



Claim Denials – Why They Happen and How to Avoid Them

by: James A. Lauerman, President

One of the most enduring myths about aviation insurance is that many (if not most) claims are denied by the insurance company. To inject some reality into this perception Avemco Insurance Company has publicly reported our claim denial data for the past nine years. Many of you have analyzed those numbers and commented how much you appreciate our frankness about this unpleasant aspect of our business.

For the first few years, our format was to report on only the most recent year's numbers. For the past five years, however, we have changed the format slightly to include an analysis for the entire period. Over this time, the numbers are large enough to have gained considerable credibility. This analysis gives clear direction about how you can avoid having a claim denied.

The reason we go through this exercise is to educate our customers and our underwriters. Claim denials are something to be avoided, both for us, and for our customers. We are therefore trying to help our customers understand how they happen so they can avoid them. In addition, we use this data to train our underwriters to look for situations that might cause confusion so they can help avoid any such confusion in our customers' minds. Fortunately, this effort has steadily reduced the percentage of claims that are denied. Never a large number to begin with, we have cut the percentage of claim denials in half since we began tracking them in 2001.

I must point out that these are Avemco®'s numbers. If you are insured with someone else, the numbers will likely be different. To our knowledge, none of our competitors publicly report claim denial data. At Avemco, we do not deny a claim unless we believe there is a rock-solid contractual reason to do so. We do not deny claims with the hope that the customer will not bother to argue the point, or in an attempt to establish a legal precedent. We let the merits of each claim stand on its own.

2010's denied claims continued at an extremely low level. Of our 460 claims, only 6 (or 1.3%) were denied for all reasons. Over the past five years, the percentage of claims denied has never exceeded 1.5%. This likely represents about the minimum percentage that a company can expect in any year.

Historically, the reasons that claims get denied at Avemco follow the famous "80/20" rule, in which 80% of the claims are denied for only about 20% of the reasons. If you avoid those common reasons, your historic odds of a claim denial drop to almost nothing.

Those areas are:

Not an Approved Pilot Under the Policy

The single biggest reason for claim denials over the past nine years is that the pilot operating the aircraft at the time of loss was not an approved pilot under the policy. 16.7% of all claim denials are for this reason.

Aviation insurance policies (unlike your personal auto policy) are "named operator" policies. The reason for this is quite simple; the insurance company needs to know who will be flying the aircraft in order to properly underwrite and price their exposure. As a policyholder, be sure that anyone who flies your aircraft is approved to do so. If you are insured with Avemco, a look at your current Data Page, or a simple phone call or e-mail to us, can verify that he or she is an approved pilot.

Denials for this reason have been dropping steadily over the years, and in 2010 we had only one. A customer called and bought a policy stating that one person, a licensed and relatively experienced pilot, was the owner and the only pilot on the aircraft. Later, a claim was submitted indicating that the pilot in command at the time of the incident was in fact someone else flying on his first solo. That student was *not* named as an approved pilot. Incidentally, it turned out that the aircraft was not owned by the person named on the insurance application which also nullifies the contract of insurance. This claim was denied not only for the unnamed student pilot, but also for the misrepresentation about the aircraft ownership.

Excluding In Flight Hull Coverage

Over the past nine years, 15.1% of Avemco's claim denials have been because the loss was an "in flight" loss as defined in the policy, but the customer had purchased "excluding in flight" coverage for the aircraft. Excluding in flight coverage substantially reduces the hull premium, but there can be a steep price to pay in the event of an "in flight" loss. If you choose to purchase excluding in flight coverage, be sure of what is and what is not covered by understanding the definition of "in flight." (Our policy definitions can be read in our policy on our website at avemco.com) A better alternative is to buy "in flight" coverage and avoid the problem altogether.

In 2010, two of our denials were for this reason. On the first, the customer had called about a year before the incident requesting a reduction in coverage to excluding in flight hull in order to save money. Our underwriter explained the difference in coverage and the customer still decided to make the change to his policy.

continued on page 2

On the second, the customer had been insured with us for 16 years with excluding inflight hull coverage. Fortunately for him, the premium he had saved over that time was significant enough to make a major contribution to the cost to repair the aircraft.

