

# History of Aviation Insurance

## cartel<sup>1</sup>

A combination of producers of any product joined together to control its production, sale, and price, and to obtain a monopoly in any particular industry.

Also, an association by agreement of companies having common interests, designed to prevent open competition.

<sup>1</sup> Black's Law Dictionary

The first aviation insurance policy was written by Lloyd's of London in 1911. The company stopped writing aviation policies in 1912 after bad weather and the resulting crashes at an air meet caused losses on many of those first policies. Since then the majority of aviation's insurance has been concentrated within just two insurance pools. Think of it, over 50% of all U.S. aviation was and is still written by either USAIG or AAU. In 1932, the New York Department of Insurance commenced an investigation regarding this concentration and, again in 1958, Congress also commenced an investigation into the aviation marketplace. The intent was to break up the cartel, much like Standard Oil a decade or so before.

The industry dodged the bullet by appointing a "committee" to work with first with New York Department of Insurance and then later with Congress, but that went away when Congress passed The McCarran-Ferguson Act which turned regulatory control of the insurance industry over to each individual state and **exempted insurance from anti-trust laws to boot.** (This exemption is enjoyed by only a few other "activities" such as unions, baseball and newspapers.)

Of course, the states resolved the issue by decreeing that aviation was an unregulated line of insurance, which means there is minimal oversight. To give you an example of just how incestuous the aviation industry is, more than half of all insurance regulators come from the industry and, after serving a period of time as a regulator, return to the insurance industry — typically in a more exalted position than when they left. Talk about the "fox guarding the hen house."

If this was any industry other than insurance, the Justice Department would be having a field day in court with these scoundrels facing more prison time than Bernie Madoff!

The result of all this is that aviation in the United States is the second most profitable line of liability insurance just after surety (principally, performance and completing bonds). All other liability lines would be delighted with an 80% loss ratio (percentage of dollars paid out in claims from premiums paid) whereas aviation has averaged in the mid 50% range for the past twenty plus years. That's thirty points more profit than the average!

Of course, over the years, other insurance providers have tried to break the cartel, but each time, the cartel has driven them out of business by savagely cutting prices until the new competitor fails and then they predictably revert back to their old ways.

Why we think that AAIRRG will survive is that with few exceptions, each new aviation marketing effort in the past have been 'generalized' whereas AAIRRG is exclusively focused on certified Part 145 repair stations. Please read on to learn why repair stations are a much safer risk than FBO's, charters, flight schools, firefighting, etc. This is the "miscellaneous" aviation class of business that repair stations have been lumped in with. So in effect, all these years, you have been subsidizing "others" with your enviable low rate of claims.

Resource: *Introduction to Aviation Insurance & Risk Management*, second edition, Alexander T. Wells and Bruce D. Chadbourne, authors