State of the Property & Casualty Market for Public Entities
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It has been commonly discussed and widely understood that the insurance market is considered to be a “Global” market. Wildfires in California, tornadoes and convective storms throughout the Midwest, earthquakes in Mexico, as well as the recently faced Pandemic known as COVID-19 all contribute to the overall insurance marketplace stability. This will continue to affect every insured. Each event takes its toll on the market and wreaks havoc on the overall bottom line. It is no secret that the insurance marketplace has been “hardening” over the course of the last 18-24 months; with many considering our current situation the worst market conditions ever recorded, or at least since the 1980’s. Rates continue to skyrocket, carrier capacity is evaporating, retentions are increasing, new exclusions and coverage limitations are being added and introduced, and the list goes on.

The most recent, and arguably most significant factor, is the once in a generation pandemic known as COVID-19. According to Lloyd’s of London, COVID-19 is estimated to be a $3 - $4.3 billion event against their portfolio alone. In addition to this, social unrest, rioting, protesting, and increasingly severe Named Windstorm and Hurricane events are causing billions of insured losses. These are some of the more obvious factors behind the hard market, as they are commonly discussed and frequent contributors to the evening news. However, there are a number of additional underlying factors contributing to the current environment which are less frequently discussed.

The following outlines three underlying factors that have contributed to the current market conditions. These findings are supported by industry knowledge, real life examples, and direct market experience:

1. **“Social Inflation”**

   With no real definition being offered, Social Inflation often refers to the perception — or even expectation — by plaintiffs and courtroom juries that injured parties should receive highly inflated, multi-million (or billion) dollar awards. In today’s legal environment, there appears to be a common sentiment that “insurance will pay for it” when determining these large verdicts. To date, Social Inflation has large concentration in the following sectors; commercial auto, medical malpractice, certain professional and management liability lines such as directors’ & officers’ (D&O), and umbrella and excess liability. Social Inflation tends to be a more prevalent issue where coverage is in place for large corporations, municipalities and the perceived “deep pocket” organizations and individuals, as these are where the largest limits tend to be purchased. The Commercial Auto marketplace has been hit particularly hard by this emerging trend. Cases have involved trucking companies, or even state and federal employees, have been involved in accidents where no negligence on their part had been found. They may just happened to be in the wrong place at the wrong time. Due to injuries sustained by the other parties involved, these entities have seen verdicts in the range of $30 million, $50 million and sometimes up to $100 million. These losses quickly erode the entity’s primary layers, and pierce the excess policies in a hurry, which is where the higher limit amounts are offered. Excess and Umbrella underwriters had not fully anticipated being in play as frequently as they have been in recent history. Mike Hudzik, who is the managing director and head of casualty underwriting for the US & Canada at Swiss Re. is quoted as saying the following:

   > “Probably one of the biggest drivers of social inflation is the general anti-corporate sentiment that exists, reaching back to the financial crisis. It seems like it’s a long time ago in our rear-view mirror, but it really created an environment that continues to gain momentum today. Since that time, there’s been a greater division or separation of wealth, and there’s just generally a feeling that someone needs to pay when there’s some kind of damage or injury sustained, regardless of negligence.”

2. **Prevalence of Nuclear (or Super-Nuclear) Verdicts**

Nuclear, as well as Super-Nuclear jury awards, are reaching into the tens of millions, and in some cases, even billions of dollars. This is particularly seen in cases where human contemplative decision-making is prevalent. The reason behind this is due to the fact that humans are the only decision makers who can act based on emotion, with heightened emotions often amplifying outcomes rather than mitigating them. States, Counties, Public Entities and other Municipalities have all become too familiar with these large verdicts. This holds especially true in states such as California, New York, as well as others that do not have any form of tort liability reform. While some states have more "municipality-friendly" laws and tort reform to help shield them from these large verdicts, the overall insurance industry continues to feel the effects and is greatly impacted financially. According to the Wall Street Journal's analysis of data from verdictsearch.com, in 2019, there was a 300% increase in what is considered "nuclear verdicts" compared to the prior ten years. With new legislation making its way into states with favorable tort laws, insurers are choosing to shift capacity from the public sector into more favorable and profitable sectors and/or regions.

3. **Continuing Increase in Loss Cost Trend or "Loss Creep" and Valuations**

The commercial property insurance market has continued to tighten as we begin the fourth quarter of 2020. Two of the major factors that continue to impact this tightening property market are "loss creep" and "valuations." Bob Black, Executive Vice President and AmWINS' National Real Estate Practice Leader states:

> "Unlike in years past where blanket limits were many times granted without pushback, each account is now being reviewed on its own merits. Nearly every carrier is scrutinizing the valuations being utilized. Scheduled limits (applied via an Occurrence Limit of Liability endorsement) and margin clauses are making their way back into the equation for those insureds that are unwilling to increase their valuations to the point where the market is comfortable providing blanket limits."

Traditionally, property insurance was not considered to have a "tail" AmWINS explains, but "loss development", or "loss creep," is a growing concern for the market today. When a loss occurs, insurers will set an expected loss amount for that event which is known as the "loss reserve". Adjusters need to take the practice of reserving claims very seriously, and strive to be as accurate as possible. That being said, recent history shows that what we have been experiencing as of late is that months, or even years after an event occurs and a loss reserve has been set, claims are needing to be reevaluated, causing the initial reserve set for that claim to "creep" upwards. This is due in part to higher than anticipated construction and labor costs, the increased cost of materials, and improper valuation of the property originally reported to the company. This upward creeping is especially hard on insurers due to the fact that reserve funds had been previously set aside to pay for these losses, which in turn contributes to their bottom line. Insurers are now seeing those reevaluated claims increase over time by anywhere from twenty to forty percent. AmWINS states: "No longer is it just the 'magnitude' of losses that are considered: underwriting assumptions around perils that had traditionally been viewed as attritional, rather than catastrophic, are changing."

As you can see, there are multiple factors contributing to the adverse condition of the insurance marketplace; making an already complex industry even more complex. Alliant continues to stay intimately involved and in-tune to the challenges that lay ahead; actively preparing and strategizing the best course of action for our clients. We are specialists in municipality and public entity risks, but there are plenty of industry-wide concerns at play. Alliant will continue to actively track and stay abreast of each of the factors affecting the global insurance marketplace.

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