

# INSIDE THE IMPACT OF LIABILITY TRENDS AND SOCIAL INFLATION ON INSURANCE

During the last couple of years, the insurance industry has seen a significant shift from what we refer to as a “soft” to a “hard” market. A hard market is characterized by a rise in premiums, tighter policy terms and conditions and, in some cases, reduced availability of coverage. Catastrophic property and liability losses impacting the underwriting profitability of carriers are in part responsible for the shift in the market. In addition, social inflation has also played a significant role in the hardening market, impacting the insurance programs of high-net worth individuals, family offices and businesses.

## How Social Inflation Has Changed the Litigation Landscape

Social inflation is a term used by insurers to describe the rising costs of insurance claims as a result of various factors, including jury sentiment, the increased use of litigation financing firms, an aggressive plaintiff’s bar, tort reform rollbacks, and larger compensatory jury awards.

Anti-corporate, anti-wealth sentiment among jury pools dates back to the financial crisis of 2008 fueled by economic inequality and the feeling that someone needs to pay for a loss when damage or injury is sustained, regardless of negligence. Entitlement attitudes are specifically strong among jury pools comprised of 18-to-29-year-old members, according to a survey conducted by the American Jury Centers of mock jury participants. Participants ages 60 and above tend to have lower entitlement attitudes according to the survey.

## The Rise of Litigation Financing

Third-party litigation funding has also impacted jury pools and the mega verdicts and settlements rendered in liability cases. Litigation financing firms fund plaintiffs and law practices in cases where there

is likely going to be a big payday. The capital that helps fund the lawsuits is returned — and then some — in return for the risk taken. If the lawsuit is unsuccessful, the plaintiff is under no obligation to repay the funds provided. In the end, litigation funding serves to



“2012-2019, broadcast television ad spending for legal services increased by 44% in both Baltimore and Los Angeles”

- Insurance Research Council

neutralize the incentive for the plaintiff to settle a lawsuit in a timely manner, driving up legal fees for defendants and their insurers.

## Big Ad Budgets for Legal Services

An aggressive plaintiff’s bar with big advertising budgets is another influential factor in litigation cases. In a recent article, the Insurance Research Council (IRC) cites that from 2012-2019, broadcast television ad spending for legal services increased by 44% in both Baltimore and Los Angeles and by 42% in Miami, for example. There is also evidence that digital ad spending for legal services has increased significantly in an effort to attract potential clients in class-action suits.

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## Rollbacks of Tort Reforms

Tort reform refers to change in the civil justice system that aims to reduce the ability of victims to bring litigation or reduce damages a victim can receive. Rollbacks of previously enacted tort reforms, intended to control costs and legislative actions to retroactively extend or repeal statutes of limitations, have also been instrumental in the growth of liability risk and costs. The supreme courts of at least eight states with caps on non-economic damages have overturned reforms, according to the IRC.

## What Coverage Lines Have Been Impacted

Certain insurance lines have been most affected by litigation trends and social inflation, including Commercial Auto Liability, Commercial Umbrella/Excess Liability, Product Liability, and Management Liability, such as Directors & Officers (D&O) Liability. Commercial Auto is particularly impacted by litigation trends because of the frequency of low-impact accidents where businesses are involved, combined with the availability of higher policy limits in that line, which make it an easy and attractive target for lawsuits and nuclear verdicts.

Evidence also shows that Personal Auto Liability is being affected by the same social inflation and litigation trends impacting Commercial Auto Liability insurance. For example, bodily injury losses in Personal Auto insurance claims have experienced a steady increase in attorney participation – from 47% of all claims nationwide in 2002 to 52% in 2017. In addition, the average payment for bodily injury claims from 2014-2019 grew at an annualized rate of 5.5% – three times the rate of inflation.

D&O Liability insurance has experienced some of the highest premium rate increases over the last couple of years because of emerging risks and social inflation. According to a report by Milliman, there was a “staggering” increase in the size of D&O

settlements, from \$1.4 billion in 2017 to \$2.4 billion in 2018. Another report about D&O trends by insurer Allianz highlighted the growth of a “global investment class” related to litigation financing, in particular the funding of group securities class action suits. Sexual misconduct lawsuits on the heels of the #metoo movement, discrimination cases, and the failure to disclose or address climate change risks have also contributed to the uptick in D&O lawsuits.

## Mitigating Risk

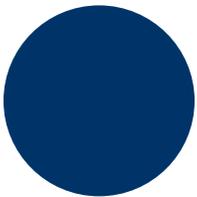
A strong investment in risk management education and safety measures by family offices, high-net worth individuals and businesses is necessary to bolster legal defenses against litigation. This involves taking a deliberate approach to risk management that includes staying up to date about relevant threats (workplace disputes, cyber security, and D&O liability, for example), developing a strategic plan to address them, and establishing a trusted network of partners who can help meet their unique needs.

In the event of a liability claim, good claims handling is critical to ensure that you – the insured – and the insurance company remain in alignment. Early claims investigation is also critical, so there are no surprises, such as non-compliance on your part that can impact the case. In addition, defense attorneys recommend that in high-dollar-exposure, but highly defensible cases, insureds and insurers carefully prepare their own estimate of reasonable settlements, rather than only respond to estimate requests from plaintiff’s counsel.

If your case goes to trial, be sure you and your attorney show that you care and accept responsibility, including demonstrating actions that you have undertaken to rectify the situation that caused the loss. This will help diffuse the anger juries feel and the resulting mega verdicts they render.

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As an insurance brokerage, AHT receives reports about certain higher-risk litigation cases and, when necessary, we've been involved with the insurance company and our clients in discussing strategy. We add value and a different perspective from the others involved, including wanting to protect the reputation of our client and ensuring the ability to place responsive coverage in the future.



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