Insuring BIG Risk

The Vertical Placement:

By Thomas H. Chappell

Have you ever wondered which underwriting company is strong enough to provide coverage for the loss of an airliner? Many airliners carry as much as $1,500,000,000 in liability coverage. What about the small regional airliner? Many of these carry $200,000,000 in liability limits. What if it is just a 19-passenger seat turboprop used in general aviation? Sizable liability limits are still the norm at $50,000,000 and up.

Over the last few years, many insurance underwriting facilities have experienced a great shrinkage in their capacity to cover those risks with high exposure to catastrophic loss. Aircraft like a 30-passenger seat Saab 340 or 19-passenger seat Jetstream 31 or 32 carrying large passenger loads are particularly scary to the underwriting community. To the underwriter, the definition of nightmare would be the crash of an aircraft carrying 30 business executives. This scenario is especially scary if the individuals are high income or high profile individuals like a professional sports team.

When presented with a risk of this nature, many underwriters will simply decline to offer a quotation. Others may accept only a small percentage of the risk. This reduced participation may be as small as two or three percent or they may accept as much as fifty percent or more. The insurance broker will present the account to as many underwriters as necessary until he has received commitments totaling 100 percent participation. This may take as few as two underwriters or eight, ten or more may be involved. By these means, each underwriter has put a cap on the maximum loss the company might endure. An account placed in this fashion is referred to as a "vertical placement."

Vertical placements have always been the norm when insuring scheduled airlines. It has only been in the last few years, however, that we have seen high seating capacity aircraft enter the general aviation industry to any large degree. Turboprop and older jet powered airliners no longer in use with the airlines have become very affordable and are being put to work in charter operations for corporate shuttle work or for the transportation of large groups of vacationers to resort areas. Some of this equipment is being reconfigured to 10, 12 or 14 spacious and luxurious seats from the original airline-seating configuration of 19 to 30 passenger seats. Although the seating may be reduced, thus reducing the maximum catastrophic loss, the underwriter may continue to be reluctant to accept one hundred percent of the exposure of the reconfigured airline equipment.

Underwriters have shared the exposure to loss on risks since the beginning of the insurance industry. The high risk of catastrophic loss and the need for high liability limits required by the airline industry, products manufacturers, military contractors and others have only one resource - vertical placement through the worldwide insurance market.

They say there is nothing new under the sun. In the insurance industry, this seems to be the case. What appears to be a new approach in the placement of the larger general aviation underwriting risk is just "old hat" to the traditionally high exposure industries.

Any time partners share in an investment, confusion can occur. Underwriters sharing in the vertical placement of a risk are no different. The burden then falls to the insurance broker to keep things straight. The broker must be knowledgeable in placing a vertical risk in order to avoid confusion. Each participating underwriter may sign on to the risk at a different rate or with different deductibles. Claims settlements may be slower to collect than if just one underwriter is involved. Simple coverage changes such as the addition or deletion of an aircraft may be confusing and a bit of an accounting challenge. A knowledgeable broker will arrange the placement so that only the "lead" underwriter's approval is needed in order to affect changes. Nevertheless, the system works and is the only way certain aviation risks can be insured. Q