

Case Study: Aon's Assistance in Latin Finance Magazine's Financing Innovation of the Year (2018)

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Aon served as the insurance advisor and broker to CELSE on the Sergipe I Thermoelectric Power Plant, which consists of the development, construction, financing, ownership, operation and maintenance of a gas-fired combined cycle thermal power plant with total capacity of 1,516 MW in the town of Barra dos Coqueiros, Sergipe, Brazil. The Project also includes a 33 Km transmission line, and a gas pipeline, which connects a Floating Storage and Regasification Unit (FSRU) to the thermal power plant. The FSRU belongs to and will be operated by the natural gas supplier. CELSE's thermal power plant will be among the largest in Brazil when complete.

The project won the Latin Finance Magazine's Financing Innovation of the Year Award for 2018, due to the decision to switch financing strategies from local banks to an international bank acting as global coordinator and bookrunner for a capital market offering. This shifting financing strategy led to some complications as it related to insurance issues for the project.

In the latter part of 2016, the initial construction work of this thermal power plant was about to start, and it was then that Aon started to provide services to CELSE for the structuring of an insurance program and the drafting of a contract with the Engineering, Procurement and Construction (EPC) company.

As per Aon's suggestion, CELSE succeeded in altering the original insurance specifications in the project contract to an Owner Controlled Insurance Program (OCIP), except for the transport insurance, as the EPC company negotiated the use of its global program for this project. The OCIP model enabled the owner to control the insurance procedures and claims handling,

provide the adequacy of a tailor-made insurance coverage and lower the cost of insurance.

After an analysis of the major project risks, a comprehensive Construction Erection All Risks (CEAR) policy was negotiated with the insurance market. When the coverages were submitted to the EPC company for a thorough review, the policy was praised for its comprehensive coverage and adequacy for the project.

One of the most significant conditions included in this CEAR policy was the Manufacturer's Risks cover (faulty manufacturing, material defect and project error), even though the insurance market still considered the turbine model as a prototype.

A few months after construction of the thermal power plant commenced, once the main insurances had already been placed, financing negotiations were finalized with the Lenders (among them, the IFC and IDB). Lenders' insurance requirements are often perceived to be very demanding, and sometimes excessive, requiring coverages and endorsements that provide more coverage than may be necessary for the project; and it was not different in this case.

One of these requirements was the obligation to provide Delay in Start-Up (DSU) coverage for covered perils under the CEAR, Transport and Builder's Risk policies, with the Builder's Risk policy applying only to the manufacturing of the FSRU.

DSU insurance covers financial losses arising from delay in the start-up of the plant operations caused by losses insured under the CEAR, Transport and Builder's Risk policies.

However, the risk of financial losses from delays had already been analyzed by CELSE, which, at the time the insurances were contracted, had decided to self-insure this risk instead of transferring it to the insurance market. Additionally, the lenders' insurance requirement to procure the DSU coverage occurred after the CEAR, Transport and Builder's Risk policies had already been issued and in force. This presented significant challenges as the insurers would hardly accept to insure the coverage from delay on existing policies.

Complying with the Lenders' insurance requirements was necessary to obtain financing approval, yet the insurance markets were reluctant to provide the necessary covers which prompted Aon to create negotiation teams to handle the matter with the Lenders and the insurance market in order to obtain the inclusion of the DSU cover in the CEAR, Transport and Builder's Risk policies. This was critical to achieve the necessary approval for the financing.

The teams worked together with the Aon Global Risk Consulting team as back-up resources to prepare a qualitative and quantitative analysis of the major risks involved with the construction of the plant and the FSRU. This qualitative and quantitative analysis and the subsequent extensive negotiations aided in successfully convincing the insurance

markets to provide the DSU coverage in order to comply with the lenders' insurance requirements.

Specifically, Aon's efforts to comply with the lenders' requirements can be described as the following:

- Placed the construction insurance program that was completely accepted by the contractors due to the comprehensive scope of coverage and adequacy of limits.
- Obtained DSU coverage for the CEAR, Transport and Builder's Risk policies in an exceptional situation, given that it is not standard to obtain DSU coverage once construction has commenced.
- Prepared a well-structured engineering report to ensure that the Lenders were in agreement with the limits specified in the policies.
- Succeeded in negotiating the inclusion of several unusual insurance clauses required by the lenders with the insurance markets

In view of the foregoing, Aon is proud to be part of the financing operations process structured by CELSE, aiming to ensure the feasibility of this project, which resulted in CELSE having been recognized and awarded the "Financing Innovation of the Year - 2018" by Latin Finance magazine.

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