Why choosing the right insurance formula is essential to mining projects

The turnaround in the mining and resources sector was predicted by the World Bank in early 2017, when it forecast strong gains for commodities including energy and metals, on the back of tightening supply and strengthening demand - a prediction which has been borne out through the year.

123rf.com

The simultaneous historically low interest rates have facilitated a substantial increase in capital infrastructure projects related to mining across the globe.

“After a four-year slowdown, the last few months have seen the revival of a series of mining infrastructure plans and feasibility studies for greenfield developments together with some substantial upgrades to existing operations,” says Paul Pryor, Aon’s global mining practice leader.

“Many [projects] had been mothballed during the slowdown to rein in costs but resources companies are now again moving to upgrade existing facilities to increase mine life viability and operations and break ground on new developments,” he adds.

During this resurgence of the mining sector, it is critical not to overlook the importance of robust insurance cover.

“Insurance coverage and a sound risk management strategy are essential for the entire project lifecycle. It should transition seamlessly through the design and early works phase, into the construction phase and finally into commercial operation. Without it, the upside of the mining resurgence could be short-lived,” Pryor says.

Whole of project approach

“Forward-thinking mining companies work with brokers from the get-go. They engage brokers when working through feasibility studies and all the way to production to ensure ‘whole of project’ protection. It’s the best way to make sure insurance is properly costed for the project and that no elements of coverage are overlooked,” Pryor explains.

“This is particularly critical on large-scale construction projects with lots of moving parts and when there is not always a clear delineation between the phases. It may be that there is a phased handover and stepped commissioning of completed works so that roads, rail, port facilities and site accommodation are brought on stream at different times,” he adds.

Working with specialist brokers guards against insurance oversights which are possible as the lines between construction and operation can be blurred. Construction activities may also continue whilst mining development is being undertaken, and ore can be extracted, ready for processing, while construction is still taking place.

“It is vitally important that there are no gaps in coverage as the project transitions from construction to phased, and then to full-scale operations. Managing this seamless transition from the construction phase to operational is made more complex in projects where individual contractors are responsible for their own insurance. In larger projects, this sprawls across potentially hundreds of entities making it extremely hard to manage, and any opacity regarding contractor coverage can increase project risk,” says Pryor.

“Principal-controlled insurance is far more manageable and transparent, and highly recommended, particularly for larger projects where there is almost certainly a phased migration from the construction to the operational phase,” he says.

“Streamlining mining construction risk management is an emerging trend which sees some insurance companies offer a single policy that offers coverage through construction and the first six or 12 months of operation. Because there is no handover from the construction cover to the operational cover, mining companies have peace of mind that they are properly covered through the lifecycle. Not all insurers offer this alternative – and some insurers will cover construction and operation, but not always in the same proportion.

Advanced business interruption protection

“The challenge from an insurance perspective on construction mining development/construction projects, particularly where there is a requirement for full revenue type cover, is that when there has been a delay due to construction over-runs, insurers may well argue that the organisation has not in fact lost the opportunity to mine the ore; rather that the ore is still in the ground and so there is merely a revenue delay. Arguments could also be made that additional profits could accrue if the commodity price continued to increase in the period until the mine became operational.”

Whatever the argument, full revenue claims are inevitably highly contested and often settled on a commercial basis.

“Careful analysis of the anticipated earnings forecast, along with any built-in assumptions such as commodity prices and exchange rates, is essential when seeking the most effective cover. It is possible to build escalation factors into coverage, of up to 25%, which would be reflected in the premium paid. This is a complex area – but the risks can, with careful consideration, be identified and managed without impeding the all-important opportunity for growth,” he says.

“It is essential to work with a broker for a comprehensive assessment of the most appropriate cover for each development.”