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The Social Inflation Survival Guide:

Identifying and Surviving the Dangerous Triple Barrel Threat of Social Inflation, Economic Inflation, and Greenflation in a Judicial Environment Swarming With Reptiles and Bombarded With Nuclear Verdicts

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Insurance professionals and counsel deal with it on a daily basis, plaintiffs' personal injury lawyers are driving and benefiting from it, consumers and policyholders are paying for it, litigation funders are financing it, and pundits are now writing about it with greater frequency. It has been around since the 1970s, but something about it is looming much larger these days. When coupled with economic inflation, it appears to be on steroids. It, of course, is social inflation and a civil tort system that, in some respects, is out of control.

Part 1: Identifying the Causes and Scope of Social Inflation

I. Social Inflation 101

Social inflation refers to the increasing costs of insurance claims (defense and indemnity) resulting from societal trends such as litigious proclivities, large defense costs, nuclear jury awards, broad insurance policy interpretation, and a plaintiff-friendly and policyholder-friendly environment. *The Wall Street Journal* recently described social inflation in insurance industry parlance as referring to: "[A]n upward creep in perceptions by an injured party of what they are owed, their willingness to pursue that via the legal system, and what that means for insurance policies covering companies' liabilities." Telis Demos, *The Specter of Social Inflation Haunts Insurers*, Wall St. J. (Dec. 27, 2019), available at https://www.wsj.com/articles/the-specter-of-social-inflation-haunts-insurers-11577442780. Another way to define social inflation is the amount that liability claim costs are rising above the rate of general economic inflation.

Social inflation has existed at least since the 1970s. As early as 1977, Warren Buffet referred to social inflation as "a broadening definition by society and juries of what is covered by insurance." *Id*. (internal quotation marks omitted).

Undoubtedly, the impact of social inflation has been felt most heavily in the United States due to our civil justice system. Other countries such as Australia, Canada, and the U.K. have experienced social inflation, but to a lesser extent. Social inflation appears to be gaining traction now in Europe**.** Collective actions, the rough equivalent to class actions in the U.S., have doubled between 2018 and 2020, even prior to an EU directive giving rise to additional actions. There have been substantial litigation funding activities in Europe as well. Even acknowledging differences in policy wordings and issues, insurers in the United States to date have generally done better in the COVID-19 business interruption coverage litigation than those in the U.K. Although jury trials are not available in the U.K. for civil actions, there are plaintiff-oriented judges(just as there are plaintiff-oriented jurors), and many of the societal aspects driving social inflation can influence judges as well as jurors.

There are two prongs of social inflation. The first involves abuses in the tort system, which impact both corporate policyholders and insurers. Corporate policyholders feel the effects insofar as they are subjected to large verdicts and defense costs for which they are self-insured and, to some extent, in the form of higher costs of doing business (including insurance premiums). Insofar as insurers are required to provide a defense and/or indemnify under policies issued to businesses and other entities, the impact of social inflation directed at their policyholders is also visited upon insurers. Accordingly, as to this component of social inflation the interests of corporate policyholders and insurers generally are aligned.

Many of the means to controlling this prong of social inflation—such as damage limitations, tort reform, requiring full disclosure of litigationfunding, and dialing down the abuses in the tort system—often are best achieved through cooperative efforts of the defense bar, businesses, and insurers.

Insurers, however, face a second prong of social inflation aimed directly at them. This prong includes such things as: expansive reading of policy coverages and rulings by courts in coverage litigation, shifting of policyholder attorney fees in coverage litigation, increasing bad faith liability and extracontractual damage awards, use of time-limited demands, independent counsel fees, efforts to hold adjusters personally liable, and some legislative and regulatory pronouncements impacting insurers specifically. With respect to this component of social inflation, the interests of corporate policyholders and insurers often diverge. For a discussion of this prong of social inflation, *see* Scott M. Seaman & Jason R. Schulze, Allocation Of Losses In Complex Insurance Coverage Claims (11th Ed. Thomson Reuters 2023) at Chapter 19.

