

## SOCIAL INFLATION

*Social inflation is challenging the liability environment for companies and impacting potential claims payments for insurers, driven by a wide variety of factors such as anti-corporate sentiment, the rise of the litigation funding industry and even the growing use of jury psychologists. And it is no longer just a US phenomenon....*

<<>>

### THE 1 MINUTE DIALOGUE

- Social inflation trends are challenging to predict, as they're driven by 'soft' social ideas like public perception of corporate behavior, social media and changing demographics
- The increasing sophistication of the plaintiffs' bar and the changing composition of jury pools which can influence how cases are viewed and verdicts awarded
- New collective action options and a growing collective redress trend have resulted in increased liability exposure for companies amid softening of EU regulatory obstacles
- Traditional public and product liability insurance, as well as motor, professional, medical, workers' compensation and D&O insurance claims can all be affected by social inflation

<<>>

'Social inflation' describes increased insurance losses resulting from the growing phenomena of for-profit litigation funders, higher jury awards, more generous workers' compensation claims, legislated compensation increases and new tort and negligence concepts. It is especially established in the US, but is increasing globally. Driven by a generation-long decay in public trust of corporations, social inflation trends are challenging to predict, largely because they are driven by 'soft' social constructions, such as public perception of corporate behavior and changing demographics, especially with the increasing influence of social media.

"Simply put, the US has developed a culture of fault which can be exceedingly dangerous to businesses," says **Larry Crotser, Regional Head of Key Case Management, North America, at AGCS**. "The acute perception of economic disparity in the US, a deep-seated institutional distrust and the perception of the value of an injury, translates into larger than expected claim values. There's a deep dissatisfaction and resentment – even anger – with the status quo."

One way this plays out is larger jury awards, with a review by VerdictSearch showing a more than 300% increase in the frequency of verdicts of \$20 million or more in 2019 when compared to the annual average from 2001 to 2010<sup>1</sup>.

---

<sup>1</sup> Wall Street Journal, The specter of social inflation haunts insurers, December 27, 2019

## **RUNAWAY SOCIAL INFLATION: THE US PICTURE**

In the US, there were 79 class action settlements totaling \$2.3bn in 2020, up slightly from 74 settlements totaling \$2bn in 2019. Securities class action filings, as opposed to settlements, however, decreased by 22% (210) – an average of 17.5 cases filed per month. Despite the decrease, the total was still 13% more than the 10-year average<sup>2</sup>. The 2020 settlements included two in excess of the \$1bn mark for the first time since 2016. Most impacted sectors were technology (28% of filings), biotechnology (19%), financial services (15%) and manufacturing (12%). The median settlement amount of the top 50 US verdicts from 2014 to 2018 nearly doubled from \$28mn to \$54mn<sup>3</sup>.

A significant contributing factor to the social inflation phenomenon in the US is the increasing sophistication of the plaintiffs' bar, which has adopted tactics including the expanded use of jury consultants and psychologists specializing in group dynamics to influence the size of jury awards to plaintiffs.

Another factor is the changing composition of jury pools which can influence how cases are viewed and verdicts awarded. So-called 'millennials' and 'Gen Z' age groups now participate as jurors and their world view may significantly differ from older groups. However, in many cases, they also tend to seek consensus and may agree with the majority of fellow jurors while deliberating a verdict to keep from "making a scene", says Crotser. Jury composition impacts the outcomes of verdicts in a big way.

"In effect, the plaintiff uses psychological tactics to convince the finder-of-fact to more readily accept an inflated value of a case," says Crotser. "This process, known as 'anchoring,' starts at the outset of the case, sometimes before the lawsuit is filed in court, and acts as a leitmotif during the duration of the litigation."

With anchoring, people are influenced by information from their environment when making decisions without realizing they're being influenced, potentially impacting the eventual settlement amount.

## **AROUND THE WORLD**

Although social inflation is primarily a US phenomenon it has already impacted global tort activity due to similar drivers: perceived social inequalities, social justice demands, developments to include higher duties of care, expansions of liability theories, weakening of exclusions and the emergence of litigation funding firms and fewer cost deterrents.

While rare in Canada, since civil personal injury trials seldom proceed to jury there is a cross-over when Canadian companies are hit in US cross-border claims, where a company targeted in the US sees its Canadian affiliate also named in the lawsuit, an increasing activity:<sup>4</sup> 2019 saw 14 cases (four more than 2018) and just one less than the top year of 2011<sup>5</sup>.

---

<sup>2</sup> Woodruff Sawyer & Co., 2020 Securities class actions exceed the 10-year average, January 27, 2021

<sup>3</sup> Willis Towers Watson, Insurance marketplace realities 2020: How long will it last? 2019

<sup>4</sup> AGCS, Collective actions and litigation funding and the impact on securities claims: A global snapshot, July 2020

<sup>5</sup> NERA Economic Consulting, Trends in Canadian class actions: 2019 Update: Cannabis litigation leads to new highs, March 19, 2020

At the same time, the litigation funding industry - which first rose to prominence in North America and Australia - has ramped up activity outside of these territories. New collective action options and a growing collective redress trend have resulted in increased liability exposure for companies amid softening of EU regulatory obstacles. There has also been notable litigation funding growth elsewhere around the world – as widespread as in Saudi Arabia and South Africa.

