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United States General Accounting Office
Washington, DC 20548

September 17, 2003

Congressional Requesters

Subject: Aviation Assistance: Information on Payments Made Under the Disaster Relief and Insurance Reimbursement Programs

As a result of the September 11, 2001, terrorist attacks on the United States, the airline industry incurred significant losses resulting from the temporary shutdown of the nation's airspace and passengers' apprehensions about flying following the attacks. The Air Transportation Safety and System Stabilization Act¹ (the Act) provided, among other things, \$5 billion in emergency assistance to compensate air carriers for their direct and incremental losses stemming from the attacks. The Act also authorized the Department of Transportation (DOT) to reimburse air carriers for increases in their insurance premiums.

On September 28, 2001, we completed and briefed you on the first phase of the work you requested, concluding that there was a reasonable basis to assume that the airlines' financial losses related to September 11 would exceed the \$5 billion made available in the Act.² Since then and pursuant to the second part of your request, we monitored DOT's progress in administering the disaster relief and insurance reimbursement programs and provided periodic status updates to your offices.

On September 3, 2003, we provided our final briefing addressing the second aspect of your request. Specifically, for the \$5 billion disaster relief program, we discussed the process DOT employed to help ensure that the payments it made were only for the direct and incremental losses stemming from the terrorist attacks. We also provided information about the losses claimed by the major air carriers and payments made by DOT to these carriers and others that applied for assistance. For the insurance reimbursement program, which was administered by the Federal Aviation Administration (FAA), we discussed the process FAA used to determine and reimburse air carriers for insurance premium increases resulting from the September 11, 2001, disaster. We also provided information on the total payments made under the program. Finally, we discussed FAA's expanded in-house aviation insurance program and the potential impact to the federal government. The briefing slides, which provide more detail on our analysis, are enclosed.

¹ Pub. L. No. 107-42, 115 Stat. 230 (2001).

² The briefing slides and a summary of our analysis were included in our October 5, 2001, correspondence to you. See GAO-02-133R *Financial Management: Assessment of the Airline Industry's Estimated Losses Arising From the Events of September 11*.

Results in Brief

DOT designed and implemented a structured claim review process to help ensure that the \$5 billion in disaster relief funds were used only to compensate carriers for their September 11 related losses. A team of DOT accountants, economists, and aviation analysts with support from the department's Offices of the General Counsel and the Inspector General administered the disaster relief program, reviewed carriers' loss claims, and determined carriers' allowable September 11 related losses. As specified in the Act, each carrier was compensated the lesser of allowable actual losses or the market share formula amount.³ The major air carriers claimed losses of \$5.6 billion related to the terrorist attacks. These carriers have been paid \$4.1 billion or 88 percent of the total \$4.6 billion distributed. As of August 26, 2003, DOT reported that most air carriers had received their final payments pursuant to this program, although a small number of claims remained open due to unresolved issues. All the major carriers except Federal Express have received their final payment. Federal Express has an administrative appeal and a lawsuit pending with regard to its payment.

Overall, the major carriers recovered approximately 73 percent of their claimed losses, although 8 of the 14 major carriers had all their September 11 losses compensated. The remaining 6 carriers' losses were only partially compensated because their allowable September 11 losses exceeded the amount determined by applying the market share formulae prescribed in the Act. Industry wide, 355 of the total 448 applicants receiving assistance were paid based on the formula. Because 93 carriers had actual losses less than their formula amount, DOT will not distribute the entire \$5 billion provided in the Act. DOT advised the Congress of this fact and in February 2003 the Congress rescinded \$90 million.⁴ DOT officials plan to return any remaining unused funds to the Treasury upon the completion of the program.

With regard to the insurance reimbursement program, the FAA implemented a systematic review process to determine the increases carriers experienced in their war risk insurance premiums following the terrorist attacks and to reimburse the carriers accordingly.⁵ FAA utilized insurance providers' invoices to substantiate the premiums being charged immediately before September 11 and to evidence premium increases following September 11.⁶ For each of the major air carriers, we verified FAA's reimbursement determinations by independently recalculating these amounts. In total, 183 carriers were reimbursed \$68 million for their increased insurance costs. The major carriers received \$58 million, or 85 percent, of this total.

