



Unpacking "Social Inflation"

Ken Klein

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Meeting

Who am I?

- NAIC Consumer Rep.
- Former, long-time Business Defense Attorney.
- Law School Professor holding an endowed chair in preventive law.
- I went into academia in part so I could dig into questions like these without a client or boss giving me a pre-determined answer I had to try to defend.

There is a lot of talk recently about “Social Inflation” – a label for the general assertion that the way insurers are treated in courts is causing dramatic rises in premiums and loss ratios. Here is an example of one such statement from Triple-I’s CEO :

“It’s no secret that inflationary factors are **spreading at an alarming pace in the courts**, and their **impact is a growing concern** throughout the insurance industry. In my six years at the helm of Triple-I, I’ve seen **social inflation** become an **increasingly dangerous phenomenon**...with **devastating consequences** for consumers and insurers alike.”

-Sean Kevilighan, CEO I.I.I., socialinflationinsight@iii.org (June 22, 2022)

Historically, vigorous assertions of some form of a 'Litigation Crisis' have been a theory in search of evidence, with the assertion fading once research testing the assertion has been done

Legal Views of the Malpractice Crisis

In Search of the "Lawsuit Crisis"

by Michael J. Saks, Ph.D., M.S.L.

By now nearly everyone knows about the liability crisis. Municipalities, doctors, businesses, and others are paying soaring premiums for their liability insurance. The unlucky ones cannot find coverage at any price. The result is that services are becoming increasingly scarce and expensive. Curiously, the causes sound even more familiar. A new booklet being circulated by the Insurance Information Institute puts

In all the public discussion of the liability crisis, I have heard much about the system's false positive errors but nothing about its false negative errors.

them succinctly: "While our judicial system is basically a good one, it has been handicapped by unnecessary lawsuits, . . . exorbitant awards, and unpredictable results."¹

Thus, the liability crisis is seen as a lawsuit crisis. The press and industry lobbyists overflow with stories of frivolous lawsuits, out-of-control damage awards, and a nation turned litigious. Accordingly, state leg-

is not that the anecdote plaintiffs with unmeritor cases that should never have the "false positives" of this such horror story, equal found—the "false negative" people who suffered injuries and morally entitled to compensation, but who for or recover much or at all. If the liability crisis, I have ten's false positive error: negative errors.

Though the liability crisis say about them, the false certainly in large number lose a trial they should have money to pay medical expense. Or most likely of complaint. In a study of claims, only one in ten find true of victims of medical filed, fewer than one in 100.



HOW THE CASH-RICH INSURANCE INDUSTRY FAKES CRISES AND INVENTS SOCIAL INFLATION

By:

J. Robert Hunter, Director of Insurance, Consumer Federation of America

Joanne Doroshov, Executive Director, Center for Justice & Democracy

Douglas Heller, Insurance Expert, Consumer Federation of America

The Myth of the Liability Insurance Claims Explosion: An Empirical Rebuttal

David J. Nye* and Donald G. Gifford**

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I. INTRODUCTION

A perceived crisis in the nation's liability in 1986.¹ Some businesses saw their insurance period of two years, and others found the liability totally unavailable.² While trial lawyers and

Thomas M. Susman
Director
Governmental Affairs Office

November 12, 2013

Re: Lawsuit Abuse Reduction Act of 2013

Dear Representative:

I am writing on behalf of the American Bar Association to urge you to oppose H.R. 2655, the Lawsuit Abuse Reduction Act of 2013, which is scheduled for consideration by the House this week.

H.R. 2655 seeks to amend Rule 11 of the Federal Rules of Civil Procedure by reinstating a



But that doesn't mean this time around is the same. I am doing this presentation to unpack whether this most recent claim about a litigation crisis (this time called, "Social Inflation") has evidence supporting it.

Because I am trying to unpack an industry-assertion, I have focused my work entirely on reading (1) industry-affiliated assertions and (2) research by independent academics.

Unpacking the current claims about Social Inflation can be complicated because within the industry...