II. The Costs of Social Inflation

"Approximately 40 million lawsuits are filed every year in the U.S., making it the country with the largest number recorded each year. Over the last few years, businesses have been hit with numerous nuclear verdicts (verdicts that surpass $10 million) and have faced increasing costs for defending claims. According to Statista, large U.S. companies spent $22.8 billion in 2020 due to litigation." "Global Trends and Politics Legal System Abuse is Rampant What Insurers Can Do and How Reinsurers Can Help" Munich Re (November 16, 2022), available at https://www.munichre.com/topics-online/en/economy/global-trends-and-politics/legal-system-abuse-is-rampant-what-insurers-can-do-and-how-reinsurers-can-help.html

The costs of social inflation are reflected in increases in defense costs, settlements, and verdicts. In November 2022, the U.S. Chamber of Commerce Institute for Legal Reform published a comprehensive empirical analysis examining tort costs of social inflation in America. U.S. Chamber of Commerce Inst. for Legal Reform, Tort Costs in America: An Empirical Analysis of Costs and Compensation of the U.S. Tort System (Nov. 2022), available at https://instituteforlegalreform.com/wp-content/uploads/2022/11/Tort-Costs-in-America-An-Empirical-Assessment-of-Costs-and-Compensation-of-the-U.S.-Tort-System.pdf. This report examines the costs of our civil tort system and social inflation.

The entire report is worth reading, but the report's key conclusions are:

> We find that in 2020 (the latest year for which full data is available), tort costs amounted to $443 billion, or 2.1 percent of U.S. gross domestic product (GDP). These tort costs include: $229 billion in general and commercial liabilities, which cover a broad range of personal injury, consumer, and other claims; $196.5 billion in automobile accident claims; and $17.5 billion in medical liability claims. . . .
>
> To provide comparative context, we extend our analysis from 2020 back to 2016 and explore the development of tort costs throughout that period. Overall, the direct economic costs of the tort system have grown at an annual rate of six percent a year over the period 2016 to 2020, with commercial liability growing at a faster rate than personal or medical professional liability. This rate exceeds both the growth in inflation, which averaged 1.9 percent, and GDP, which grew at 2.8 percent over the same period. Because growth in the tort system has outpaced GDP, tort costs as a percentage of GDP grew from 1.88 percent to 2.13 percent. This result has been exacerbated by the contraction in GDP in 2020 caused by COVID-related shutdowns, but even through 2019 tort costs grew at a faster rate than GDP. . . .

> We estimate that U.S. tort costs in 2020 equate to $3,621 per household ..... [T]his per-household figure has grown consistently since 2016. . . .
>
> The results reveal significant variations across states ..... Florida has the highest tort costs as a percentage of state GDP (3.6 percent), while Nebraska, New Hampshire and South Dakota have among the lowest (less than 1.5 percent). Tort system costs per household are about $2,000 in states such as Maine, New Hampshire, South Dakota, and West Virginia, but over $4,500 in states such as California, Florida, and New Jersey, and as high as $5,408 in New York. . . .
>
> Finally, we estimate that the tort system is relatively inefficient at delivering compensation to claimants. Compensation to claimants only represents 53 percent of the total size of the tort system, while the remaining 47 percent covers litigation costs and other expenses. . . .

Id. at 2–4. Further, the report indicates, "for every dollar paid in compensation to claimants, 88 cents were paid in legal and other costs." *Id*. at 8. The report details the methodology used and provides interesting break-outs by tort category and state. The take-a-way is clear—social inflation has a definite and substantial cost.

The Consumer Price Index (CPI) "rose 10.5% from 2017 through 2021, while property and casualty industry general liability incurred losses have skyrocketed more than 57% during this same period." "Civil Justice Reform Gains Steam At Lawsuit Abuse Summit" (Nov. 17, 2022), available at: https://insights.zurichna.com/Civil-justice-reform-gains-steam-at-lawsuit-abuse-summit

A study released earlier this year by the Insurance Information Institute and the Casualty Actuarial Society estimates that commercial auto insurers cumulatively paid out $20 billion more (or approximately 14 percent more) on liability claims between 2010 and 2019 than would otherwise have been expected because of social inflation-related factors. J. Lynch and D. Moore, "Social Inflation and Loss Development" (Casualty Actuarial Society and Insurance Information Institute 2022).

Advisen found that, from 2015 to 2020, the median cost of a jury award over $10 million increased by 35 percent from $20 million to $27 million. It also found that the number of cases with verdicts over $20 million rose from 89 in 2017 to 102 in 2019. "In The Know: Social Inflation and the Increasing Costs of Large Jury Awards (Oct. 7, 2021), available at: https://www.vgminsurance.com/blog/post/in-the-know-social-inflation-and-the-increasing-cost-of-large-jury-awards

This author has been addressing social inflation, the factors driving it, and the steps insurers, policyholders, and their counsel should take to contain social information. *See, e.g.*, Scott Seaman, *et al.*, "*The Legal Trends Behind "Social Inflation" In Insurance,"* LAW360 (Feb. 21, 2021), available at https://www.law360.com/articles/1245725/the-legal-trends-behind-social-inflation-in- insurance; Scott M. Seaman & Jason R. Schulze, Allocation of Losses in Complex Insurance Coverage Claims (11th Ed. Thomson Reuters 2023) at Chapter 19; Scott M. Seaman & Sarah Anderson, *Key U.S. Insurance Decisions, Trends, & Developments: ESG, Social Inflation, COVID-19, Cyber/Privacy, Civil Unrest, Opioids, Lead, Sexual Assault & Other Perils Figure Prominently*, Mealey's Litigation Report: Cyber Tech & E-Commerce, Vol. 23, No. 11 (Jan. 2022).