Soon after the terrorist attacks, insurance providers generally cancelled carriers' war risk insurance coverage but then offered to reinstate the policies at a substantially

³ The formula amount is calculated by dividing the carrier's available seat miles (ASMs) or revenue ton miles (RTMs) by the universe of ASMs/RTMs (a reflection of market share) multiplied by available compensation.

⁴ Public Law 108-7, sec 333, 117 Stat. 414 (2003)

⁵ War risk insurance provides coverage to carriers for losses resulting from war, terrorism, or other hostile acts. These policies typically provide coverage for the aircraft and liability.

⁶ The Act specified insurance increases were to be measured against the rates in effect during the period September 4-10, 2001.

higher cost and with reduced coverage limits. For the major carriers combined, the total annual cost for war risk coverage jumped from approximately \$12 million prior to the attacks to more than \$700 million immediately afterwards. This led to the Secretary of Transportation's determination that war risk insurance was not available commercially on reasonable terms and conditions and thus FAA was authorized to begin temporarily selling war risk coverage to air carriers operating domestic flights. Under current legislation, FAA may continue to provide war risk coverage through August 2004 with a possible extension through December 2004. In its 2003 Accountability Report, FAA reported that it had extended \$113 billion in coverage to 71 carriers, thereby increasing the federal government's risk exposure. Meanwhile, air carriers have begun to explore other options including a risk retention group to provide more affordable coverage in anticipation of FAA's offering of war risk insurance terminating in 2004.

Scope and Methodology

Our review primarily focused on the major air carriers. DOT defines a major carrier as an air carrier whose annual operating revenue exceeds \$1 billion. To achieve our objectives we performed various procedures, which are described in detail in Appendix I of the enclosed slides. We did not audit the major air carriers or the underlying records supporting the claims for disaster relief payments. Also, we did not assess the reasonableness of the pre- or post- September 11 premiums charged to carriers for war risk insurance coverage. We conducted our review from September 2001 through August 2003 in accordance with generally accepted government auditing standards.

Agency Comments

We requested comments on a draft of these briefing slides from the Secretary of Transportation or his designee. On August 26, 2003, DOT provided us with oral comments expressing the department's general agreement with the facts presented. DOT provided some technical comments, which we incorporated as appropriate.

As agreed with your offices, unless you publicly announce the contents of this report earlier, we plan no further distribution until 30 days from its date. At that time, we will send copies to the Secretary of Transportation, the Administrator, Federal Aviation Administration, and interested congressional committees. We will also provide copies to others on request. The report will also be available at no charge on the GAO Web site at <http://www.gao.gov>.

If you have any questions about this report, please contact me at (202) 512-9508, or Phillip McIntyre, Assistant Director, at (202) 512-4373. You may also reach us by e-mail at calboml@gao.gov or mcintyre@gao.gov. Other key contributors to this assignment were Jeffrey Jacobson, Ruth Walk, and Doris Yanger.

A handwritten signature in black ink that reads "Linda Calbom". The signature is written in a cursive style with a large initial "L".

Linda Calbom
Director, Financial Management
and Assurance

Enclosure

List of Requesters

The Honorable Robert C. Byrd
Ranking Minority Member
Committee on Appropriations
United States Senate

The Honorable Ernest F. Hollings
Ranking Minority Member
Committee on Commerce, Science and Transportation
United States Senate

The Honorable John D. Rockefeller IV
Ranking Minority Member
Subcommittee on Aviation
Committee on Commerce, Science and Transportation
United States Senate

The Honorable Ron Wyden
United States Senate

The Honorable Lloyd Doggett
House of Representatives



Air Transportation Safety and System Stabilization Act: Aviation Assistance Programs

Information on Payments Made Under
the Disaster Relief and Insurance Reimbursement Programs

Briefing for Congressional Requesters
September 3, 2003



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- Disaster Relief – Payments
- Insurance Reimbursement – FAA’s Claim Review Process
- Insurance Reimbursement – Premium Increases and Payments
- FAA’s Aviation Insurance Program
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- In the aftermath of the September 11 terrorist attacks, air passenger traffic sharply declined. This, coupled with the already slumping economy and reduced business travel, led aviation industry officials to predict significant financial losses for calendar year 2001.

- On September 22, 2001, the President signed into law the Air Transportation Safety and System Stabilization Act (act) which provided, among other things,
 1. \$5 billion in disaster relief funds, and
 2. authority to reimburse air carriers for increases in their insurance premiums.