- **The term “Social Inflation” has no agreed upon, specific definition**

- Casualty Actuarial Society Research Paper: “there’s **no universally agreed-upon definition** of social inflation.” (C.A.S. goes on to detail 12 different recent definitions of “social inflation” in published papers 2010-21.)
- The Geneva Association: “Social inflation is a term that is widely cited in insurance debates, but it is often **ill-defined** or at best **only loosely explained**.”
- InsuranceThoughtLeadership.com: “as an industry, we are **struggling to define** it”

- **The only consensus about the current evidence of “Social Inflation” is that it is hard to find evidence**

- Triple-I CEO: “...a concept that’s **hard to measure**...”
- Gen Re article: “...**hard to find empirical evidence** that supports or disproves it.”
- InsuranceThoughtLeadership.com: “as an industry, we are **struggling to ...measure** it”

- **There is disagreement about which are the primary contributing factors to possible “Social Inflation”**

In other words, what I am unpacking, and testing, is:

The validity of the somewhat unfocused (but not necessarily wrong) intuition of insurers that external, societal factors are in some way causing premiums and loss ratios to improperly, unjustifiably, and quickly rise.

What I have done:

- Explored what evidence there is that Social Inflation, in general, is happening.
- Explored what evidence there is of any of the alleged social inflation factors.
- Explored the accuracy of assumptions underlying the social inflation debate (such as 'the involvement of plaintiffs lawyers in insurance claims is bad' or 'Millennials have a sense of entitlement.').

Is there compelling
evidence of Social
Inflation, in general, even
existing?

Often the cited 'evidence' of Social Inflation either is along the lines of...

- Insurers are talking about it in conference calls.*

or

- Insurers' gross dollars of incurred losses are rising "more rapidly than economic inflation would suggest or explain."**

...neither of which, of course, is compelling evidence at all in any rigorous sense.

* See, e.g., Noah Heim, "Social Inflation: Rising Tides in the Insurance Markets" (Dec. 9, 2021); Sangmin S. Oh, "Social Inflation" (Oct. 31, 2021).

** See, e.g., Insurance Research Council, "Social Inflation: Evidence and Impact on Property-Casualty Insurance (The Institutes, June 2020).

In research attempting greater rigor, the evidence that social inflation actually is occurring still falls short of compelling. Consider, for example, the conclusion from the most recent work by C.A.S. and I.I.I.:

If one "**assumes no changes within the insurance organization, ...and one assumes inflation has been constant;**" ..."**three lines of business ...display characteristics consistent with** what one would expect from most common discussions of **social inflation**...."


In other words, the industry still is a long way from establishing that currently there is a social inflation problem at all.

Further (and crucially), work on social inflation often is loose with its logic:

- The research often equates **"litigation"** with **"frivolous litigation."** "Litigation" is neutral between a good faith dispute, a bad faith plaintiff's position, and a bad faith defense position.
- **Just because a defendant loses a case, or even loses a case big, does not mean the verdict was wrong or the litigation was frivolous.** It does not even mean that the verdict will be paid. Verdict data is sparse and poor, but we know that 90%+ of civil cases do not go to trial or verdict, and that the judicial system is structured to reverse verdicts unsupported by evidence.
- **Litigation only is frivolous if it is unsupported by the evidence.**
- If verdicts are supported by the evidence, then **a rise in gross dollars of verdicts is INCONSISTENT with an increase in frivolous litigation** but is **CONSISTENT with an increase in questionable claims justifications by insurers.**
- **Work on social inflation often misses these points.**
- For example, **just last month at NCOIL, an ACPIA spokesperson made the error of asserting that if the gross dollars of verdicts are going up then it must be social inflation.**

In the end, after reading all industry published work I can find, ...

- **I cannot find any compelling data showing that there is an overall increase in insurance litigation at all** (either challenging claims denial or bad faith or subrogation).
- **I cannot find any compelling data showing that there is an increase in *frivolous* plaintiffs' insurance litigation** (meaning plaintiff's lawsuits unsupported by evidence).
- **I cannot find any compelling data establishing and quantifying the effect of alleged *frivolous* plaintiffs' insurance litigation** (meaning plaintiff's lawsuits unsupported by evidence) **on premiums.**
- **I cannot find any compelling data establishing and quantifying the effect of alleged *frivolous* plaintiffs' insurance litigation** (meaning plaintiff's lawsuits unsupported by evidence) **on insurer loss ratios.**



Generalities aside, what evidence
is there of each claimed Social
Inflation Factor happening?

