

# The Advisor

## **Trends to watch: Social inflation driving up claims costs**

In 2022, juries returned 70 “nuclear verdicts” against corporations. Among those nuclear verdicts – each of which topped \$10 million – twenty were for more than \$100 million, and four were above \$1 billion, according to a report from Marathon Strategies, an independent communications and research firm.

Skyrocketing jury awards are one example of how social inflation is driving up insurance costs, as more people turn to litigation to resolve claims.

### **Social inflation: Causes**

The term social inflation is broadly used to describe the factors causing insurance claims costs to rise above what would be expected based on economic inflation. During the last five years, liability claims costs in the United States have jumped an average of 16 percent, while the average economic inflation rate has increased about 4 percent, according to a report from Swiss Re Institute.

Beyond economic inflation, there are several factors believed to be contributing to social inflation and driving up claims costs for insurers:

- **A push for litigation**

Trial lawyer advertising has exploded during the last several years, data from the American Tort Reform Association shows. From 2017 to 2021, \$6.8 billion was spent on trial lawyer advertising nationwide.

In addition, more plaintiffs and law firms are relying on third-party litigation firms to help fund court cases. These litigation firms, which are not affiliated with the lawsuits, provide funds to help cover expenses while litigation is ongoing, in exchange for a portion of the award if the lawsuit is successful. In 2020, \$17 billion was invested in litigation funding globally, according to Swiss Re Institute, with about half that funding supporting legal action against companies in the United States.

When these third-party litigation firms get involved, they can make cases run longer, subsequently raising defense costs: A study from the U.S. Government Accountability Office found that because some of these third-party funders charge high rates, plaintiffs are incentivized to reject fair settlement offers and push for additional funds to help cover the cost of repaying the third-party firm.



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- **Growing distrust of large corporations**

In addition, public opinion about large corporations is becoming more negative. A 2022 Gallup poll shows the percentage of adults who describe themselves as having “a great deal” of confidence in big business dropped from 23 percent in 2019 to just 14 percent in 2022.

Similarly, global law firm Orrick surveyed potential jurors in places where nuclear verdicts have been most common, asking questions not only about their opinions about large corporations and the lawyers who defend them but also the extent to which they trust science and the justice system. The results showed jurors today have an increasing lack of trust in all institutions – including large corporations – and believe they can use their role on a jury to punish and send a message to big businesses.

- **Nuclear verdicts**

Between 2020 and 2022, the number of nuclear verdicts against corporate defendants doubled, according to the Marathon Studies report. In 2022 alone, the combined total of all nuclear verdicts reached \$18.3 billion.

Some examples of recent nuclear verdicts include:

- In 2019, a jury in Ohio returned a **\$44 million verdict** against Oberlin College following a dispute about racial profiling at a local bakery. In 2016, a Black university student attempted to use a fake ID to purchase a bottle of wine and shoplift two additional bottles, and the son of the bakery’s owners, who is white, chased the Black student out onto the street. A physical altercation ensued, with two other Black university students joining in. Following the incident, Oberlin College students initiated a protest and a boycott of the business, alleging racial profiling. The bakery sued, accusing the college of defamation because members of the college’s administration had attended the protest.
- In 2021, a jury in Texas awarded **\$730 million** to the children of a 73-year-old woman who was killed in a collision with a tractor hauling an oversized load. The wrongful death lawsuit initially was filed against the trucking company and the companies that employed the front and rear escort vehicles; however, the trucking company settled ahead of trial for \$50 million, and one of the escort driver employers settled for \$1 million. Following a week-long trial, the jury delivered the \$730 million verdict against the employer of the front escort vehicle driver.
- In 2022, a jury in Minnesota awarded **more than \$35 million in damages** to a man who was burned by hot water that escaped from a hose while he was working at a brewery. He was spraying the floor with a 35-foot hose when a connector on the spraying end of the hose became loose and the hose caught on his belt. Jurors ruled against both the manufacturers – because they didn’t warn of the risk of clothing getting snagged by the hose – and against the brewery – because they didn’t provide the worker with protective gear.

### **Social inflation: Consequences**

Ultimately, social inflation pushes up insurance costs for policyholders, as insurance companies raise rates to account for the increased costs of resolving claims. The Insurance Information Institute says the coverage areas feeling the biggest squeeze as a result of social inflation include directors and officers liability, professional liability, product liability and commercial auto, though no area is immune.

In response, some insurers have reduced their capacity in these riskier sectors or have offered reduced coverage limits, which leaves businesses with increased liability risk.

While businesses – and risk management brokerage firms like Schauer Group – can't stop social inflation, there are steps that can be taken to mitigate its potential impact:

- Implement strong policies (such as fleet safety guidelines and employee handbooks) to manage risk and help protect from larger losses by having appropriate procedures in place
- Consider the potential financial impacts of social inflation when making decisions about insurance coverages and policy limits
- Practice corporate social responsibility, which can help combat anti-corporation sentiment locally

Schauer Group's team of experts is available to advise on best practices related to social inflation risks. If you'd like to discuss this topic further, please reach out to your Schauer Group representative.

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