- At your request in September 2001, we performed a preliminary, high-level assessment of the airlines' projected losses between September 11 and December 31, 2001, and reported that as an industry, there was a reasonable basis to assume that those losses related to the attack would likely exceed the \$5 billion made available under the act.¹
- We have been monitoring the Department of Transportation's (DOT) administration of the \$5 billion disaster relief program and the disbursement of the insurance reimbursements.
- Now that DOT has substantially completed its claim evaluation and payment processes under the disaster relief program and finished making payments under the insurance reimbursement program, we are providing information about DOT's process and payments made.

¹ See U.S. General Accounting Office, *Financial Management: Assessment of the Airline Industry's Estimated Losses Arising From the Events of September 11*, GAO-02-133R (Washington, DC: October 5, 2001). 4



- Specifically, for the disaster relief program, we are discussing:
 1. the process DOT used to help ensure that the payments it made were only for the direct and incremental losses stemming from the September 11 terrorist attacks, and
 2. the major airlines' reported September 11 related losses and the compensation payments they received for those losses.

- For the insurance reimbursement program, we are discussing:
 1. the process employed by the Federal Aviation Administration (FAA) to determine how much of any insurance premium increases occurred as a result of September 11 and that the reimbursement payments made properly reflected those increases, and
 2. the amount of reimbursements made for increases in insurance premiums.

- We are also providing overall summary payment information for both the disaster relief and insurance reimbursement programs.



- In addition, we are providing information about the current state of aviation insurance and the potential impact to the federal government.
- We provided DOT our views on its administration of the payment processes as they occurred and are not making any recommendations as the programs are substantially completed.



Disaster Relief Program

- The disaster relief program was administered by a team of DOT accountants, economists, and aviation analysts with support from the offices of the General Counsel and the Inspector General. DOT designed and implemented a structured claim review process to help ensure that only September 11 losses were compensated.
- The process was documented in publicly available program rules that provided guidance to the air carriers applying for assistance.
- DOT determined an air carrier's allowable actual losses by analyzing its applications and supporting documentation and, where necessary, consulting with the air carrier. Certain losses, such as impairment losses, were generally disallowed.
- After applications were reviewed, carriers received the lesser of allowable actual losses related to the terrorist attacks or the market share formula amount² as specified in the act.
- On average, it took over 3 1/2 months longer to determine the compensation amounts for carriers that were paid on the basis of allowable actual losses.

² The formula amount is calculated by dividing the carrier's available seat miles (ASMs) or revenue ton miles (RTMs) by the universe of ASMs/RTMs (a reflection of market share) multiplied by available compensation. 7



Disaster Relief Program

- Final payments for most carriers were issued by December 31, 2002. As of August 26, 2003, a small number of cases remained open due to unresolved issues.
- The 14 major air carriers claimed \$5.6 billion in losses related to September 11. As of July 22, 2003, \$4.1 billion in disaster relief funds had been distributed to the major air carriers.
- \$363 million of the disaster relief funds were not distributed because 93 carriers had actual allowable losses that were less than the formula amount. Of these funds, \$90 million was rescinded by P.L. 108-7 and at the conclusion of the program DOT plans to return any unused funds to the Department of the Treasury.
- Determining actual losses added complexity and lengthened the payment process. Ultimately, many carriers were compensated less than their September 11 losses while some carriers recovered all of their September 11 losses.



Insurance Reimbursement Program

- The FAA implemented a systematic review process including the review of invoices from the air carriers' insurance providers to (1) determine rates in effect during September 4-10, 2001, and (2) evidence actual increases.
- FAA reimbursed carriers for 30 days of increased premiums using funds from the Aviation Insurance Revolving Fund.
- Estimated annual war risk insurance premiums³ for the 14 major air carriers increased from approximately \$12 million to approximately \$719 million. Due to this increase, carriers are considering forming a risk retention group to obtain more affordable coverage.
- FAA reimbursed 183 carriers \$68 million.
- In response to the lack of availability of third-party liability insurance, FAA expanded its in-house aviation insurance program from a standby basis to as much as \$113 billion in coverage which increased the government's risk exposure.
- The current balance in the Aviation Revolving Fund from which claims are paid may not be sufficient to pay a carrier's claim in a timely manner.

³ This estimate is calculated based on invoices air carriers received from commercial insurance carriers immediately after September 11.



