

Risk management in the air: What you need to know about insuring your drone

By **Tod A. Northman, Tucker Ellis LLP**

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Use of unmanned aerial vehicles has skyrocketed in the United States and globally. Because most UAVs are operated recreationally and are therefore exempt from most U.S. regulations, it is difficult to estimate how many are in operation.

However, one indication of the growth in UAV operations is the number of UAVs that have been registered with the Federal Aviation Administration. Although the requirement to register recreational UAVs was suspended for much of 2017, the total number of UAVs registered with the FAA has eclipsed 1 million since the registration rule took effect Dec. 21, 2015.

The total includes 878,000 recreational UAV users, who receive one identification number for all the UAVs they own, and 122,000 commercial, public and other UAV operators, who must register each UAV individually.¹

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Leaving aside recreational operations, the commercial applications for UAVs are myriad and exciting. Last year, a UAV was critical in saving six swimmers off the coast of France, and UAVs are proving invaluable in monitoring and fertilizing crops, in monitoring infrastructure — including pipelines and power lines — and to survey and map land and buildings.

The United Nations has recognized the value of UAV application for humanitarian, development and peacekeeping operations.²

Further, the FAA is developing regulations that will permit greater use of UAVs. In the United States, UAVs can currently be operated only within narrow parameters. For example, they must be operated within the visual line of sight of the operator and during daylight.

Further, they cannot be operated over people not directly involved in their operation, from a moving vehicle or at a height of more than 400 feet (except near a structure than is more than 400 feet high).

Existing FAA regulations are designed to minimize risk to people and property. As regulations permit greater flexibility of operation, however, risk to property and life from such operations will inevitably increase significantly. Consequently, it is incumbent that businesses consider how best to manage that risk. UAV insurance should play a central role in this regard.

UNDERSTANDING THE BASICS

The most important step to risk mitigation is to understand the risks posed. To do so, you will need to consider several questions: Who owns the UAV? What are the UAV's operational capabilities and limitations? Are the capabilities sufficient for the planned operation? Who will be operating the UAV? Does the operator hold all necessary certifications and licenses? What training has the UAV operator received, and how many flight hours has the operator logged? What operations are contemplated, and are they permitted by existing law? Where will the operations be conducted? Does the business have a UAV operational policy?

As with operations of automobile, watercraft and other type of aircraft, UAV operations are not covered by a commercial general liability policy. Generally, a CGL policy contains a specific exclusion for aircraft operations.

To cover UAV operations, a business must procure specific UAV coverage. As with manned aircraft operations, coverage for UAV operations is a specialized product that is best provided through aviation-specific brokers and underwriters.

Aviation insurance coverage is complex and nuanced. Historically, aviation insurers have sought to work only through specialized aviation insurance brokers, who are experienced with aviation insurers and flight professionals.

Policies that are adapted from CGL policies that are written by non-aviation property insurers may appear convenient and inexpensive, but aviation risks and exposures are unique and a best practice is to seek out coverage that is written on aviation insurance policy forms.

Aviation policies are customarily bespoke products. Appropriate coverage and the associated premiums depend on numerous

factors, such as the experience and training of the operator, loss history, whether the operator is an employee or a contractor, and the location and type of operations to be conducted.

There a number of possible aviation insurance coverages, starting with third-party liability coverage, which is primary, and expanding to hull and payload coverages, non-owned aircraft coverage and premises coverage.

In addition, manufacturers should maintain products liability coverage and professionals should evaluate the benefits of maintaining errors and omissions coverage. There are also specialized coverages for military, law enforcement and other government applications.

For operations of owned UAVs, third-party liability coverage is the “base” of the various types of aviation coverage. The coverage protects the insured from property damage and bodily injury claims that arise from the commercial operation of a UAV.

Liability limits can be obtained as low as \$100,000 and can be negotiated to as high as is required by the business and the operations. As the sophistication of the UAV has grown, limits have increased to as high as \$100 million per occurrence. Other coverage types may be added to the liability coverage.

