COVID-19 & AVIATION INSURANCE

WHEELS UP FOR AN UNCHARTED RIDE

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Remember when 2020 kicked off with a booming economy, low unemployment and record-setting stock values?

2020

Through the reverse zoom lens of time, that now feels like the experience of a distant age. As we head into the second quarter, the COVID-19 pandemic has become one of the most consequential and transformative events of our lifetime, and conditions are changing under our feet.

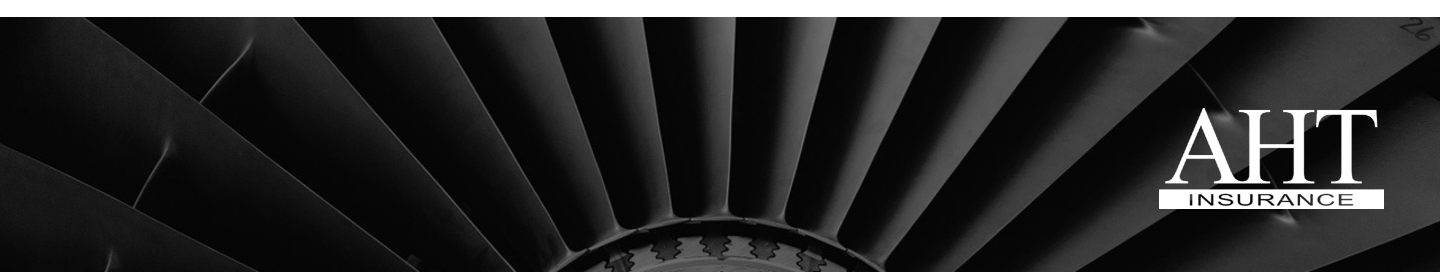
On the regulatory front, California is leading the nation in directives and guidance to insurers relating to COVID-19, including premium refunds, credits and reductions and, currently, nonbinding directives about reviewing business interruption claims. States may look to Workers' Compensation Insurance as a solution for the financial toll arising from the virus. Undoubtedly, there will be a variety of changes to both insurance regulations and insurance company approaches to coverage.

SHORT TERM | There is no lack of expert opinion explaining the nuances of federal support and predicting what happens next. We at AHT are focused on supporting customers through the short-term financial stress by keeping you informed about regulatory developments, evaluating potential coverage where needed and finding creative options for premium and cashflow relief.

LONG TERM | For the longer-term outlook, no doubt there is much speculation about how COVID-19 will change the environment.

In the first quarter of 2020, aviation insurance carriers were averaging between **20%-40% rate increases** and lowering their liability exposures with policy limit changes, such as cutting back line share or reducing passenger sublimits. At the same time, insurers were removing formerly generous "throw-in" coverages and shifting to more restrictive warranties and conditions, such as stringent pilot training requirements.

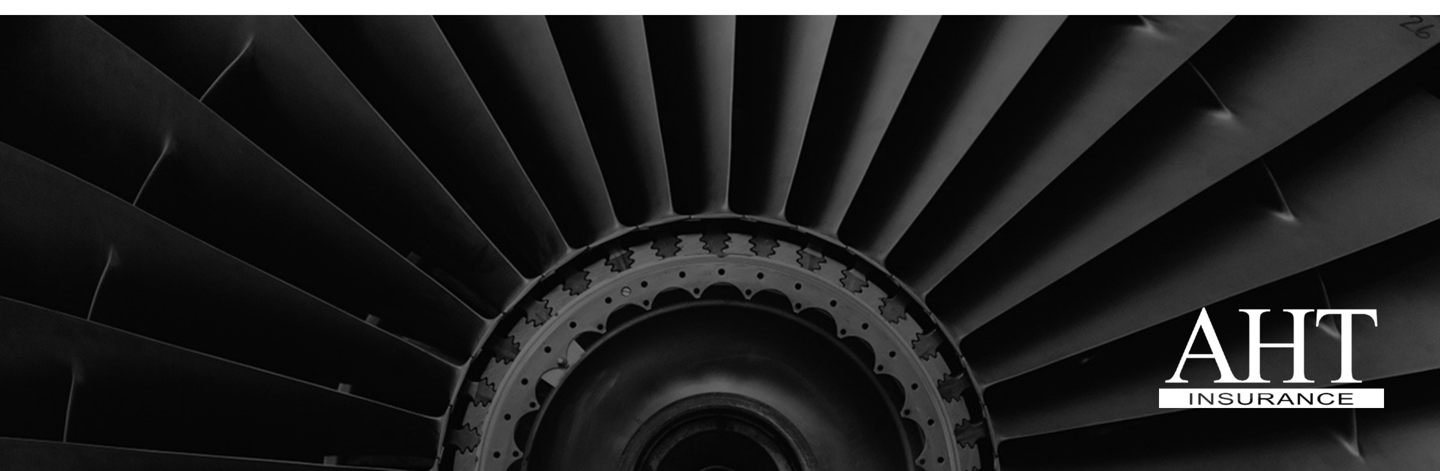
We don't expect this trend to change due to the recent crisis. The lower loss rates owing to inactivity during March, April and possibly May will be offset by premium returns. Discussions with the underwriting community yield mixed opinions, but almost all underwriters confirm that they don't expect any change to their pricing models. Indeed, unless there is new investment in the aviation insurance marketplace, which seems unlikely in the near term, we can expect rate increases to continue.