- The act was intended to compensate air carriers for losses incurred as a result of the terrorist attacks. Title I created the Disaster Relief program and Title II authorized the Insurance Reimbursement program.
- Title I provided for the payment of \$5 billion to air carriers for direct losses incurred as a result of the ground stop order issued on September 11th and incremental losses incurred by air carriers through December 31, 2001.
 - Title I allocated
 - \$4.5 billion to passenger-only or combined passenger and cargo carriers (passenger carriers) and
 - \$.5 billion to cargo-only carriers (cargo carriers).



- Further, Title I directed that the maximum amount of compensation paid to each carrier may not exceed the lesser of
 - its allocated share of the passenger carrier or cargo carrier distributable amounts, \$4.5 billion and \$.5 billion, respectively (referred to in this briefing as the “formula amount”), or
 - the actual direct and incremental losses incurred by the carrier as a result of the September 11 terrorist attacks (referred to in this briefing as “allowable actual losses”⁴) as demonstrated to the satisfaction of the President.
- The Aviation and Transportation Security Act (Public Law 107-71) signed November 19, 2001, amended the act by providing that a portion of the \$4.5 billion passenger carrier disaster relief funds could be set aside for smaller air carriers such as air ambulances and tour operators.

⁴ Allowable actual losses were generally determined based on the difference between pre-September 11 forecasts and actual financial results for the compensable period.



- Title II of the act gave the Secretary of Transportation the authority⁵ to reimburse air carriers for the increase in the cost of insurance, with respect to a premium for coverage ending before October 1, 2002.
- Cost increases were to be measured against the rates in effect September 4–10, 2001.
- Following the attacks, war risk insurance⁶ was cancelled by air carrier insurers and reinstated with reduced coverage at higher prices.

⁵ The Secretary delegated this authority to the FAA Administrator.

⁶ War risk insurance provides coverage for flights to cover losses resulting from war, terrorism, or other hostile acts. Both hull and liability insurance coverage are provided.



- The higher premium included surcharges⁷ that were imposed for both:
 - hull war risk which covers loss of or damage to the aircraft, and
 - liability war risk which covers death or injury to passengers and third parties.
- Prior to September 11, a separate premium was charged only for hull war risk and there were no surcharges.
- The post-September 11 surcharges for hull and third-party liability war risk were:
 1. Hull war risk surcharge -- \$.05 per \$100 of the average fleet value.
 2. Liability war risk surcharge -- \$1.25 per passenger per enplanement.

⁷ Currently, insurance providers have incorporated the surcharges into the overall hull and comprehensive war risk premiums and are no longer charging amounts separately.



- We focused our work on the major air carriers.
- Major air carriers are air carriers whose annual operating revenue exceeds \$1 billion.
- The 14 major air carriers as of September 11, 2001, were:
 - Alaska Airlines⁸
 - American Airlines
 - American Trans Air
 - Delta Air Lines
 - Northwest Airlines⁸
 - Trans World Airlines¹⁰
 - United Parcel Service⁹
 - America West Airlines
 - American Eagle Airlines
 - Continental Airlines
 - Federal Express⁹
 - Southwest Airlines
 - United Airlines
 - US Airways
- See appendix I for additional discussion of our scope as well as the methodology used for this review.

⁸ Alaska Airlines and Northwest Airlines submitted separate applications for disaster relief compensation for their cargo operations. The annual operating revenue for these cargo operations did not exceed \$1 billion and therefore we only reviewed the claims related to their passenger operations in our work.

⁹ Federal Express and United Parcel Service are cargo carriers.

¹⁰ As of the quarter ended March 31, 2002, DOT no longer classifies TWA as a major air carrier.



- The disaster relief program was administered by a team of DOT accountants, economists, and aviation analysts within the Office of the Secretary with support from the Office of the General Counsel and Office of the Inspector General.
- This review team designed and implemented a structured claim review process to help ensure that only September 11 losses were compensated.
- A team of reviewers analyzed each of the major air carriers' final applications.
- The process was documented in publicly available program rules that provided instructions, forms, deadlines, and guidance to air carriers applying for assistance.