For businesses that contract with a third party to provide UAV services, non-owned UAV coverage can provide a nice backstop to the UAV operator’s coverage. Any contract with a third party to provide UAV services should be scrutinized to ensure that risk is addressed appropriately.

Many UAV providers have cribbed and inelegantly adapted their form contracts from the internet. The contractor, who is by definition conducting commercial operations, should be required to carry adequate liability coverage.

As with other forms of insurance coverage, the business can require that an insurance certificate be issued and that the business be added as an insured party to the policy, to ensure that the coverage is in place.

Also, limitations of liability and other risk allocation provisions within the contract should be reviewed and reconciled to ensure that the business receives the benefit of the insurance coverage’s protections.

If your business owns one or more UAVs, obtaining hull coverage can provide protection against physical damage to the aircraft. Typically, this coverage is quoted on an “agreed value” basis.

The business, the insurance broker and the insurance company will agree on a value and insure the UAV based on that valuation. It is important to periodically evaluate whether the value of the UAV remains accurate. The fair market value of a 2-year-old UAV is not its purchase price; in fact, its value is likely to have dropped by more than half.

In the event of a loss, the insurance company can adjust the value of the UAV to its current market price and pay out only that amount less the deductible, even though the premium has been pegged to the agreed value.

Depending on the type of UAV being operated and the purposes for which it is operated, payload coverage can be critical. As the sophistication of UAV operations increases, such as by adding various sensors available for agricultural uses, the value and mission-criticality of the payload can exceed that of the UAV itself.

For a business that depends on the cameras or sensors that are designed to be carried by a UAV, payload coverage is imperative. This coverage is specially scheduled to the hull coverage and should list a separate value for each scheduled item. Establishing a separate value in advance of a claim helps to avoid later disputes. As with hull coverage, a deductible of between 5 and 10 percent of the insured value of the scheduled item will apply.

Depending on the type of UAV being operated and the purposes for which it is operated, payload coverage can be critical.

Non-owned coverage is important not only for the business that contracts with a third party to provide UAV services; the coverage also protects the operator who flies the UAV or flies payloads that are not owned by the operator.

As with third-party liability for owned UAVs, non-owned UAV liability coverage is the starting point. The coverage extends to claims of property damage or bodily injury that arise from the operator’s use of the non-owned UAV.

Note that the coverage does not protect against physical damage to the UAV itself, which the owner can protect against with the owner’s hull policy.

If the parties determine that the operator should carry the hull coverage, non-owned UAV hull coverage can be procured. This coverage mirrors owned hull coverage in that it covers physical damage to the non-owned UAV operated by the named insured.

If the parties adopt this approach, they should be careful to document the owner’s agreement to the insured amount, address which party will bear the deductible in the event of a loss, and document whether receipt of the insurance proceeds is the owner’s exclusive remedy.

Similarly, if the parties determine that the operator should bear the risk of loss to non-owned payload, non-owned payload coverage can be added. This coverage is particularly important when the operator carries expensive payload, such as specialized cameras or sensors owned by the hiring company or some other third party.

Depending on the insurer and the relationship with the insured party, such coverage can either be added on a case-by-case basis or through a policy endorsement to the policy that has a set coverage limit.

Either way, the parties should be deliberate to address in writing the same factors that are addressed with respect to hull coverage, such as which party bears the deductible.

Although we have been specifically considering UAVs, frequently the entire unmanned aviation system should be considered. Specialized equipment added to the UAV, such as computers, communication devices or other items associated with the insured UAV, can also be covered. Working with an experienced aviation insurance broker will help evaluate whether and in what circumstances such equipment might not be covered by an existing CGL policy.

Privacy is one of the frequently observed concerns about UAV operations. It has drawn media attention and resulted in lawsuits against UAV operators — even when they are operating within the bounds of their authority.