Some social inflation is inherent in the structure of the U.S. civil justice system, but there are societal trends and developments driving it to new levels.

III. Social Inflation Is Endemic in the U.S. Civil Justice System

A myriad of underpinnings in the United States civil justice system make it rife for social inflation. These include:

- an organized, well-funded plaintiffs' bar;
- the availability of punitive/exemplary damage awards for some claims;
- the availability of juries in civil actions;
- class actions (which foster litigation that would not or could not be brought economically as individual cases) and multidistrict litigation;
- securities and shareholder derivative litigation excesses;
- extensive pretrial discovery and disclosures (including interrogatories, document requests, requests for admission, physical and medical examinations, depositions of fact witnesses, corporate representative witnesses, and experts witnesses) and abuses of the discovery process;
- the use of contingent fees in bodily injury cases;
- the American Rule on attorney fees, which generally works against corporate defendants;
- use of junk science and lax evidentiary standards, including insufficient scrutiny of expert witnesses testimony;
- fee-shifting statutes that, when applicable, usually benefit policyholders and some underlying claimants;
- doctrines such as *res judicata* and collateral estoppel that generally work against corporate defendants and insurers; and
- the availability of alternative fora to plaintiffs, carpetbagging, and forum shopping.

These realities have necessitated protracted battles for tort reform waged on many fronts. Although some meaningful tort reform measures have improved affairs in some jurisdictions and in some respects, they have not had a meaningful impact in other jurisdictions. Challenges have been presented by plaintiff-oriented legislatures. Even where tort reform has passed, sometimes—as in the state of Illinois—state supreme courts have struck down provisions based on state constitutional grounds. Suffice it to say, tort reform has not been a panacea. At least from the perspectives of defendants and insurers, the civil justice system remains highly flawed.

In the current environment, social inflation appears to be on steroids.

IV. Societal Trends and Developments Fueling Social Inflation

Apart from the mixed success and erosion of tort reform, there are several factors in modern society and developments impacting litigation that are fueling social inflation in the United States.

A. Litigation Funding

The use and surge of litigation funding in recent years has been a boon for plaintiffs' counsel. Litigation funding has increased the volume of cases that are being pursued. It has enhanced the ability of plaintiffs to take cases further and pursue larger recoveries — extending the litigation timeline, increasing the costs of defense, and increasing the potential for larger verdicts and settlements. Specifically, it has enabled plaintiffs to invest in experts, research, studies, and other weapons to deploy against defendants. Because of the larger awards associated with compelling cases, litigation funders can justify a greater investment of funds, thus allowing creative plaintiffs' lawyers to run wild in civil tort litigation. Not only are compelling cases likely to result in larger awards, but the disposition costs of mediocre cases have also increased as plaintiffs' lawyers invoke cost-intensive discovery. With the proliferation of nuclear verdicts discussed below, funders understandably view litigation funding as a good investment. Although litigation funding generally covers attorney's fees and costs, it has broader uses, including providing operating capital for business parties during litigation.

A report by Swiss Re Institute highlights the impact of litigation funding:

> The US is the centre of the world's third-party litigation finance (TPLF) industry, in which investors such as hedge funds and family offices finance legal action against companies. More than half of the USD 17 billion investment into litigation funding globally in 2020 was deployed in the US. Litigation funding companies (LFCs) invest in consumer and commercial litigation by funding legal action in return for a percentage of a successful claim sum.
>
> We see TPLF as a contributing factor to the trend of social inflation in the US. US general liability and commercial auto lawsuit data show a strong rise in the frequency of multi-million-dollar claims over the past decade. LFCs back claims in many of these areas, such as trucking accidents, bodily injury, product liability mass tort, medical liability claims etc. We find TPLF contributes to social inflation by incentivising litigants to initiate and prolong lawsuits. Higher claims costs drive up insurance premiums, can reduce the availability of liability cover, and lead to higher uninsured legal liability risks for US businesses. US casualty insurers have incurred many years of underwriting losses linked to outsize legal awards[.]