Here is a list of the collective set of seven external factors that in some form or another show up in one or another discussion of Social Inflation (the quoted, descriptive language is from Triple-I's website on Social Inflation):

- **The Government** (in two ways):
 - "Rollbacks of previously enacted tort reforms intended to control costs"
 - "Legislative actions to retroactively extend or repeal statutes of limitations"
- **How Plaintiffs' Lawyers do Business** (in three ways):
 - "Increased attorney advertising and increased attorney involvement in liability claims"
 - "The emergence and growth of third-party litigation financing"
 - "Proliferation of class-action lawsuits"
- **The General Public** (in two ways):
 - "Changes in underlying beliefs about the appropriateness of filing lawsuits and expectations of higher compensation"
 - "...an increase in juries' sympathy toward plaintiffs and in their willingness to punish those who cause injury to others"

Data on the Government

- This turns out to be is a very specific assertion that **four State Supreme Courts have found damage caps violate their State Constitutions**, and that from 2015 to 2019, **more than 10 states and the District of Columbia made changes to their laws on civil statute of limitations for child sexual assault victims**. (See, e.g., Geneva Assoc.).
- A super-majority of states have done neither. **There is no national trend**.
- That said, two obvious ways to demonstrate that legislative/judicial rule changes cause rises in incurred losses and premiums would be (1) to do a **sister state comparison** of incurred loss and premium data in states that have damage caps or shorter statutes of limitations with those that don't; or (2) to do a **before and after comparison** within the states where the law changed.
 - The **Geneva Association** did the **sister state comparisons** and concluded, **"It is not obvious that changes in judicial protocols and reinterpretations of legal doctrines can explain the recent pick up in compensation awards**. There is **at best only a weak correlation** between those jurisdictions where the very highest jury awards have occurred and those states with a relatively poor reputation for fair and reasonable liability systems."
 - And I cannot find any public-facing data that incurred losses or premiums went up in States that struck down damage caps as unconstitutional, or in states that changed their statutes of limitations (although **insurers certainly have data that they could show you if it helped their position**).
- Just last year, the **Cato Institute** published a book focusing on medical malpractice, which found that **damage caps don't work**.*

*Bernard s. Black et al., ""Malpractice Litigation: How It Works. Why Tort Reform Hasn't Helped." (Cato Institute 2021).

Data on how Plaintiffs' Attorneys do Business

- Here the assertion is that in insurer involved litigation, incurred losses are going up because of three influences:
 - (1) **plaintiff's attorneys** are advertising more resulting in them getting involved earlier and more often in claims;
 - (2) **third party litigation funders** increasingly are financing more plaintiffs and attorneys; and
 - (3) there are more **class actions**.
- Last year's work by the Cato Institute also found that if there is a problem with rising litigation costs, the problem does not track back to plaintiff's lawyers, but rather to **hourly billing practices of insurance industry lawyers as a key reason why insurance litigation costs are rising**.
- Work published just last month by finance professors from the business schools of Harvard and Stanford concluded that **TPLF's do not drive frivolous litigation filings**.
- It turns out that the assertions about class actions focus almost entirely on securities class actions, and **in 2021 both the number of securities class actions and the aggregate settlement amount of those claims went down**. (National Economic Research Associates) Of course, premiums did not go down.


Data on the General Public

- Here, the specific claim is that **millennials** have an **anti-insurer bias** and **a sense of entitlement** that is seeping into the jury pool **inflating the frequency and size of verdicts unsupported by the evidence**.
- This claim assumes millennials constitute a sufficient percentage of the jurors to impose a verdict—**there is no data** concluding either **that jurors are mostly millennials** or **that the attitudes of millennial jurors are changing verdicts**.
- There isn't even compelling data on the premises--a rise in plaintiff's winning cases, or a rise in average jury awards, or a rise in generic anti-insurer sentiment. Rather, according to industry and independent sources, **the evidence either is scant, mixed, non-existent, or proves the contrary**.
 - While there is some evidence that average verdicts are rising, there is "scant evidence that, social inflation has led to a profusion of jury verdicts out of proportion to actual damages," and to the extent there are such verdicts, the verdicts "were likely reduced by the appellate courts and/or trial judge." (CLM)
 - "The empirical evidence for the link between anti-corporate bias and jury awards is mixed;" and even the most supportive study on the effect of anti-corporate bias on the size of jury awards found the effect was "modest." (Geneva Assoc.)
 - It has been and continues to be that most Americans believe there are too many personal injury lawsuits today, although younger people feel this less so. (IRC Survey results released 6/28/22)
 - "Despite numerous anecdotal reports, there is" little direct evidence about general attitudes of entitlement." (IRC)
 - "the perceptions of companies' senior attorneys and executives of the litigation environment have improved over recent years despite the pick-up in jury verdicts." (Geneva Assoc.)
 - "Mixed evidence in support of the changing sentiment towards big business and insurance companies as the primary driver of social inflation." (Oh)