There are, however, some changes that need to be factored in as we move out of “shelter in place”. As air carriers and associated businesses move back into operation, we will be facing a severely hampered economy with an **unemployment rate at or above 18%**, according to some reports. Aviation insurers are members of the aviation community and have a stake in its continued health. Delivering 40% increases to the overall community during recovery will be very difficult. We expect that during the next phase, the insurance cost differential between policyholders will increase based on underwriter perceptions of operational quality. How you are perceived by the markets will become more important than ever.

Workers’ Compensation had been the one insurance product bucking the trend for rate increases. Workers’ Compensation rates were down almost across the nation, with ample capacity offered by the insurance markets. We expect COVID-19 may mark a turning point, for a variety of reasons. Claims activity will be down but financial stress tied to lay-offs could drive an increase in nascent allegations of injuries predating COVID-19. If COVID-19 is deemed compensable as an occupational disease under state workers compensation acts, which is likely given pending legislative initiatives for expanded coverage in several states, the effect on claim costs could be substantial. With new **jobless claims topping 5.2 million nationally for the week ending April 11**, pressure from increasing claim costs against declining payrolls could likely lead to a rise in filed rates, derailing the favorable trend in Workers’ Compensation pricing.

On the bright side, starting with California, states are directing, and we expect will ultimately mandate, that insurers offer midterm audits and afford premium relief to policyholders whose premiums are based on pre-COVID-19 payroll estimates. The National Council on Compensation Insurance and independent state regulatory agencies are working to address the question of payroll for employees who are being paid but are not working, as it relates to the basis of payroll for premium rating.



PRACTICAL CONSIDERATIONS

1 NEGOTIATING PREMIUM RELIEF DURING WORK SLOWDOWNS OR STOPPAGE

Auditable rating structures, such as Workers' Compensation policies – there is no reason to wait for the state to dictate a change. If your premium is based on estimates set prior to March 11th, press for a midterm audit and a restructure of your estimated deposit premium.

Scheduled asset coverage – look at increasing deductibles, negotiating reduced premium in exchange for coverage limitations, or potentially self-insuring assets when justified by a cautious risk/return calculus. In some cases, coverage can be placed in nontraditional ways at lower cost, such as insuring static aircraft hull coverage with a Property or Inland Marine insurer rather than through the standard aviation markets. This is a great time to get creative but, be aware that if your property is leveraged, you will need to review your lender requirements, which may contain limitations, such as maximum allowable deductibles or other coverage stipulations. Banks may need to be contacted before any major restructuring to negotiate flexibility on standard conditions.

For those operators who face downturns significant enough to ground some or all of their fleet, there are a variety of ways to cut costs. Some carriers are following lay-up percentages already written into policies and offering flexibility for a one-time COVID-19 credit and others are applying a universal lay-up percentage for COVID-19 inactivity, typically for a minimum period of at least 30 days. Your broker can assist with providing the details about how your insurer is responding to lay-ups, so you can understand how that will impact your annual insurance premiums.

Reducing your liability limits or employing a per-seat sublimit can be an effective cost-saving measure. Before considering this, engage your broker in a discussion about your operating environment, average passenger loads or other underlying factors driving your liability exposures, your own balance sheet and capitalization structure and recent court awards. Consider your regulatory or contractual minimum limit requirements, as these constraints can make reducing liability coverage problematic.

2 FAA GUIDELINE UPDATES DON'T AUTOMATICALLY CHANGE THE INSURANCE CONTRACT.

Be sure you have reviewed and understand your policy warranties and, if you need flexibility, contact your insurance representative. As always, be sure you receive written evidence that specific considerations have been afforded and for what timeframe.

3 COMMUNICATION IS KEY.

Be transparent with your insurance representative about the challenges, but also about the opportunities. If you can retool your operations in a manner that keeps revenues flowing, be sure to run the changes by your broker. There may be policy warranties, limitations or exclusions that need to be addressed.

