

Fronting/local content requirements



John Croucher, Offshore Underwriter

+44 20 3320 8879
john.croucher@ctplc.com

Local content requirements are an increasingly popular government policy in jurisdictions where oil and gas exploration and production is still a developing industry. Such a policy is aimed at balancing a desire for foreign investment whilst advancing local knowledge and skills.

Operators from more developed jurisdictions clearly seek opportunities in unexplored fields, whilst the exploration potential of developing countries is often used to attract investment in local people, services and infrastructure.

The challenges for offshore operators include not only to keep abreast of often rapidly changing requirements, but to ensure that they remain compliant with local laws without reducing their operational standards, either by employing crew that perhaps lack knowledge or experience, or by being obliged to employ service providers that are unfamiliar with ever more sophisticated operations.

One of the requirements that is often faced by our members is that their insurance cover must be 'fronted' locally at additional cost. This is a requirement whereby insurance for certain classes of business must be insured by a locally registered insurance company which will be reinsured, either in whole or in part, by a non-domestic insurer.

The initial questions that need to be answered relate to the scope of the local fronting obligations – this will include asking 'what is the scope of the activities is that would fall to be included under the relevant local statute?'. For example, would it include fixed platforms only, or does it extend to floating production systems? What about floating storage or offtake tankers, or support ships such as supply boats or AHTS. Also important is the jurisdictional reach of the relevant local statute – for example, does it apply to risks in the territorial waters or the exclusive economic zone of a particular jurisdiction?

We have had recent experience in the Standard Offshore team of arranging compulsory insurance fronting in a number of jurisdictions, including:

- Turkmenistan
- Mexico
- Kazakhstan
- Azerbaijan
- Vietnam
- Angola

In addition to this, Nigeria has been expanding its local fronting requirements recently, and we are investigating the extent to which recent legislation demands that P&I cover is fronted through a local insurance company. We will keep our member advised of these developments.

If there is an underlying poolable entry with the club, we are only able to front poolable cover and limits by using an entity that has been pre-approved by the International Group (known as a 'grandfathered' entity). If there is no such pre-approved entity, it may be that a fixed limit cover is required, which will usually be placed to limits defined under the operating contract of a particular ship or offshore unit.

If the unit is not poolable (such as drilling or production risks) we are not bound by the constraints of the International Group pooling agreement and can arrange a number of fronting solutions, albeit to a fixed limit, up to a maximum of \$1bn.

Where we are fronting cover with a fixed limit on a non-poolable basis, we would typically front the minimum limits required under contract in order to save the member costs in respect of local insurance taxes and fronting fees. The underlying club entry would sit behind the fronted insurance so that the member retains the limits of cover that they would usually have direct with the club.

It is unusual, but not unheard of, for the local insurer to retain some of the risk. Typically, we would seek to persuade the local insurers that they are not capable of retaining any of the liability themselves given that they are fronting P&I cover, with unlimited reinstatements of an approximate \$6.9bn limit in the case of poolable cover, or up to a \$1bn limit under the **Standard Offshore Rules**. This is usually sufficient for them to seek 100% reinsurance from the club.

Whether or not there had been some level of retention by the local insurer, we would consider ourselves to remain the primary ground-up insurer for the P&I risks arising out of the ship or unit and that the local fronting requirements really represent an operational cost for the member.

Where we arrange fronting, this is usually evidenced by including a clause in the certificate of entry noting the 'original insured' and the 're-insured' entities, and by signing a slip prepared by a local broker, including agreement between the member, the club and the local insurer that there is a premium cut-through clause, so that the premium due to the club does not get caught or delayed in the local jurisdiction, and a clear claims control clause making it unequivocal that the handling of a claim is to rest with the club.

Should you have any queries regarding fronting requirements or the impact that our local content requirements have on club cover, please speak to your usual contact at the club, who will be more than happy to help.