APR - ALTERNATIVE MARKETS

DEDICATED TO PUBLIC ENTITY

Public Entity Insurance Market Outlook for 2022

The demand on insurance carriers to deliver profits, the limited participants in the public entity market, and inflationary pressures on operational and claims expense contribute to increased premiums throughout 2022. As operational and claim costs increase, premiums are adjusted to cover anticipated liabilities to deliver acceptable profit margins. The limited number of carrier participants in the public entity market compounds the costs associated with losses and operations. Over the last 18 months, several carriers have exited the public entity sector because of rising risks and falling profits. Carriers that remain in the market are either reducing limits or requiring a higher SIR but are offering no premium reduction in return.

The insurance market, like many industries, is struggling with the effects of inflation. Talent management is challenging, and the acquisition and retention of staff relies on competitive salaries, effective training, benefits, and a manageable workload. Wages and benefits are driving up the cost of business as the demand to improve system efficiency to prevent malicious cyber-attacks in remote work environments increase.

Claims-related expenses such as medical costs, public sentiment toward target defendants, inconsistent jurisdictions, and defense costs drive volatility in claim values. Public entities are struggling to maintain a balance between settling cases or vigorously defending them. In either case, the public entity's reputational capital may be at risk.

Large losses and reduction of investment income drive the increase of combined ratios.

Revenue from premiums and investment income are not offsetting carriers' increased claims and operational expenses. Catastrophic property losses due to storms and fires and nuclear verdicts on liability cases significantly impact the overall cost of claims to insurers. Inflation is increasing the general operating expenses for workforce and administration while decreasing the return on investments. Because the combined ratios are increasing, insurers are forced to charge higher premiums to cover expenses.

Reduction in public entity market participation continues to inflate premiums.

Several carriers who write public entities have exited the marketplace because the outcome of claims is less predictable. Contributing causes for the exit include district, state, and federal courts that inconsistently apply qualified immunity to law enforcement; civil unrest and distrust of public officials influence state legislators to rewrite laws to hold officers and officials accountable; and waning public faith in the justice system. People are losing patience waiting for the judicial system to deliver justice, and public opinion is often shaped by camera footage posted online and 24/7 media coverage before all the facts are known. Public entities that have not yet established reputational capital with the communities they serve are in danger of a large verdict by an unsympathetic jury. With fewer insurance carriers in the space, the demand is increasing financial risk for the remaining insurers and driving higher premiums.

Emerging Trends: Notable Factors Impacting Each Line of Coverage

No line of coverage is immune from premium increases, and each is associated with a unique risk that may increase its financial exposure. Inconsistent court decisions, supply chain, deteriorating infrastructure, inflationary costs, and unsettled case laws are all unpredictable factors that insurers must consider in anticipation of future losses.

Auto

New and expensive vehicle technology and difficulty obtaining necessary parts lengthen the repair time and related loss of use. New cars are not abundant, making the purchases of new fleet or replacement vehicles challenging. Because of the increased costs associated with repairs, replacement, technology, special equipment, and claim settlements, auto premiums are expected to increase.

The following factors impact the average costs of auto claims:

- The costs of replacement vehicles have increased because of lower supply.
- Technological improvements in vehicles have increased repair and replacement costs.
- Rental vehicles are scarcely available, and fees have increased.
- Repair and replacement parts are not readily available.
- Medical treatment costs, wage losses, and future medical and home care costs have increased and impacted the value of injury settlements. Traumatic brain injury claims, in particular, are highly subjective and difficult to defend.
- Auto claims involving law enforcement often involve the community's overall sentiment (whether positive or negative) toward law enforcement.

Liability

Trends influencing liability risks and costs include the legal environment, stressors on infrastructure, risk transfers, and road design. In general, plaintiffs target certain deep pocket defendants such as large pharmaceutical companies, public entities, or trucking companies that are easy to dislike or fear. Defense attorneys attempt to humanize corporate or public entity defendants amidst negative publicity; however, a defendant's tarnished reputation may be unsurmountable, resulting in historically high costs to settle and defend cases. In 2020, many states extended the statute of limitations and postponed hearings and trials due to the pandemic. The result is prolonged litigation, some of which has bled into 2022.