- DOT structured the program into three payment rounds.
 - Because the amount of losses submitted by the air carriers in round 1 were based upon early estimates, air carriers received 50 percent of estimated compensation amounts in this round.
 - In round 2 (where losses were based upon estimated and actual financial data), air carriers received additional compensation to equal a cumulative total of 85 percent.
 - In round 3, where losses were based upon actual financial data for the period September 11 through December 31, 2001, and were approved by DOT, most carriers received additional compensation to equal a cumulative total of 100 percent of allowable compensation.
 - As discussed later, final payments have not yet been made to several carriers, primarily those smaller carriers qualifying for the set-aside program.
- DOT required agreed-upon procedures to be performed by independent public accountants on the information submitted in the round 3 applications, which sought to verify that the amounts submitted by the air carriers either agreed with or were reconciled to the carriers' financial systems and other supporting documentation.¹¹

¹¹ Small air carriers were required to submit simplified agreed-upon procedures.



Figure 1: Losses Claimed by the Major Air Carriers under the Disaster Relief Program

	Losses claimed by the major air carriers
Passenger carriers	\$5,343,782,846
Cargo carriers	\$244,799,999
Total	\$5,588,582,845

Source: Major air carriers' 3rd round applications.

Note: These amounts were the losses claimed on the major air carriers' 3rd round applications. These losses generally exclude items such as impairment losses¹² but may not be adjusted in some cases for other losses DOT would have disallowed.

- In round 3, the DOT review team analyzed the applications and supporting documentation to determine the air carriers' allowable actual losses. DOT consulted with the carrier by phone and e-mail to clarify issues and make payment determination decisions.

¹² Impairment losses, which can also be referred to as devaluation, are the amounts by which the fair (market) value falls below the book value of an asset, such as a carrier's aircraft. 17



- Such decisions regarded the inclusion or exclusion of certain expense items based upon the item's relation to the terrorist attacks. For example, DOT excluded approximately \$2 billion in impairment losses because, in its judgment, air carriers could not show that impairment losses were fully attributable to the terrorist attacks nor fully realized in the compensation period.
- While the review team's payment decisions were not always fully documented in the air carrier payment files, the review team was able in all cases to explain to us the basis for their payment decisions affecting the major air carriers.
- As part of its efforts to maintain consistency in payment determination decisions, the review team in some cases held discussions with and/or requested additional information from air carriers which were taken into consideration in settling and closing claims.



- Although a laborious task as described above, once the review team determined the air carrier's allowable actual losses related to the September 11 terrorist attacks, DOT issued, in accordance with the act, compensation equal to the lesser of allowable actual losses or the carrier's formula amount.



- The length of time it took to issue final compensation payments to the air carriers varied.
- After the round 3 applications were received from the major air carriers, it took an average of
 - 16 days (with a maximum of 26 days) to determine the compensation for the air carriers paid on the basis of the formula, and
 - 128 days (with a maximum of 248 days) to determine the compensation for the air carriers paid on the basis of allowable actual losses.
- On average, it took over 3 1/2 months longer to determine the compensation amounts for carriers that were paid on the basis of allowable actual losses.
- Final compensation for most carriers (74 percent) was issued by December 31, 2002. However, as of August 26, 2003, a small number of cases were open due to remaining unresolved issues.



- A few carriers have sued DOT challenging the department's rule making. As of July 22, 2003, Federal Express (FedEx) was the only major air carrier suing DOT.
 - FedEx received approximately \$101 million¹³ in compensation in round 1, which approximated 50 percent of the losses FedEx originally estimated.
 - In round 3, DOT determined FedEx's actual losses to be only approximately \$69 million after reviewing its application. FedEx has administratively appealed this determination.
 - DOT has sought repayment of approximately \$32 million¹³ from FedEx.
 - FedEx is claiming approximately \$119 million¹³ in losses in round 3, and is seeking remedy in the U.S. Court of Appeals for the District of Columbia Circuit. A hearing has been set for October 2003.

¹³These amounts were made publicly available in FedEx's SEC filing for the fiscal year ended May 31, 2003.



- As specified in the Act, air carriers were compensated the lesser of their allowable actual losses or a market share formula.
- As of July 22, 2003, 79 percent of applicants receiving assistance were compensated using the market share formula and so received an amount that was less than their actual September 11 losses.

Figure 2: Number of Carriers Compensated on the Basis of the Formula Amount Versus Allowable Actual Losses

	Passenger carriers	Cargo carriers	Total
Formula amount	278	77	355
Allowable actual losses	62	31	93

Source: DOT's Disaster Relief Program Database, July 22, 2003.