Thomas Holzheu, et al., "US litigation funding and social inflation: the rising costs of legal liability", SwissRe Institute (Dec. 9, 2021), available at https://www.swissre.com/institute/research/topics-and-risk- dialogues/casualty-risk/us-litigation-funding-social-inflation.html.

Litigation funding was once widely prohibited by the legal doctrine of "champerty" or "maintenance," which generally barred strangers to a lawsuit from funding litigation fees and costs in exchange for a financial interest in the outcome of the case. Litigation funding has gained traction as many states have abandoned or substantially limited their anti-champerty laws over the past two decades. Reform directed at litigation funding must be sought in a comprehensive basis. Some advocate for the return of anti-champerty laws,but that ship is unlikely to return to harbor.

Some states have enacted legislation addressing litigation funding. For example, Illinois enacted the Consumer Legal Funding Act, effective May 2022, 815 ILL. Comp. Stat. 121/1, *et seq*. The Illinois act includes licensing and contractual requirements, limitations on consumer legal funding fees, preclusions against funder control of litigation and settlement decisions, and disclosure and acknowledgment requirements. The act prohibits a litigation funder from certain activities, such as lawyer and medical provider referrals or referral fees and limits the amount of funding (generally $100,000). The act does not

contain any provision requiring disclosure of the legal funding agreement or information to courts or opposing counsel. Instead, it provides that disclosure of information to the funder does not waive or abrogate the attorney-client privilege or work product doctrine. Other states, such as Arkansas, Indiana, Maine, Nebraska, Nevada, Ohio, Oklahoma, Tennessee, Vermont, and West Virginia, have required registration or licensure, imposed disclosure requirements, and/or regulated interest rates or fees.

The main focus of the defense bar has been to seek requirements of disclosure of third-party funding. Court decisions on disclosure have been mixed with some courts denying discovery of litigating funding information as being irrelevant. Other courts, such as federal district courts in New Jersey and Delaware, have issued orders or rules requiring disclosure of litigation funding. *See* United States District Court for the District of New Jersey, Order (June 21, 2021), available at https://www.njd.uscourts.gov/sites/njd/files/Order7.1.1%28signed%29.pdf (amending Local Civil Rule 7.1.1 on the Disclosure of Third-Party Litigation Funding); United States District Court for the District of Delaware, Standing Order Regarding Third-Party Litigation Funding Arrangements (Apr. 18, 2022), available at https://www.ded.uscourts.gov/sites/ded/files/Standing%20Order%20Regarding%20Third-Party%20Litigation%20Funding.pdf.

Courts have reached different conclusions as to whether such materials are subject to attorney work product protection or the attorney-client privilege. *Compare Fulton v. Foley*, No. 17-CV-8696, at *4. (N.D. Ill. Dec. 5, 2019) (holding materials are protected by work product), *with Miller UK Ltd. v. Caterpillar, Inc.*, 17 F. Supp. 3d 711, 740-741 (N.D. Ill. 2014) (holding materials disclosed to third-party funders in the absence of a confidentiality agreement are not subject to the attorney-client privilege or work product protection). Disclosure should be required as an important first step, but disclosure itself may prove to be inadequate.

Whatever role litigation funding may have in some types of litigation, it presents particular dangers in personal injury litigation where plaintiffs' counsel handle matters on a contingency fee basis. Although contingent fees allow plaintiffs to pursue litigation without bearing the financial risks, at least in the absence of litigation funding, plaintiffs' counsel presumably had some incentive to avoid taking meritless cases in which recovery was unlikely. Litigation funding reduces that risk and is a significant driver of social inflation.

B. Hamstrung Defense

Unfortunately, while plaintiffs are investing in achieving bigger verdicts and settlements, many corporate defendants and insurers have relinquished to plaintiffs the traditional budgetary and leverage advantages that they enjoyed historically by what appears, at times, to be a myopic focus on limiting defense expenditures. The need to control costs and ensure expenses are reasonable is undeniable. But perhaps the pendulum has swung too far, and too much attention has been focused on attorney hourly rates, legal bills, fee audits, and appeals. This focus appears to have come at the expense of devoting the money and efforts needed to contain swelling indemnity numbers and discourage future litigation.

The impact is not simply short-term. Concerns have been expressed about the ability of defense firms to compete against plaintiff firms and other corporate practice areas for top legal talent. Millennial and Generation Z attorneys appear to be less receptive to being tied to tracking billable hours, complying with litigation and billing guidelines, responding to audits, and "paying their dues" for advancement in law firms than prior generations of attorneys.