The legal environment for liability claims against public entities is evolving. As state populations shift and grow, jury pools are changing, and past outcomes may not be indicative of future results. Additionally, judges are reluctant to grant summary judgments based on immunity so cases are often forced through a lengthy litigation process. Tort cap limits that align with the consumer price index are increasing.

As a result of the COVID-19 pandemic, many people have relocated, thus impacting jury pools. According to the US Census, Texas, Florida, and Arizona saw the highest increase in residents in 2021; California, New York, and Illinois, by contrast, experienced population decreases of 367,299, 352,185, and 122,450, respectively, due to domestic migration. The impact of the population shift on traditionally conservative juries is yet to be determined.

Many state tort caps are sensitive to inflation, those that are will increase in 2022. For example, Colorado increased its tort cap from $387,000 for a single person injury to $424,000 beginning January 1, 2022. North Dakota created a schedule through July 1, 2026 that increases the current single person injury limit of $375,000 to $500,000: the per occurrence limit over the same time frame will double from $1million to $2million. Such increases, along with the erosion of the application of immunity to preclude litigation, has created rising expenses for defending such suits and higher risk of trial by jury.

Weather and climate disasters soared in 2021. According to the National Centers for Environmental Information, 20 events were recorded, the total losses of which exceeded $1 billion. These events include one drought, two floods, eleven severe storms, four tropical cyclones, one wildfire, and one winter storm. The brutal nature of these storms not only causes severe property damage but impacts infrastructure and increases the likelihood of falling trees—both a prelude to catastrophic injury or property damage and an increase in financial risk to public entities.

Public entity infrastructure for water and sewer systems has also been negatively affected by the recent surge in natural disasters. Population growth has increased the physical demand on older structures and systems to work consistently and effectively. Across the country, hurricanes, 100-year floods, and tornadoes test the capacity of water and sewer systems. To effectively manage storms and flooding, these systems require increased capital and time to repair or replace. Water breaches and sewer backup claims can impact large residential areas, and public entities may not be adequately protected by ordinances, immunities, or tort caps. The environment may entice plaintiff attorneys to formulate class action lawsuits that are costly to defend.

Contracted services required for capital improvement related construction projects present another high hazard risk. Many contracts for road construction, dam maintenance or other upgrades continue to require minimum indemnity limits of $1 million, inadequate to cover the cost of catastrophic claims. As a result, public entities are in jeopardy of incurring a portion of these costs. Contracts for high hazard construction must be scrutinized for indemnity language and adjusted to require higher minimum limits for contractors.

Public entities have also experienced an increased volume of road design cases. Roads and traffic designs are impacted by increases in population, and public entities must budget to alleviate congestion and repair streets to avoid vehicular accidents. State mandatory financial responsibility laws have been stagnant for years and are typically inadequate to cover serious injury. Some examples include California's mandatory limit of insurance of $15,000 for liability, and Florida's limit of $10,000. Claimants who are severely injured are often inclined to develop theories of poor road design or inadequate traffic signals to pursue damages against a public entity for compensation.

Law Enforcement

Congress did not pass the George Floyd Act, and there are no statutory changes regarding law enforcement and immunity at the federal level. The US Supreme Court has maintained that officers are held to a reasonable standard based on the circumstances of each individual case and clearly established laws. Many states, however, have passed legislation that limits immunity, requires body cameras, changes policies related to search and seizures, and places restrictions on restraining methods. New legislation has not been tested in state courts, and interpretations of these statutes remain to be seen. It is anticipated that, in the states that have passed legislation, more cases will be brought in state rather than in federal courts. There will be fewer cases disposed of based on immunity, and claim costs will increase because of unlimited damages, reimbursement of plaintiff fees, and increased defense costs.