Note: "Passenger carriers" includes carriers receiving assistance under the set-aside provision. An air carrier who applied for both passenger and cargo payments was considered to be two applicants in the chart above. Twenty-nine air carriers applied for both Passenger and Cargo payments. Federal Express is considered to have been compensated on the basis of allowable actual losses.

- As illustrated above, 355 carriers, including 278 passenger carriers, were not fully compensated for their September 11 losses while 93 carriers were fully compensated.
- Eight of the 14 major air carriers were compensated based on actual losses and therefore were compensated for all their September 11 losses.



- As of July 22, 2003, \$4.6 billion (93 percent of the \$5 billion) was distributed under the program.

Figure 3: Amounts and Timing of Payments Distributed under the Disaster Relief Program

	Total	Passenger carriers	Cargo carriers
Amounts distributed as of September 30, 2001	\$2,328,126,342	\$2,202,165,142	\$125,961,200
Amounts distributed as of December 31, 2001	\$3,846,963,999	\$3,659,296,165	\$187,667,834
Amounts distributed as of December 31, 2002	\$4,603,108,649	\$4,292,313,681	\$310,794,968
Amounts distributed as of July 22, 2003	\$4,636,891,322	\$4,325,720,094	\$311,171,228
Undistributed funds	\$363,108,678	\$174,279,906	\$188,828,772
Total available under the Disaster Relief program	\$5,000,000,000	\$4,500,000,000	\$500,000,000

Source: DOT's Disaster Relief Database, July 22, 2003.
Note: Distributed funds include refunds of overpayments.



- Overall, the 14 major air carriers were compensated 73 percent of their claimed losses under the Disaster Relief program.

Figure 4: Major Air Carriers' Claimed Losses Related to the Terrorist Attacks Compared to Funds Distributed under the Disaster Relief Program

	Total	Passenger carriers	Cargo carriers
Claimed losses	\$5,588,582,845	\$5,343,782,846	\$244,799,999
Funds distributed	\$4,065,346,384	\$3,883,442,976	\$181,903,408
Percent of claimed losses compensated	73%	73%	74%

Source: Major air carriers' 3rd round applications and DOT's Disaster Relief Program Database, July 22, 2003.

Note: "Claimed Losses" were the losses claimed on the major air carriers' 3rd round applications. These losses generally exclude items such as impairment losses but may not be adjusted in some cases for other losses DOT would have disallowed. "Funds Distributed" includes the \$101 million distributed to Federal Express.



- Of the \$363 million in undistributed funds:
 - A small amount will be distributed to approximately 50 smaller air carriers that have not yet been issued final payment.
 - DOT officials said that some funds have been set aside for a litigation reserve.
 - In February 2003, \$90 million was rescinded by Public Law 108-7 because DOT assured the Congress that it would not need the full amount of the remaining funds to complete the program.
 - DOT plans to return any remaining undistributed funds to the Department of the Treasury at the conclusion of the program.



- The act authorized the DOT Secretary to reimburse airlines for increases in insurance premiums following the terrorist attacks. The Secretary delegated this authority to the FAA Administrator.
- The act also specified that the reimbursements be made from the Aviation Insurance Revolving Fund.¹⁴ However, no additional funds were provided, thus limiting the amounts FAA could reimburse carriers. As a result, insurance reimbursements were limited to 30 days.
- FAA established a systematic process for verifying carriers' post-September 11 war risk premium increases, including obtaining and reviewing invoices from the carriers' insurance providers to (1) determine rates in effect during September 4-10, 2001, and to (2) evidence actual increases.

¹⁴ The Revolving Fund finances FAA's Aviation Insurance Program that was established by the Congress in 1951 to provide war risk coverage to carriers flying into hostile territories. In 1977, the Congress authorized the program to cover any risk, not just war risk. To date, FAA has issued only war risk insurance. 26



- Due to limited staff, FAA hired contractors to assist in reviewing applications and invoices.
- For all carriers that received \$100,000 or more under the Insurance Reimbursement program, including all the major air carriers, FAA instituted a process to reconcile what is commonly called the
 - deposit premium (the up-front premium paid by a carrier based upon the estimated value of its aircraft and the number of passengers expected to be flown) to the
 - earned premium (the end-of-period adjusted premium based on the actual value of the aircraft used during the period and number of passengers flown), and
 - adjusted the carriers' reimbursement payments accordingly.