Two conclusions on data:

- I have focused today's presentation on the industry's data and neutral data, and discussed what it shows or does not. That said, there is opposing data. If you have not read the joint work of the Consumer Federation of America and the Center for Justice and Democracy, entitled *HOW THE CASH-RICH INSURANCE INDUSTRY FAKES CRISES AND INVENTS SOCIAL INFLATION*, then you should. It responds in detail to every industry data assertion about social inflation. <https://consumerfed.org/wp-content/uploads/2021/04/How-the-Cash-Rich-Insurance-Industry-Fakes-Crises-and-Invents-Social-Inflation.pdf>
- Limiting oneself to just the industry's own data of data from neutral sources, however, **if one looks for data supporting essentially any aspect of the claim that Social Inflation** is a "increasingly dangerous phenomena" "spreading at an alarming rate" "with devastating consequences for consumers and insurers alike," then **either there is no data, or the data is far from conclusive, or the data actually supports the opposite conclusion.**

Assuming Social Inflation
Factors are Inflating Incurred
Losses, how should we think
about this?



Plaintiffs' Attorneys and TPLFs

- With reference to plaintiffs' attorneys, industry-affiliated work complains that **insurers are "losing the analytics arms race against the legal system."** (InsuranceThoughtLeadership.com) This is an assertion that the folks funding plaintiffs are good at gaming the system.
- In considering this concern, it bears remembering that **TPLFs and plaintiffs' contingency lawyers are putting their own money up-front and on the line.** If attorneys and TPLFs are more frequently involved in claims, then that suggests they are seeing a lot of inaccurate claims handling by insurers, because otherwise it wouldn't pencil out to fund the litigation. In this way **it should work as a levelling of the playing field.**
- Nonetheless, the Chief Insurance Officer of Triple-I calls "litigation funding" the "most troubling" "key driver" of social inflation.
- But the **research** does not bear this out. Rather, it **confirms the 'levelling of the playing field' hypothesis.** A June 2022-published paper by Prof. Samuel Antill (Harvard Business School, Finance) and Prof. Stephen Grenadier (William F. Sharpe Chair of Financial Economics, Stanford Graduate School of Business) finds:
 - **"litigation financing does not lead to the filing of risky frivolous lawsuits,"** and
 - **"litigation financing deters defendants from engaging in wasteful bullying strategies"***

*Samuel Antill and Stephen R. Grenadier, *Financing the Litigation Arms Race* at 29, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3719238 (June 5, 2022). Prof. Antill confirms that he expects this result to hold for any mechanism of litigation funding; in other words, the study was of TPLFs but the findings should equally apply to TPLFs and to plaintiff contingency attorneys.

“Rollbacks of previously enacted tort reforms intended to control costs”

- While the data does not show any relationship of tort reform rollbacks to rising premiums or loss ratios, it bears noting that the entire design of litigation is premised on the assumption that an adversarial system will work as a free-market mechanism to sort out and control bad behavior by, for example, both insurers and policyholders. So-called “tort reforms intended to control costs” are **interfering in that free market** mechanism by putting **a thumb on the scales** in favor of one side – insurers.
- **There is no evidence that awards in excess of caps are not real and proper.**



“Legislative actions to retroactively extend or repeal statutes of limitations”

- **The industry concedes that this simply is a reference to some State legislatures determining that child victims of sexual abuse may not be in a position to seek justice until many years later when they are adults.** I assume that absent compelling reasons, no one opposes these victims having the right to recover from their abusers, and no one truly believes that a child is positioned to do so.
- **There is no evidence that awards in these cases are not real and proper.**
- There is no evidence that these cases have any material impact on incurred losses or premiums.

