Social Inflation is Back!

Thursday, February 13, 2020
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Questions

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Meet Your Presenters

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• **Introduction**
• Definition
• Legal Trends
• Judiciary
• Third Party Litigation Finance
• National Mood: People/Juries are Discontent and Angry!
• Will Social Inflation Spread to Personal Lines?
• Concluding Remarks
A Topic Since Early 2017…

We began our series entitled Social Inflation is Back! in early 2017. Since then, it has become our most requested topic as to speaking engagements, forwards to industry contacts, or requests for use in internal presentations.

Our efforts these past few years have been directed toward trying to define and quantify elements of social inflation. But *quantify* is probably the *wrong word*—trying to find *objective signals of social inflation in the economy* better describes our efforts.
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Virtually every conference call during the 3Q19 (and QTD4Q19) included extensive discussion of ‘social inflation’ or ‘the worsening tort environment’, etc.

The quote below is from Bill Berkley (WRB); but he is not the only executive asking if people are ‘just angry’

...we're really seeing a group of people who are fermenting resentment of those who have. We're seeing court decisions that make no economic sense that the court is just trying to punish people. The trends are not going to change. We have a while before you are going to see it change, a while meaning you probably have on the short end, it would be 18 months; on the longer end, 3 years. People are unhappy and angry, and that resentment is coming through in court decisions...
Social inflation burst onto the scene.

...when it comes to plaintiff activity... I would say we have seen a more aggressive plaintiff activity. Now that was certainly a big driver of the Commercial Auto charge that we took last quarter...

Alan Schnitzer, CEO of TRV on 1Q19 CC

What exactly is social inflation?
Social inflation is one of the most frequently mentioned terms on quarterly conference calls:

➢ It captures an increased propensity to sue; rising jury awards and expanding judicial theories beyond the ‘four corners’ of a contract.

➢ Social inflation is pernicious because it’s difficult to spot or measure objectively. It’s also a “social” phenomenon…are juries just *angry*?

Ways to quantify social inflation is to track:

1. Court statistics
2. Judicial appointments
3. Legal advertising
4. Third party litigation funding
5. Measures of inequality

*We place inflation in 3 buckets:*

1. Measures ‘stuff’ – CPI
2. Measures medical inflation
3. Measures everything else – social inflation
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Legal Trends at State Courts

Tort Caseloads

Increase due mainly to NJ

2012: 243  
2013: 242  
2014: 251  
2015: 243  
2016: 247  
2017: 255  
2018: 259

Statewide Tort Caseloads (000)

Civil Caseloads

2012: 6,808  
2013: 6,561  
2014: 6,426  
2015: 6,083  
2016: 5,958  
2017: 6,317  
2018: 6,565

Statewide Incoming Civil Cases (000)

Tort cases from 17 states representing about 33% of Liability Premiums.

Civil cases from 7 states representing about 50% of Liability Premiums.

Source: National Center for State Courts, Assured Research
Medical Professional – Jury Verdicts Rising

The largest MPL jury verdicts have been rising (and at all size ranges such as $10, $25, and $50 mil.)

Verdicts are small fraction of total claims but have outsized influence on claim settlements

Source: Captive International with data and analysis by TransRe, Assured Research. Arrow added by A/R for emphasis
Interesting correlation between federal tort actions and the liability combined ratio; up to 64% correlation through mid 1990s.

Source: Office of the U.S. Attorney, Assured Research
Good and Bad News…

– As part of our continued study of social inflation, we looked at trends in multidistrict litigation.

– While overall cases are down 35% since 2012 (good news), products liability cases, the largest classification, are only down 10% (bad news).

– And, the number of large cases is up significantly (more bad news).
### Multidistrict Litigation Cases Pending: 2012-Current

<table>
<thead>
<tr>
<th></th>
<th>Cases</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Products</td>
<td>All</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>Liability</td>
</tr>
<tr>
<td>2012</td>
<td>291</td>
<td>72</td>
</tr>
<tr>
<td>2013</td>
<td>287</td>
<td>67</td>
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<td>2014</td>
<td>290</td>
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<td>2016</td>
<td>250</td>
<td>71</td>
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<td>2017</td>
<td>221</td>
<td>70</td>
</tr>
<tr>
<td>2018</td>
<td>207</td>
<td>68</td>
</tr>
<tr>
<td>2019</td>
<td>196</td>
<td>65</td>
</tr>
<tr>
<td>Current</td>
<td>190</td>
<td>65</td>
</tr>
<tr>
<td>Change</td>
<td>-35%</td>
<td>-10%</td>
</tr>
<tr>
<td></td>
<td>Products</td>
<td>All</td>
</tr>
<tr>
<td>2012</td>
<td>25%</td>
<td>75%</td>
</tr>
<tr>
<td>2013</td>
<td>23%</td>
<td>77%</td>
</tr>
<tr>
<td>2014</td>
<td>24%</td>
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<tr>
<td>2015</td>
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<td>2016</td>
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<tr>
<td>2017</td>
<td>32%</td>
<td>68%</td>
</tr>
<tr>
<td>2018</td>
<td>33%</td>
<td>67%</td>
</tr>
<tr>
<td>2019</td>
<td>33%</td>
<td>67%</td>
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<td>Current</td>
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<td>66%</td>
</tr>
<tr>
<td>Change</td>
<td>-35%</td>
<td>-10%</td>
</tr>
</tbody>
</table>