Across the country, the potential for a successful defense of officers and departments is closely related to community perception. Civil unrest related to law enforcement negatively impacts social sentiment toward law enforcement in many communities, and thus defending law enforcement has become more challenging. George Floyd's family settlement was $27 million; Breonna Taylor's family settlement was $12 million. Given the latest social sentiment and negative publicity around law enforcement, plaintiffs are more confident than ever about demanding large sums, regardless of liability or potential immunity. The large recovery potential is not lost on litigation finance firms; accordingly, investments in the pursuit of social justice and large cash settlements provide capital to plaintiffs, pressure to deliver a return, and less opportunity to resolve for a reasonable amount short of trial.

Sexual Abuse and Molestation

Settlements for sexual abuse and molestation have reached record levels. Target defendants for related claims include schools, religious organizations, and nonprofit entities. Many states have extended the statute of limitations, and the publicity surrounding allegations of abuse has increased, which has encouraged additional claimants to step forward.

The USC sexual abuse and molestation case encompassed over 700 victims in three settlements that exceeded $1.1 billion. The Michigan State/Larry Nassar settlement awarded $500 million to 300 victims in total. Additionally, the Michigan Department of Corrections settled a class action lawsuit brought on behalf of 1,300 juveniles alleging a failed classification system wherein they were not segregated from the adult male population; here, the settlement was $80 million. The reputational harm to these institutions and others similarly situated is incalculable, and future claims of this nature are certain to be heavily scrutinized by the public.

Good hiring practices, training, and accountability are the keys to preventing claims. Workforce shortages and expectations of higher wages have added to the existing challenge of finding skillful talent to fill vacancies. Unfilled positions can lead to desperation and result in compromising new-hire qualifications. Adequate background checks should be completed and carefully examined before hiring. Complaints that are received about existing staff should be investigated thoroughly and carefully weighed to determine whether the infraction warrants disciplinary warning, transfer, or termination.

ALLIED PUBLIC RISK

Employment Practices

As diversity and inclusion efforts within companies intensify, discrimination-related claims have increased. Firms should proceed with caution to ensure that diversity and inclusion policies and practices are current, compliant, and do not embody exclusionary practices.

Recent notable settlements include an action against the Michigan Department of Corrections wherein a couple pursued a discrimination and hostile work environment claim based on unwelcome conduct and communications based on race; the combined settlement was $11.4 million. St. Louis County negotiated a post-verdict settlement for $10.25 million based on sexual orientation discrimination and failure to promote an employee. A man in North Carolina obtained a verdict of $10 million for reverse discrimination, claiming that as a white male, his employment was adversely impacted because of his employer's efforts to diversify management. Employment cases typically shift plaintiff attorney fees and costs to the defendant, further increasing the expense of verdicts.

COVID-19-related exposures are another potential risk to public entity employment practices. Mandatory vaccinations, mass terminations for refusal to vaccinate, work-from-home accommodation requests, and potential breaches of privacy within remote work may give rise to future claims. The Public Readiness and Emergency Preparedness Act (PREP) and workers compensation as an exclusive remedy may offer effective defenses for employment claims related to COVID-19. The nature of these complaints is unprecedented, and it remains to be seen how courts will decide these cases.

Summary

Given the volatile and unpredictable conditions outlined above, it is expected that carriers currently in the public entity space will continue to reduce limits and require higher self-insured retentions without reducing premiums. Policyholders may need to increase their self-insured retention and in so doing, must focus on strong risk management and claim prevention strategies to maintain costs and obtain adequate coverage. When presenting an application for insurance, public entities are encouraged to share specific efforts on capital improvements, community engagement, policies, practices, and claim prevention strategies to facilitate coverage as effectively as possible.

Resources

https://www.census.gov/newsroom/press-releases/2021/2021-population-estimates.html

https://www.ncdc.noaa.gov/billions/

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