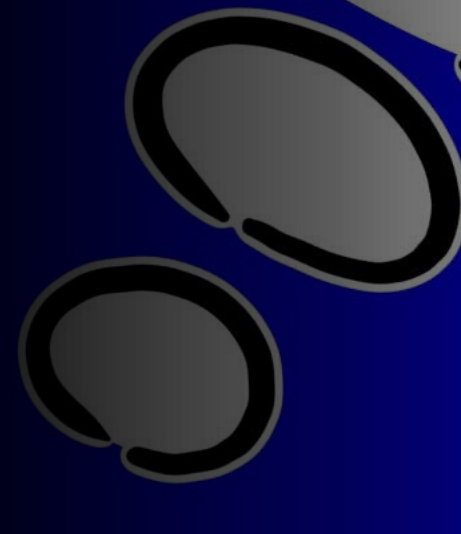
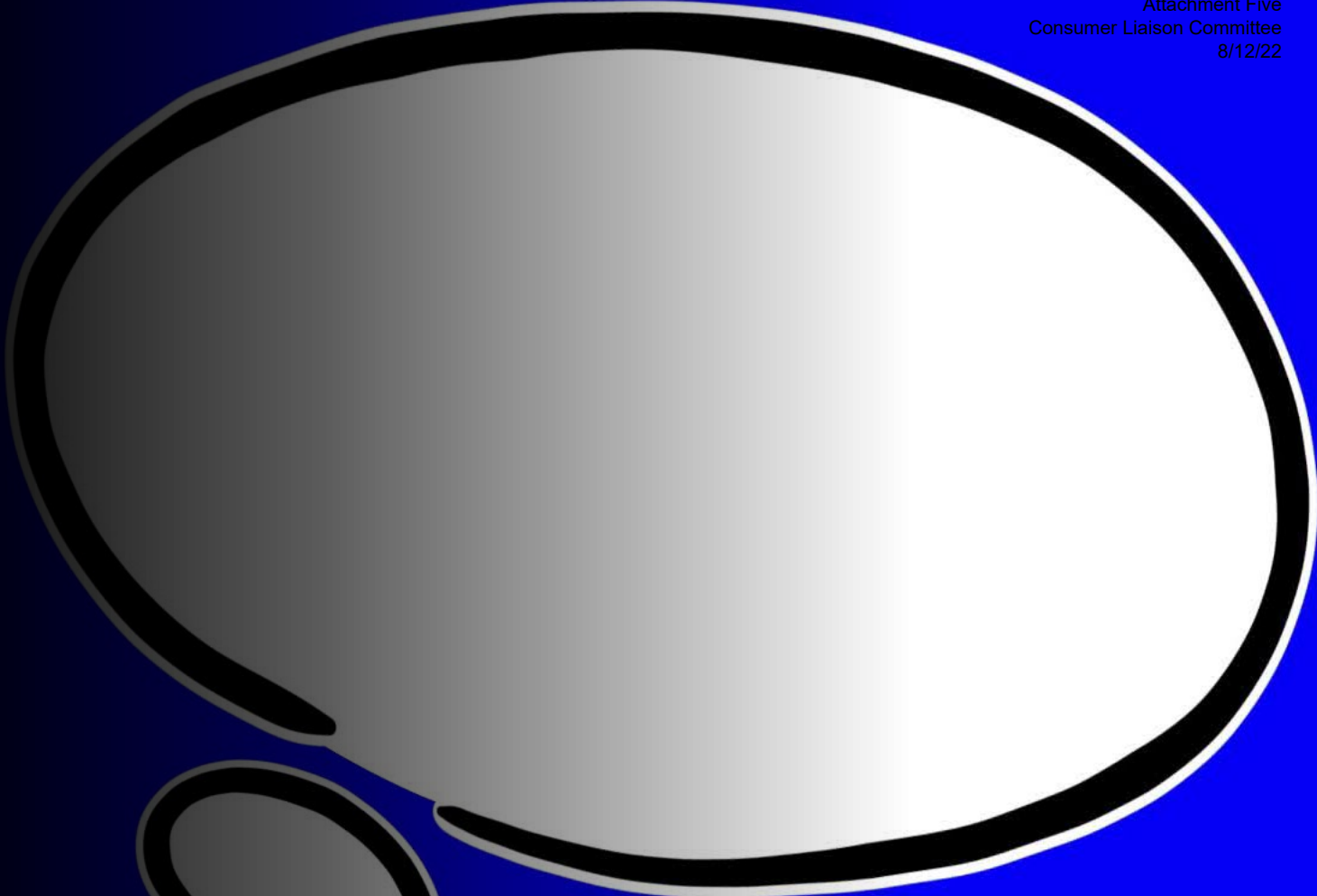
"Increasing numbers of very large jury verdicts, reflecting an increase in juries' sympathy toward plaintiffs and in *their willingness to punish those who cause injury to others*"