“We see an uptick in the value of product liability claims that can result in payments that are astronomical compared to what they were before litigation funding was widespread, and with recent reports pegging the capital available to fund litigation at \$10B in the US alone<sup>6</sup>, that’s a lot of financial support for plaintiffs’ lawsuits,” says Crotser.

Meanwhile, in Germany, liability insurers are also beginning to finding out that the potential impact of social inflation can be expensive, adds **Joerg Ahrens, Global Head of Claims Key Case Management, Long Tail Lines, at AGCS**. “More court cases, higher settlements and more customer-friendly analyses of contracts have all impacted German corporations. It's not yet a dominant issue, but it's becoming visible, especially among self-insured companies with international programs.”

In addition, there is a growing number of parties involved. Ahrens cites an example from the logistics industry: “More and more people are ordering goods online, and logistics companies are responding with more drivers, who may be not as well trained as in the past, and more trucks. If a fatigued truck driver causes a car accident, the issue quickly moves beyond the individual's fault and liability. In such cases, lawyers focus not only on the driver's individual liability, but also on the employer's organizational fault,” says Ahrens.

Traditional public and product liability insurance, as well as motor, professional, medical, workers’ compensation and D&O insurance claims can all be affected by social inflation. “Brokers should install a multi-faceted approach to ensure they’re steering companies towards insurance partners who are experienced in the area of social inflation and very proactive on litigation/insurance trends analysis,” says Crotser. “Understanding what its impact can look like, with help from their insurance carrier, and having timely dialogues on expectations as new terms and conditions come out or renewals of insurance policies come around, is key.”

## **COURT CLOSURES AND SETTLEMENT TRENDS**

In the wake of the Covid-19 pandemic, court closures and uncertainty around reopening is impacting the legal environment. With attorneys working and conducting depositions remotely, the legal process has become more complex and sluggish. Plaintiffs realize that, even if their case makes it to court, it could be two years or more before it is tried before a jury. Others worry that jury trials won’t be feasible as long as social distancing rules apply. While there are some jurisdictions which have recently begun trying cases, it looks like there will be a significant delay before court business is back to normal.

“We saw very limited blockbuster personal injury trials since the beginning of March 2020, with one out of Washington with a verdict of \$410M for a Florida highway crash, and one for \$125M

---

<sup>6</sup> Bloomberg Law, How litigation finance works: Making millions off other people’s lawsuits, 2021

in New Jersey for a plaintiff severely injured by a falling telephone pole<sup>7</sup>. Many firm trial dates were pushed to 2021, or later, so we don't know if Covid-19 will stem the tide," says Crotser. "Perhaps plaintiffs suspect that when courts reconvene and some jurors are out of work, they won't be as prone to return outlandish awards, as we've seen in earlier economic downturns, but some commentators see no signs of "nuclear verdicts" abating. And some plaintiffs seem more willing than before to settle outside of court – we have seen that trending to a certain extent in our claims portfolio, driven, in part, by cash- flow issues."

<<>>

BOX

## **SOCIAL INFLATION**

### **WHAT'S BEHIND IT IN THE US?**

- Jurors distrust in big corporations and their lawyers
- Emergence of an industry dedicated to financing plaintiffs' lawsuits (litigation funding) – fewer cost deterrents
- Increasing sophistication of the plaintiffs' bar
- New psychological tactics to convince fact finder to accept more readily an inflated value – "anchoring" – emotions versus facts
- Active print and electronic advertising by the plaintiffs' bar
- Changing composition of the jury pool has potential impact on how cases are viewed
- Prospective jurors are more aware of "blockbuster" verdicts due to social media
- Medical expenses have increased year on year

### **WHAT'S BEHIND IT IN THE REST OF THE WORLD?**

- Shifts in perceptions and attitudes - delivering 'social justice' (judicial bench) because of assessment of new public sentiment and social norm
- Influence and proliferation of social media (narrative versus facts)
- New litigation tactics (e.g. exploitation of advanced analytics)
- Shorter claims cycles due to cost pressures and reputational aspects
- Legislative developments:
  - Collective redress (opt out – opt in, onus of proof, inhibition of statute of limitations)
  - Lower pleading standards
  - Developments in tort law – higher duties of care, expansion on (public nuisance) liability theories, weakening of exclusions, reverse burden of proof
- Emergence of an industry dedicated to financing plaintiffs' lawsuits (litigation funding) - fewer cost deterrents

<<>>

---

<sup>7</sup> Law 360, The biggest personal injury decisions and verdicts of 2020, December 18, 2020