

# Insurance Buyers' News



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## Social and Economic Inflation Drive Up Auto Liability Claims

Combined U.S. personal and commercial auto insurer liability claim payouts were \$96 billion to \$105 billion higher between 2013 and 2022 because of social and economic inflation, according to a new Insurance Information Institute (Triple-I) study.

For personal auto liability insurance, increasing inflation drove loss and DCC (defense containment costs) higher by \$61 billion," the study said. "For the same period (2013-2022), increasing inflation drove commercial auto liability loss and DCC higher by \$35 to \$44 billion."

Liability insurance covers what the policyholder is legally obligated to pay because of bodily injury or property damage caused to another person, or persons. Every U.S. state except New Hampshire requires its drivers to purchase a personal auto insur-

ance policy, with mandatory minimum amounts of liability coverage, as a condition of operating a motor vehicle. Commercial auto insurance liability policies are commonly bought by small businesses and corporations to cover trucks and other vehicles used for commercial purposes, such as limousines and taxis.

Economic inflation is measured in the study as the Consumer Price Index (CPI) – All Urban metric, a U.S. Bureau of Labor Statistics benchmark, whereas social inflation indicates how insurer claim payouts exceed the CPI.

## Surplus Lines Policies Grow by Double Digits

OLDWICK, NJ--Total U.S. surplus lines direct premiums written (DPW) marked a double-digit growth rate increase for the fifth consecutive year, climbing by 19.2% to reach a record \$98.5 billion in 2022, according to a new AM Best report. (Note: In general, surplus lines companies underwrite risks that the conventional insurance market will not.)

This comes as the overall market for property risks—both personal lines property (homeowners) and commercial property—remains challenging, especially for accounts that have suffered large or multiple weather-related catastrophe losses, property risks, and an increase in claims totals due to elevated construction costs. These conditions have enabled surplus lines writers to carve out a bigger portion of total property/casualty (P/C) industry premium, which increased to an all-time high 11.2% in 2022, up from 10.4% a year earlier.

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### What Is Social Inflation?

Unlike general economic inflation, which insurers can mitigate using pricing models and loss reserves, social inflation can arise from factors that are difficult to foresee, such as rising costs from:

- ✱ increases in the number of outsized jury awards
- ✱ legal proceedings that take longer than reasonably expected
- ✱ rollbacks in tort reform that overturn statutory limits on non-economic damages.

Considered to be a growing cost of doing business in the insurance industry, social inflation is influenced by negative public sentiment about larger corporations, litigation funding, and tort reform rollbacks at the state legislative level, all of which have increased liability costs. Shifting public perceptions and attitudes may lead jurors to sympathize with plaintiffs when awarding damages. Jurors may also believe the business, or the insurance company, has unlimited financial

resources, leading to what's commonly known as "shock" verdicts. These monetary damage awards are much higher than expected based on the evidence presented at trial, often exceeding \$10 million.

### Personal and Business Auto Liability

"The business of personal auto liability insurance is also many times larger than commercial auto. Personal auto liability had \$152.6 billion in net earned premiums in 2022, four times as much as commercial auto liability," the study stated. Yet personal auto policyholders typically have \$100,000 or less in liability coverage while a typical commercial policyholder has a coverage limit of \$1 million, the study explained.

Supported by detailed analyses of claims payouts dating back years, the study concluded that, for personal auto liability insurers:

- ✱ Losses have been growing faster than premiums in recent years
- ✱ Since Accident Year 2020, standardized losses rose 15 percent while standardized premium fell 13 percent
- ✱ Severity, the size of losses, increased dramatically after 2019

The study concluded that commercial auto liability insurers saw:

- ✱ Losses grow faster than the overall economy
- ✱ Social inflation as a primary influence on these losses prior to 2021
- ✱ The average size of loss — claim severity — increase dramatically since 2020

"For both personal and commercial auto liability lines, social inflation was the main source

### *This Just In*

"The contraction in overall capacity owing to tighter admitted company risk appetites creates an environment that plays to the strength of surplus lines insurers with some of their creative market and product-oriented solutions," said David Blades, Associate Director, AM Best. "These skills are especially valued."