Mechanical Wear and Tear

16.7% of historic claim denials are because the “loss” was due and confined to a mechanical breakdown which is not covered under any property casualty insurance policy. Ensuing loss as a result of the breakdown *is* covered, but the mechanical failure itself is not. Put simply, property and casualty policies are not meant to cover maintenance issues.

We had two such claim denials in 2010. Interestingly, in both cases the pilots experienced engine failures and successfully landed the aircraft without any damage other than the engine failure itself. That is a rare occurrence and to have it happen twice in one year is certainly a statistical anomaly for us. It is also testimony to the skill exhibited by both pilots.

Despite the good fortune of these two pilots, however, we would remind all pilots that their *first* priority is their safety and the safety of their passengers. We would much rather pay for a damaged or destroyed aircraft than to have anyone injured in a desperate attempt to avoid damaging the aircraft.

Misrepresentation

Historically, 12.7% of all Avemco claim denials are because of a material misrepresentation on the insurance application, either when the policy is new or at renewal. When a person buys or renews an insurance policy, he or she makes certain statements or “representations” to the insurance company. These statements are usually formalized in the insurance application. The insurance company then uses those representations to underwrite the risk. If those representations are false, it is impossible for the insurance company to evaluate its exposure and the customer is likely voiding their coverage. In the majority of cases the misrepresentation was that all pilots had a current flight review when in fact the loss pilot did not have a current review when the application was signed.

It is important to note that Avemco, unlike many of our competitors, does not have a policy exclusion for an expired flight review occurring during the policy term. Instead, we ask the question on each year’s application. So long as the customer tells us the truth on that application, their coverage is in force, *even if they inadvertently allow the flight review to expire during that policy year*. This avoids the “gotcha” claim denials that can occur with exclusionary language.

For the third year in a row, not one of Avemco’s claims was denied in 2010 due to misrepresentation. We believe this is because our underwriters are becoming very skilled in detecting situations in which misrepresentation might be occurring and resolving it before there is a claim.

Outside the Policy Period

Over the past nine years, 10.3% of Avemco’s claim denials have been because the loss occurred outside the policy

period. In most cases the customer failed to renew the policy, and in some others the customer was cancelled mid-term for non-payment of premium. We have worked continuously to make it as hard as possible for this to happen by implementing our popular auto-pay and auto-renewal programs, call out payment reminders, and making it possible for our customers to pay online 24/7 at our website.

The other reason for this category of denials is that customers sometimes file claims for damage that had occurred well before the effective date of their policy with Avemco. Obviously, that damage should have been covered by the insurance that was in effect when the damage actually occurred.

Fortunately, we had no claim denials for this reason in 2010.

Commercial Purpose Exclusion

Historically, 2.4% of Avemco’s claim denials are because the customer violated the “commercial purpose” exclusion in our owned aircraft or non-owner policies. While our coverage is broader in this area than most of our competitors, our policy is not a commercial policy. Again, this exclusion and the associated definition are available by reading our policy on our web site. In addition, our aviation underwriters are readily available to help clear up any confusion. Fortunately, for the fifth year in a row there were no claim denials for this reason in 2010.

In 2008, we introduced our Avemco CFI coverage for aircraft owners who engage in limited and incidental flight instruction in their own aircraft and Aircraft Trader for those who are buying and selling aircraft part time. These new coverage options are intended to bridge the coverage gap between the traditional non-commercial policy and a full blown (and expensive) FBO type of coverage. If you are engaged in these activities with your own aircraft and want to be sure of the appropriate coverage, please contact us.

In general to help avoid a claim denial it is smart to:

- Buy the coverage you need, tell the truth in making the insurance application, and keep the policy in force by paying the premium and renewing the policy on time.
- Make sure anyone flying your aircraft is approved to do so on the policy.
- * Understand that aircraft policies (like all property/casualty policies) do not cover maintenance issues except to the extent that those issues result in subsequent loss.
- Read the policy carefully, especially the exclusions sections. If in doubt about coverage, verify with an Avemco Aviation Underwriter.

Claim denials are extremely rare. Since we have been educating our customers about why they occur, we have been pleased to see their number decrease even further. With a little understanding and care, they can be almost entirely eliminated.