Insurance Reimbursement
Premium Increases and FAA Payments

- Prior to September 11, total estimated annual insurance costs for war risk coverage for the 14 major air carriers were approximately \$12 million.
- Post-September 11 total estimated annual insurance costs for war risk coverage for the 14 major air carriers increased to approximately \$719 million.
- As of April 2003, FAA paid 183 carriers \$68 million to reimburse those carriers for 30 days of increased premiums in the war risk component of their overall insurance costs.
- The 14 major air carriers received 85 percent (\$58 million) of the total reimbursements made.



- After the post-September 11 increases in war risk insurance premiums, the Secretary of Transportation determined that third-party liability war risk insurance from commercial insurers was not available on reasonable terms and conditions.
- And in accordance with the Act, FAA's in-house Aviation Insurance Program, which previously had covered only international flights into hostile territories, extended coverage to domestic flights in order to provide air carriers with an alternative to the commercial third-party war risk insurance.¹⁵
- The expansion of FAA's Aviation Insurance Program has increased the government's risk exposure from a standby basis to as much as \$113 billion for 71 carriers (for the 60-day period ending February 13, 2003) as reported by FAA.

¹⁵ Subsequent legislation required FAA's Aviation Insurance Program to provide hull insurance as well as third-party liability.²⁹



- The Aviation Revolving Fund from which aviation insurance claims are paid may not have sufficient funds to pay a carrier claim in a timely manner.¹⁶
- According to FAA, the liability for a carrier claim ranges from \$500 million to \$4 billion while the current balance in the Revolving Fund is approximately \$194 million.¹⁷
- In regards to FAA's Aviation Insurance Program, the 2003 Emergency Wartime Supplemental Appropriations Act extended war risk insurance coverage to August 31, 2004. The act also authorized the Secretary of Transportation to extend the program to December 31, 2004.
- Because FAA's offering of war risk insurance is intended to be temporary, with authority now expiring, unless further extended, in August 2004, carriers are considering forming a risk retention group to obtain more affordable coverage.
- According to an Air Transport Association official, as of July 22, 2003, no risk retention group has been created.

¹⁶ See also U.S. General Accounting Office, *Aviation Insurance: Issues Related to the Reauthorization of FAA's Aviation Insurance Program*, GAO/T-RCED-97-115 (Washington, DC: May 1, 1997).

¹⁷ Since the inception of the Aviation Insurance Program, only four claims ranging between \$626 and \$122,469 have been paid.



- Our work focused on the major air carriers because the 14 major air carriers represent about 89 percent and 41 percent of the passenger and cargo carrier industries (respectively) in terms of available seat miles and revenue ton miles.

In order to review the disaster relief program, we:

- Reviewed the act and relevant DOT policies and guidance.
- Advised on the content of agreed-upon procedures which were completed by the air carriers' auditors.
- Reviewed DOT's payment determination process, including the calculation of the ASM/RTM universe and the air carrier's formula amount.



In order to review the disaster relief program, we:
(continued)

- Reviewed all three rounds of the major air carriers' applications including the agreed-upon procedures and compared financial information to SEC filings such as annual and quarterly reports, and aviation publications where possible.
- Reviewed adjustments to the major air carriers' loss claims made by both the air carriers and DOT.
- Performed various analytical procedures on information submitted by the major air carriers.
- We did not, however, audit the underlying data submitted as part of the air carriers' applications nor the information contained in the DOT Disaster Relief database.



In order to review the Insurance Reimbursement process, we:

- Obtained and reviewed FAA's requirements for applying for war risk insurance premium reimbursements.
- Obtained an understanding of the effects of the events of September 11 on war risk insurance premium increases through meetings and phone interviews with FAA officials.
- Reviewed the reimbursement packages submitted by the major carriers to FAA.
- Independently recalculated and verified the reimbursement amount for the major air carriers using invoices and other correspondence from insurance providers.



In order to review the Insurance Reimbursement process, we:
(continued)

- Compared actual enplanement and other data used to compute final insurance reimbursement amounts to data reported by the major carriers to DOT's Bureau of Transportation Statistics to check for consistency.
- We did not, however, assess the reasonableness of the premium increases being charged by the insurance providers.
- On August 26, 2003, DOT provided oral comments on a draft of these briefing slides. DOT generally agreed with the facts presented. We incorporated DOT's technical comments as appropriate.
- Our work on the Disaster Relief and Insurance Reimbursement Programs was performed from September 2001 through August 2003 in accordance with generally accepted government auditing standards.

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