According to AM Best data generated for the report, eight of the top 10 lines of the segment's coverage grew their DPW (direct premiums written) by more than 10% in 2022, led by the commercial property, commercial auto, and general liability lines, with the latter including boosts the from umbrella and excess liability, cyber, and professional liability segments.

Pricing pressures have continued for many commercial lines of coverage in the past two years, with both non-admitted and admitted companies focusing on core business and culling what they considered underpriced, borderline surplus lines accounts from their portfolios. These factors help drive the surplus lines share of P/C commercial DPW above 20% for the first time in 2021, ending 2022 at 21.6%.

of increasing inflation before 2021. For 2021 and later, increasing inflation came from a combination of economic inflation and social inflation," the study said.

The study, "Impact of Increasing Inflation on Personal and Commercial Auto Liability Insurance," was researched and written by Jim Lynch, FCAS, MAAA, Triple-I's former chief actuary; Dave Moore, FCAS, MAAA, president, Moore Actuarial Consulting LLC; and Dale Porfilio, FCAS, MAAA, Triple-I's chief insurance officer. The research methodology compares the latest loss development patterns to a baseline assumption without social inflation and with stable inflation rates. ■

# More Rate Reductions Expected for Professional Liability Coverages

It looks like the soft markets that started last year for Management Liability (ML) and Professional Liability (PL) insurance will continue to soften over the second half of 2023.



This is the result of new entrants to that market and increasing capacity, which will continue to stimulate competition and drive down premiums. This is the conclusion of a new report, “2023 US Management and Professional Liability Market Outlook,”

by Risk Placement Services (RPS), a wholesale insurance broker and managing general agent. The report examines and provides insights into the current state of the professional liability sector.

Commenting on the report in a webcast, RPS Executive Vice President for Executive Lines

Manny Cho said, “The management liability and professional liability market as a whole is still a challenging sector .... Even if affordable coverage is not hard to come by and customers are happy with the rates they’re being presented with, there are nuances and differences of coverage that really need to be paid attention to.

“This is probably the most unique market that we’ve been in in quite some time,” continued Cho. “We have a confluence of a lot of different things coming together that is really causing soft market conditions on almost every single line of business. And then we also have economic conditions that are putting pressure on our lines of business because of the hardening or reduced capacity and increased pricing in other lines of business such as property.”

## Rate Reductions

Cho went on to speculate that rate reductions in various professional liability coverages could be “anywhere from 10 to 20 percent” during the rest of 2023.

But that doesn’t necessarily make it an easy market for brokers and agents to operate in, and with price no longer being the differentiator it used to be, agents need to look at other areas to ensure they’re delivering the best for their clients,

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while also protecting their own books of business in a shrinking market, according to the report.

According to a report in the brokerage publication *ALM Property Casualty 360*, some of the major takeaways of the report are:

- ✱ For D&O, the average renewal premiums are now at between 20% and 30% of the previous year's price. "It is truly again a buyer's market," RPS Senior Vice President Rodney Choo said.
- ✱ In employment practices liability, premiums have stabilized and most renewals without a difficult claims history are now seeing flat rates, according to RPS Area Senior Vice President Dave Tardif.
- ✱ Fiduciary lines are no longer an overlooked coverage, according to RPS Area Vice President Jack Rosen. This is due to a changing claims landscape: "A coverage that used to be a throw-in is now facing substantial litigation, and as claims frequency goes up so do rates."
- ✱ The architects and engineers sector is seeing most renewals coming in at a flat rate, but "the majority of carriers are still limiting the amount of capacity [limits] that they will put up for any one firm," says RPS Senior Vice President Ron Kiefer.

"Almost every market we operate in is in a very competitive market situation, with high levels of capacity and good rates and good terms and conditions available," Cho concluded. This makes it a difficult market for brokers, and it is in times like these that partnerships come into their own." ■

## Why Buy Professional Liability Insurance?

**It might surprise you to know that it's not just doctors, lawyers and architects.**

All kinds of people need professional liability coverage, including financial analysts, corporate trainers, numerous types of consultants and law enforcement professionals.