Total cases down 35% since 2012, but products liability cases only down 10%.

Source: Joint Panel on Multidistrict Litigation, Assured Research
Trends in Multidistrict Litigation

Good and Bad News...

- The good news: the number of MDL cases is down 33%
- The bad news: products liability cases only down 10%
- The real bad news: the number and size of large cases (over 1,000 claimants) is up big time

Source: Joint Panel on Multidistrict Litigation, Assured Research

<table>
<thead>
<tr>
<th></th>
<th>2012</th>
<th>Current</th>
</tr>
</thead>
<tbody>
<tr>
<td>Large cases</td>
<td>14</td>
<td>21</td>
</tr>
<tr>
<td>Claimants</td>
<td>47,815</td>
<td>119,278</td>
</tr>
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</table>
Are starting to parallel the 1980s.

<table>
<thead>
<tr>
<th>Present</th>
<th>1980s</th>
<th>Link</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opioids</td>
<td>Tobacco</td>
<td>Products that cause societal health issues force states and municipalities to sue responsible parties for reimbursement.</td>
</tr>
<tr>
<td>Talcum powder</td>
<td>Silicone breast implants</td>
<td>Personal care products lead to injuries and diseases and eventually class actions.</td>
</tr>
<tr>
<td>Pelvic mesh</td>
<td>Intrauterine devices</td>
<td>Industrial accidents lead to environmental disasters and numerous claims.</td>
</tr>
<tr>
<td>California wildfires</td>
<td>Bhopal gas disaster</td>
<td>Chemical exposures lead to various types of cancer.</td>
</tr>
<tr>
<td>PFAS chemicals</td>
<td>Asbestos</td>
<td>No parallel</td>
</tr>
<tr>
<td>Sex abuse</td>
<td>xxxxx</td>
<td></td>
</tr>
</tbody>
</table>

The insurance impact of these cases may not be material, but their influence over jurors and the cascading affect on ‘regular tort’ awards is real.
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3 Key Points:
1. State courts matter more than federal courts (to P/C insurers)
2. Watching federal appointments can be misleading
3. Change is slow – lifetime appointments (federal) 6-10 years states

Politics are a factor in most state judicial election processes

Most federal judges appointed through 2019 were a R-for-R swap

Sources: uscourts.gov, S&P Global (population), Assured Research
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Third party litigation finance is changing the economics of the legal profession.

- Investors are now funding law firms to pursue litigation claims
  - This is a growing business in the US
  - Managers claim 30% returns are reasonable expectation

- Insurers will see better funded claimants and possibly more legal activity—Negative.

- But, also see claimants that are more willing to settle to end litigation—Positive.
Deconstructing Litigation Finance

3 Elements:

1. Commercial Litigation Finance
   - Esoteric B2B litigation; some involvement in mass torts

2. Consumer Litigation Finance
   - Involved in ‘regular torts’ like auto, premises liability, professional liability, etc.
   - But amounts advanced are small (~$4,000) and used for daily living

3. RAND paper proposes a 3rd element of Litigation Finance
   - Specialty finance firms providing capital to personal injury firms
   - Video Clip – Advocate Capital Inc.
Specialty finance firms are “Game Changers.”

“We are a game changer for contingency fee law firms. We help them give them the confidence to be able to go into negotiations and reject low settlement offers.”

Tina Burns, VP of Advocate Capital, Inc. speaking on a promotional video found at their website.

Advocate Capital (and peers) are specialty finance firms that provide ‘working capital’ to contingency fee law firms.
National and local TV advertising for legal services set to surpass $1 billion in 2019

CAGR # ads from 2013 to 2019e is 9%; from 2016 to 2019e is 11%!

Data: X Ante analysis utilizing data provided by Kantar Media CMAG, Assured Research
Is the ROI on legal advertising good? In NYC – yes!