- **The whole point of a civil justice system is "to punish those who cause injury to others."**
- "More frequent and larger verdicts" does not equate to "inaccurate verdicts." **An equally likely and perhaps likelier explanation of an increase in the number and size of verdicts is that there is an increase in the frequency of defendant bad behavior coming to light.**

“Proliferation of class-action lawsuits”

A rational business, such as an insurance company, could conclude that if they squeeze each customer just a little bit, it will not be worth it for any customer to sue, but collectively the profit to the business will be large. Class actions are the justice system’s process response to that. **Proliferation of class actions is is consistent with the conclusion that an increasing number of businesses are misbehaving** in precisely this way.





What all this
boils down
to....

When one works through the assertions about social inflation, what emerges is that any of the industry or industry-friendly discussions of “Social Inflation” ultimately boil down to the same thesis -- the litigation strategies and skills of plaintiffs’ lawyers are the root problem. Here is but one example of how industry thought leaders say this:


“In recent years **personal injury lawyers have effectively deployed new strategies** to secure large court awards, whether through jury verdicts or out-of-court settlements. The **defense bar has been slower and less successful**”

-Jerry Theodorou, *The Scourge of Social Inflation* at 1 (R Street Policy Study No. 247, Dec. 2021)

- Keeping in mind that I am a former **defense** attorney, I am dubious of the position that if litigation is driving premiums and loss ratios, then the reason is that **defense lawyers are not as good as plaintiff lawyers.**
- As an Evidence and Civil Procedure professor who has done research on these kinds of issues, I can tell you ...
 - the system quite intentionally is designed to weed out frivolous claims, and does so even knowing the consequence will be to inadvertently throw out some meritorious claims as well; and,
 - there is no data supporting the intuition either that plaintiffs win more often than the defense wins or that the Rules of Evidence and Procedure are biased toward plaintiffs.
- The most likely accurate conclusion to draw is that if litigation is driving premiums and loss ratios, then the reason is that **insurers are doing business in a way that increasingly is making suing the best and perhaps only option for full recovery (and apparently, if these claims increasingly are being paid at higher rates in settlement or judgment, then claims adjusters, juries, and judges ultimately are agreeing).**

So, to summarize this presentation, I have tried to test the validity of the intuition of insurers that external, societal factors are in some way causing premiums and loss ratios to improperly, unjustifiably, and quickly rise. And what I found was:

- There is no evidence of social inflation as an explanation of materially rising premiums or rising loss ratios.
- There is no evidence of any alleged social inflation factor causing insurers to incur new, unusual, and materially higher, improper costs.
- There is no evidence of a social inflation crisis at all.
- It is not an indicia of the judicial or legislative system failing that defendants (or plaintiffs) are losing with a higher frequency than they expect. That is normal; all clients hope and expect to win. If the industry nonetheless is looking for explanations for losing more often and in larger amounts than it expects, then given that there is no evidence of an external cause, it perhaps is time for the industry to look inward.



So, the point of this presentation is to encourage you...

- Do not act without compelling data.
- Allow that both sides of an issue may have data and something to say.
- Do not blindly accept any side's assertion with confidence that something must be so.
- If an advocate for a position has data and does not give it to you, then consider what conclusion to draw from that.
- Do not permit premium increases or approve rate filings, nor re-order private markets, without confirming the assumptions, premises, and data being presented to you.

Questions