### Even FBI Agents Need Professional Liability Insurance

According to an article in *Law Enforcement Today*, "FBI agents tasked by fired former Director James Comey to take down Trump during and after the 2016 election were so concerned about their potentially illegal behavior that they purchased ... liability insurance less than two weeks before Trump was inaugurated as president."

Forty percent of individuals and businesses believe they may have professional liability risks but have not purchased insurance for it, according to a recent survey of small business owners by The Hanover Insurance Company.

Over the past twenty years there have been many changes in the ways businesses interact with customers and they may be surprised to discover they now have a gap in their liability coverage. Many businesses don't realize that their general liability does not cover profes-

sional liability (PL) exposures.

In addition to lawyers, doctors and accountants, many businesses now need PL insurance. You don't have to consider yourself a "professional" to need coverage for negligent acts. If you give advice and recommendations, if you create programs or products for your customers or if you provide a service, you need liability protection.

And it's not just you who could be the cause of the alleged negligent act. Your business can be sued for any alleged wrong or error committed by any employee representing your brand, including temporary staff and independent contractors.

For example, suppose a professional photographer hires a temporary assistant for a job. If the photographer's assistant is alleged to have been negligent or have committed an act of libel or slander against a client, professional liability insurance could protect the photographer's business from unexpected legal expenses.

There are risks involved in hiring temporary staff and independent contractors, but the operational and financial benefits often outweigh them.

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### Defense Costs

One of the most important reasons to carry professional liability (also referred to often as errors and omissions) insurance coverage is for defense costs.

In the medical field, where you find the most extreme examples of costly lawsuits, 65 percent of claims are withdrawn before trial and 90 percent of claims that go to trial are denied, according to the Physicians Insurance Association of America. Nonetheless, it costs an average of \$120,000 to defend frivolous cases.

### Claims-Made Policy

It is important to understand that most PL and E&O policies are written as “claims-made,” which means the policy only covers claims filed during

the policy period. A few companies offer occurrence-based policies, which cover any qualifying claim arising from an incident that occurred during the policy period — no matter when filed. If you switch from a claims-made to an occurrence policy, you must make sure you don’t create a gap in coverage.

In specific situations, a claims-made policy may allow an extended period for reporting claims: when an insured dies, retires or becomes permanently disabled. This is an important feature because new claims can be filed years after the policy period. To qualify for this feature, the insured usually must be at least 55 years old, and he/she has had to maintain coverage with the same insurance company for several years — something to plan for if retirement is in your near future.

If you have any concerns about the liability coverages for your business, please give us a call. ■

# Professional Liability Policies Are Unique

Unlike property insurance or even general liability insurance, the policy wording used for one client is not necessarily suitable for all clients. Whether you buy a PL or E&O policy, it usually will be tailored to the specific needs of your business classification. For instance, a policy for real estate brokers typically includes coverage for failure to advise clients on the existence of fungus, asbestos or bacteria. Policies for accountants might provide coverage for acting as a trustee or administrator of an estate. Some policies also cover inadvertent transmission of computer viruses and corruption of customers' data.

Examples of other professionals who need protection include:

- \* Architects and engineers
- \* Bookkeepers
- \* Certified financial analysts
- \* Dog groomers
- \* Home inspectors

- \* Landscape architects
- \* Optical and hearing aid professionals
- \* Printers
- \* Social workers
- \* Software companies
- \* Veterinarians

Many insurance companies offer group policies to members of trade associations. In other cases, insurance companies form buying pools that professionals can "join." Miscellaneous professional liability coverage is also available for a variety of businesses such as translators, meeting planners, publishers, and collection agencies. If you need coverage, we can advise you on the best approach.

Sole proprietors may choose to protect their personal assets by forming a limited liability company, but their corporate assets are still at risk unless they buy E&O coverage. ■

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