$ Legal advertising per PI claim in NYC is flattish, but average settlement value rising at 8%pa. Not a bad ROI!

Sources: Legal advertising data from X Ante analysis using Kantar CMAG Data; PI claims from NYC Municipal Liability Report, Assured Research
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Income for the top 10% has been outdistancing the other 90% since the mid-1980s

Income levels: Top 10% vs remaining 90%

Note inflection point in mid-1980s

Wealth has been steadily transferred from individuals to corporations

Wages and corporate profits as a % of national income

Sources: Federal Reserve Bank of St. Louis (FRED), Assured Research

Note the differing trend lines, with inflection points in mid-1980s
Wealth inequality has been expanding.

Sources: Federal Reserve, Assured Research
Prior societal distinctions were drawn along income lines

Upper Income
Middle Income
Lower Income

Yellow arrows indicate there was considerable opportunity for upward mobility

Source: Various data points and observations, Assured Research
Societal Distinctions

Now distinctions are by education and professional status.

Source: Various data points and observations, Assured Research

Elite, managerial, technical, professional

Mobility Barriers

Remainder of Society

Now mobility is more limited
Gallup satisfaction index is depressed given state of the economy and unemployment levels

Percentage of people satisfied with the way things are going in the United States

Sources: Data available at: https://news.gallup.com/poll/1669/general-mood-country.aspx, Assured Research

If the economy was working for most people, the satisfaction index would be higher, based on prior surveys.
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**Will Social Inflation Spread to Personal Lines?**
Concluding Remarks
Will social inflation spread to personal lines?

Main points:

– Social inflation has heretofore been a concern mainly for commercial lines
  
  • Commercial auto, general and professional liability, etc.

– We surveyed professionals in the industry and found…
  
  • A majority believe there is a credible risk social inflation will spread
    
    – Mainly through personal umbrella policies and bad faith claims

– Our review of national rate filings for personal umbrella reveals there is ‘something going on’
Will social inflation spread to personal lines?

To date social inflation has been largely concentrated in commercial lines. Do you see the credible risk that social inflation will spread to personal lines?

![Bar chart showing responses to the question:]
- Yes: 61%
- No: 17%
- Maybe: 22%

What are the main barriers to social inflation spreading to personal lines?

- Low policy limits: 79%
- Established case law (novel theories/cases difficult to bring): 19%
- Plenty of room to run in commercial lines: 30%
- Other: 25%
Will social inflation spread to personal lines?

Which lines of insurance (where social inflation has, arguably, not yet reached) are at greatest risk?

- Personal Auto: 36%
- Homeowners: 16%
- Personal Umbrella: 69%
- Workers' Comp: 25%
- Commercial Property: 9%
- Professional Lines (other than MPL): 55%

Could bad faith claims be an avenue for social inflation to spread (e.g., to personal auto or WC)?

- Yes: 45%
- Probably: 24%
- Plausible...not sure/ if I buy it: 28%
- No: 3%
Personal umbrella filings nationally – rates up!

Rate filing activity is up 50% since 2014 and the # of policyholders affected has tripled. Rates are up for reason...umbrella writers experiencing rising ‘frequency of severity’

Source: S&P Global, Assured Research
In the recent years we have seen a change in the severity of bodily injury claims with drivers including an increase in traumatic brain injuries and multi-level spinal surgeries as a result of personal automobile accidents. It seems that the state of [ ] has had an environmental change which has led to more serious claims and subsequent awards of large sums for such injuries. These areas are impacted by a recovering economy producing more miles driven and an increase in pedestrian/cyclist losses with distraction playing a major factor on frequency. Unfortunately, these types of losses lead to more fatalities, traumatic brain injuries, complex fractures, and multi-level spine surgeries. There is also a component of people being more willing to undergo surgery with the technological advancements making procedures less invasive. Unless there is a significant change in these drivers or legal environment, we expect higher volume and severity of claims to continue.

Taken from a 2019 personal umbrella rate filing in response to DOI actuary question as to the reason for high severity trends.
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Although politics is well beyond our sphere of expertise, it’s probably worth considering that the political cycle during 2020 is likely to extend (and maybe exacerbate) the social divisiveness in the U.S. that seems both simultaneously symptom and contributing cause to social inflation.

It’s hard to disagree with Mr. Berkley that social inflation will last for 18 months on the short-end to 3 years on the longer side. The good news we can offer – the clock didn’t start with that observation during 3Q19 conference calls; we see the 2016/2017 timeframe as when tort inflation began to resurface.
Thank You!

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Thank you for your time.