In response, aviation insurers have added personal injury coverage to protect operators against such claims. Similar to the CGL coverage that business people are familiar with, personal injury coverage protects UAV operators against claims for violation of privacy and copyright infringement, and likely less relevant related claims such as libel and slander.

The coverage does not replace best practices, such as alerting people near an operation that UAV activities will be conducted and answering questions and addressing concerns, which have proven effective in reducing complaints.

Particularly as operational limitations are reduced and operations are conducted near people, however, the coverage can provide valuable protection against what could otherwise be a ruinously expensive lawsuit.

COST OF INSURANCE

Liability coverage and hull coverage are the primary determinants of the cost of UAV insurance policies. That said, the cost for covering multiple UAVs under the same policy does not significantly increase from coverage for a single UAV, so long as the type and amount of flying is the same. The primary difference will be for the additional hull coverage for each UAV. That is particularly true if the same pilot will operate all UAVs.

Given the numerous factors that an insurer considers in quoting a policy, it is difficult to give a reliable estimate. With that caveat, however, for a commercial grade UAV with liability coverage limit of \$1 million, a premium of \$800 or so a year should be in the ballpark.

For comparison, for the same UAV operated by the same operator but with a \$5 million liability limit, the premium could increase threefold.

INNOVATION IN THE INSURANCE INDUSTRY

Because commercial UAV operations are so new, and perhaps because the impressive technology spurs fresh thinking, coverage options are expanding. For example, Verify is a new aviation insurance broker started by a 40-something tech entrepreneur who previously founded and sold two businesses.

Using a smartphone app, Verify offers UAV insurance that can be placed at the time of flight. Working only through the app, an operator can secure \$1 million in liability coverage for roughly \$10 per hour. Coverage is geographically specific and can be procured for longer periods, such as four or eight hours; coverage limits can be adjusted as well.

If a business is just getting started with UAV operations and is hesitant to bind a policy for a full year because the frequency of use is yet to be determined app-placed coverage is convenient.

For the novice UAV operator, however, this convenience may be overridden by the value provided by an experienced aviation insurance broker, who can walk through the operations and ensure that coverage appropriate to the business's goals is bound.

Another carrier has started to offer fleet coverage for operators who own and operate multiple UAVs. The coverage can offer liability and physical damage coverage on a cost-effective and convenient basis. The coverage provided by these policies is similar to the coverage provided by manned aircraft fleet policies.

As the regulations, technology and business needs of the commercial UAV industry continue to rapidly evolve, insurance providers are modifying and adding to their offerings to keep pace with these changes. Because aviation insurance is custom designed, insurers can tailor an insurance solution that fits an innovative use if the coverage does not already exist.

Insurance companies favor UAV pilots who follow best aviation practices from the general aviation industry. Practices such as writing and maintaining operating manuals and maintenance logs, and keeping a record of parts or add-ons, are regulatory requirements in general aviation and a good idea for UAV operations.

Meticulous recordkeeping, including proof of training or plans for future training, indicates to the insurer that the operator has a professional approach and is and will likely remain a safe flyer. By keeping meticulous records, you reduce the risk you pose with your UAV to other people, to inanimate objects and therefore to the insurance company.

As is the case with respect to car insurance, such professionalism will make it easier and more affordable to procure and maintain coverage.

NOTES

¹ Jonathan Vanian, *Drone Registrations Have Soared to a Sky-High Milestone*, FORTUNE (Jan. 11, 2018), <http://for.tn/2I2wBQW>

² *Does Drone Technology Hold Promise for the UN?*, UN NEWS (Sept. 6, 2017), <http://bit.ly/2oGBcAn>.

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ABOUT THE AUTHOR



Tod A. Northman is a partner in the corporate group at **Tucker Ellis LLP** in Cleveland. He counsels clients of all sizes in a variety of industries, with a particular focus in the areas of aviation, benefit entities and real estate. He can be reached at 216-696-5469 or tod.northman@tuckerellis.com.

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