4 YOU MAY HAVE SOME COVERAGE FOR COVID-19-RELATED LOSSES BURIED WITHIN THE BROAD REACHES OF YOUR INSURANCE PROGRAM.

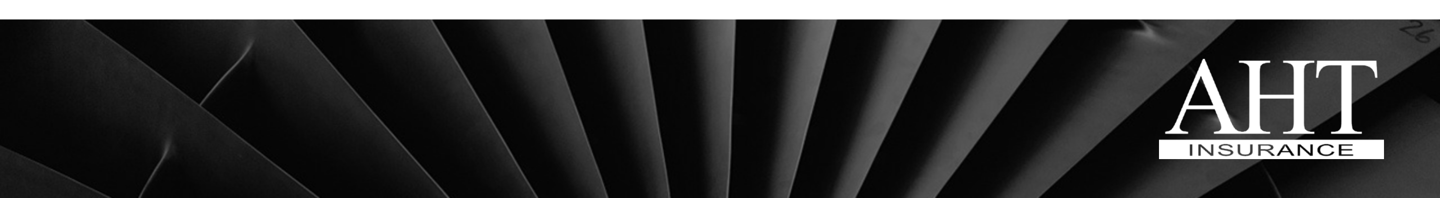
For example, Workers' Compensation policies typically include repatriation coverage, which may reimburse you for evacuation costs if employees were returned home from overseas assignments due to the virus. Other possible policy types that can be looked to for potential coverage include Business Travel Accident, Property/Business Interruption, Environmental/Pollution Liability and Management Liability/Directors & Officers/Employment Practices Liability.

Each insurer's policy language is unique and should be reviewed for coverage. Many insurers include specific exclusions for viruses, but even in those cases there may be other avenues to find coverage. When in doubt, an insurer should be put on notice for a claim.

5 FINALLY, QUARANTINE MAY HAVE SLOWED SOME CRIMINAL ACTIVITY, BUT CYBER CRIME IS ON THE RISE.

Increased online commerce and activity has exposed new vulnerabilities and increased exploitation from threat actors. From online meeting platform "bombing" attacks to an increase in phishing scams sending supposed "links" from regulatory agencies, extortion, denial of service attacks and hacking, we are increasingly under attack.

Beyond the direct protections afforded by a cyber insurance program, most cyber policies include free cyber coaching or resources to help mitigate cyber risks. As hard as it is to think about increasing your insurance costs, if you have been putting off making a decision to purchase Cyber Liability, now may be a wise time to look into options.



COVID-19 RELATED TIMELINE OF EVENTS

1/21/20 – First COVID-19 case reported in US

3/6/20 – Coronavirus Preparedness and Response Supplemental Appropriations Act passed. Authorized more than $8.0B in funding

3/11/20 – WHO declares Coronarirus COVID-19 a Pandemic. CDC announced awards of $560M to state and local jurisdictions to address COVID-19

3/18/20 – Families First Coronavirus Response Act signed into law. Available funding - $3.5B.

Intended to provide funding for virus testing, 14-day paid leave for workers affected by the pandemic, and increased funding for food stamps and other nutritional services

3/27/20 – Coronavirus Aid, Relief and Economic Security Act (CARES Act) signed into law, providing $2.2T in federal funding to address crisis

Suspends federal excise tax and fuel tax for general aviation operations; later extended to apply to both Part 135 and Part 91 operations from 3/28/20 through end of calendar year

3/31/20 – FAA announces they will not pursue enforcement against expired medical certification, effective through June 30, 2020

4/1/20 – FAA revises key procedures for drug and alcohol testing

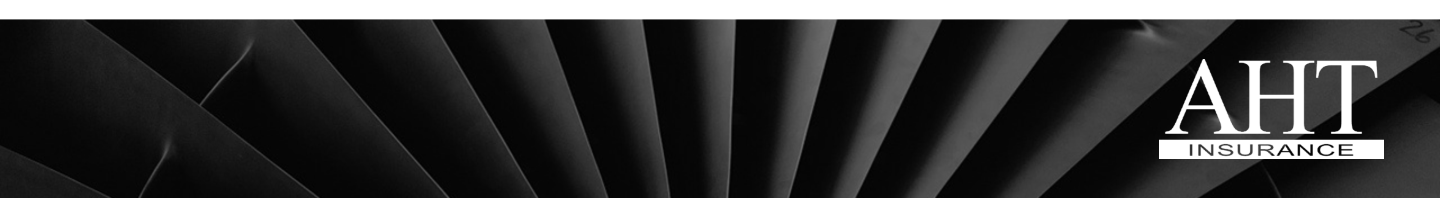
4/3/20 – Paycheck Protection Program enacted – lenders begin processing loan applications on a first-come-first-served basis. Funds theoretically available through June 30th

4/10/20 – Treasury Dept issues guidance aimed at ensuring that qualifying passenger air carriers have more flexible access to the CARES Act Payroll Support Program

4/14/20 – US DOT is awarded $10B in CARES Act grant funds for commercial and general aviation airports; $100M of this is earmarked for GA airports

FAA releases statement regarding use of two unproven medications in treatment of virus for pilots

4/16/20 – PPP initial grant, which theoretically was available through June 30th, is exhausted, with Congress currently in negotiations to appropriate more money to the program



SUMMARY

The cost of capital remains cheap and where just months ago talent was unavailable, it is now sidelined, waiting for the next opportunity. This signals optimism that once the US returns to some version of normalcy, business will rebuild quickly. Use the enforced downtime to rethink, retool and reassert discipline up and down your supply chain. Suppliers of all kinds, including financial products, are facing the same pressures and are more willing than ever to engage in creative problem-solving. If your insurance broker has not reached out to you to offer aid, request a block of time to discuss how your business is being affected and expect to receive assistance.

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