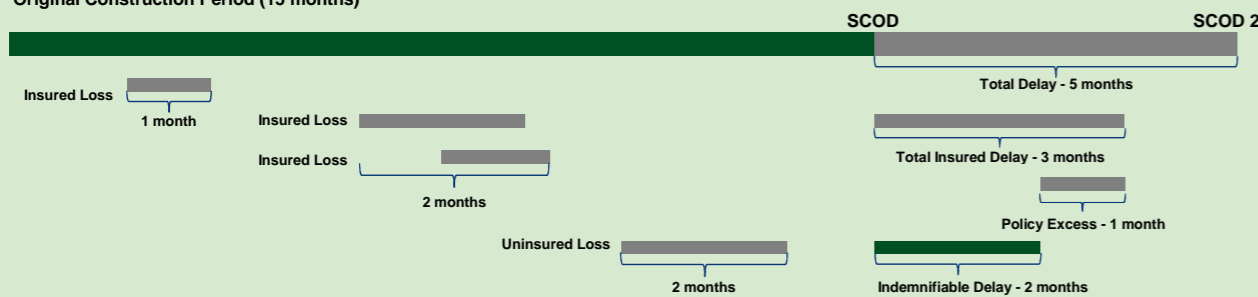
Scheduled Commercial Operational Date

DSU

Delay in Start Up insurance. Can also be referred to as Advance Loss of Profits (ALOP)

The global economic downturn has accelerated the trend of privately financed projects seeking to safeguard anticipated returns on investment through DSU insurance

Original Construction Period (15 months)



CONTACT

STEVE OSBORNE
 Managing Director
 - Construction/Surety
 T: +61 2 9290 8063
 E: Steve.Osborne@jlt.com.au

PETER JEEVES
 General Manager
 - Technical and Marketing
 T: +61 7 3246 7506
 E: Peter.Jeeves@jlt.com.au

Jardine Lloyd Thompson Pty Ltd
 ABN 69 009 098 864 AFS Licence No.226827
 Level 11, 66 Clarence Street, Sydney NSW 2000
 T: +61 2 9290 8000 F: +61 2 9299 7280
 www.jlt.com.au

The information contained in this article, which is current as at the date of publication, provides only a general overview of subjects covered. It is not intended to be taken as legal advice or advice regarding any individual situation and should not be relied upon as such. Insureds should consult their insurance and legal advisors regarding specific coverage issues. All insurance coverage is subject to the terms, conditions, and exclusions of the applicable individual policies.

BASIC PRINCIPLES

1. DSU cover is only triggered by a delay in completion to a project due to an indemnifiable loss under a material damage insurance e.g. Contract Works
2. There can only be one DSU claim during the original project period. However, the delay may be made up by a number of indemnifiable events that have occurred during the construction period.
3. A DSU loss can only occur once the project has been delayed beyond the original SCOD, although the event(s) that caused the delay may have occurred many months previously, during the construction period.

SCOPE OF COVER

The scope of cover available under DSU insurance can vary depending on the specific financial consequences a principal may experience due to a delay to completion. For example;

- Gross Profit - Enterprises with high variable costs such as

manufacturing and service organisations

- Loss of Revenue - Enterprises with high fixed costs such as hotels and power stations
- Loss of Rental - Enterprises with a specific income stream such as property developers
- Fixed costs and/or debt service - Enterprises where cash flow protection is critical

Increased Cost of Working

In respect of all of the above options, increased cost of working (ICoW) may be incurred to speed up remedial action in an effort to reduce or avoid the delay to the project and in consequence reduce or avoid the loss. This expenditure would be met by the DSU insurance provided that it was incurred for the sole purpose of avoiding or diminishing the loss and it did not exceed the amount saved i.e. the expenditure was economical.

Additional Increased Cost of Working

Available as an extension of cover and whilst still needing to be reasonably

incurred, additional increased cost of Working (AICoW) provides broader cover than ICoW in that it covers expenditure which does not necessarily reduce or avoid the loss i.e. there is no "sole purpose" test, and which may be uneconomical.

OPTIONAL EXTENSIONS OF COVER

Projects can experience delays from events that fall outside of the scope of the material damage insurance meaning that cover under the DSU insurance would not be triggered. Policy coverage can therefore be extended to include delay due to;

- Failure of public water, gas or electricity supply
- Prevention/denial of access
- Damage at suppliers or customers premises
- Fines, penalties and fees
- Infectious disease, murder and suicide



THE CLAIMS PROCESS

WHAT IS A DSU CLAIM?

In order for a DSU claim to become payable three key criteria must be fulfilled

1. An event indemnifiable under a material damage policy e.g. Contract Works
2. The resultant delay exceeds the DSU policy time excess
3. The delay causes a resultant loss to the insured. e.g. Gross Profit

SEQUENTIAL VS CONCURRENT EVENTS

There can only be one DSU claim during the original contract period, but the delay may be made up by a number of indemnifiable events occurring during the construction period. The delays suffered by a project from multiple physical damage events will therefore be aggregated, leading to one overall delay period beyond the SCOD.

Delays need to be sequential in order for

them to be aggregated for a DSU loss. For example a delay to the foundations followed by a delay in constructing the walls that sit on the foundations would be aggregated to form a single DSU loss.

Concurrent events such as a fire on one side of the site and a flood on the other would not be aggregated if the repairs went ahead independently, only the longer delay in completion of the two events would be included within the DSU claim.

A logic link bar chart is often produced which shows how different activities undertaken interrelate to other activities as illustrated in the chart below.

UNINSURED DELAYS

Delays can also occur to a project from events that are not covered by the material damage insurance such as industrial action, slow progress, redesign delays, project enhancements, late supply of materials or inadequate funding.

The overall delay to the project may therefore be a combination of Insured and uninsured delays. The DSU insurance will only respond to the insured element of the delay and therefore the uninsured element of the delay will be excluded from the claim.

REINSTATEMENT OF COVER

The DSU sum insured is invariably an aggregated limit. Therefore, once a DSU claim has been triggered, a new DSU policy will need to be arranged to provide cover for further delays from insured events during the reinstatement period.

Whilst the reinstatement of the sum insured can be agreed by insurers on an automatic basis, the unique circumstances that surround a DSU claim means that reinstatement premiums must be negotiated on the merits of the specific loss circumstance.