According to one commentator, the excessive focus by some claim departments on legal spending combined with a "dose of complacency" have helped the plaintiff's bar forge ahead and left defense counsel scrambling to play catch-up. J. Theodorou, "The Scourge of Social Inflation" (Dec. 2021), available at https://www.rstreet.org/wp-content/uploads/2021/12/RSTREET247.pdf

One senior claims executive put it this way:

> One thing that has hampered the insurance industry is its historical focus on controlling legal spend and defense costs. That's a prudent and practical strategy, but at times, it seems quite "penny wise pound foolish,"..... I think carriers need to recognize the necessity for appropriate investments in litigation that [are critical for] properly preparing their cases. It comes down to getting a better understanding of the psychology behind what's driving the plaintiffs' bar and their trial strategies or tactics, and also better preparing defense witnesses for where the plaintiff attorneys will likely try and take them.
>
> We are strong advocates of mock jury exercises and trying to understand earlier on in the lifecycle of a case how the defense's [arguments] might resonate with the average lay person. That exercise will require some upfront expense, but it will enable [insurers/defendants] to recognize what they're up against at an earlier point in time, and how well their defense arguments and witnesses will resonate with a jury. Then they can pivot, if necessary, to use differing tactics or explore settlement at an earlier point in the case and prior to allowing a jury to price the case.

Bethan Moorcraft, "*The impact of social inflation on commercial liability claims*," Insurance Business America (April 20, 2022) (quoting Michael Frantz, senior vice president and head of claims at Munich Re U.S), available at https://www.insurancebusinessmag.com/us/news/specialty- insurance/the-impact-of-social-inflation-on-commercial-liability-claims-403103.aspx.

C. Keeping Up With the Times

The plaintiffs' bar has adapted to the changing demographics of jurors and judges. Key among the changing juror demographics is the increasing number of millennials and Generation Z jurors in the jury pool."Reptile theory" employed by plaintiffs, discussed further below, has particular appeal to the values, approach, and mindset of these younger jurors—though studies are mixed as to whether they are more likely to actually render nuclear verdicts. It appears younger jurors do not value money in the same way as baby boomers.

Though defendants and their counsel are doing a better job, sometimes they have not adequately defended against reptilian tactics and have failed to mount a compelling defense. Magna Legal Services reported that 84 percent of over 3,500 prospective jurors surveyed around the country over the 18 months prior to its report agreed that juries needed "to be 'guardians of the community' by forcing companies to change bad behavior with large damage awards." *Online Jury Research: COVID's Effect on Juror Perspectives & Damages*, Magna Legal Services (Apr. 8, 2021), available at https://magnals.com/covid-effect-on-damages/. In addition, 37.6 percent of juror respondents strongly agreed that the *primary purpose* of damages was to punish defendants rather than compensate plaintiffs, while 44.5 percent somewhat agreed. This report is troubling. Although punishment may be a consideration in appropriate punitive damages claims, it should play no role whatsoever in our civil justice system with respect to liability or compensatory damages.

D. Attorney Advertising

Advertising has proven to be a powerful plaintiff recruitment tool. Lawyering up and the proliferation of attorney advertising—which have been around for some time—serve as potent recruiting tools for

plaintiffs' counsel, which they have employed masterfully. This has generated more and sometimes better plaintiffs. It also has created great expectations for recovery. At some hours, you cannot turn on the television without seeing an advertisement by a plaintiff's personal injury firm. Many advocate seeking to curb exploitative attorney advertising through regulation, but this may not be achievable to a significant degree. Perhaps, more public service messaging on the abuses of the tort system and its costs to consumers should be undertaken. When was the last time you saw a public service message about the danger of faulty assignment of blame or excessive jury awards?

E. Anti-Corporate, Anti-Insurer, and Anti-Institution Sentiment

Hostility toward and distrust of large companies is hardly a new development—it has been something plaintiffs' counsel have exploited for a long time. But anti-corporate sentiment has amped up in recent years due to, among other things, residuals from the Great Recession, the Occupy Wall Street movement, the #MeToo movement, and various protests.

F. Living in a Social Media World

Social media provides a platform for users to gather and organize and for negative public sentiment about companies and institutions to proliferate. It also impacts how jurors receive and use information in some profound ways. Further, it has interposed a degree of randomness in terms ofwhat does and does not resonate on social media. With the potential for massive "viral" impact, one individual's negative experience may inform millions of other individuals and reinforce anti- corporate bias or begin to instill it. With the flood of information available at one's fingertips and invisible algorithms serving up preferred types of information, users seeking social validation haveno shortage of content to reinforce their bias. 'Echo chambers' of like-minded individuals on the internet reinforce and further polarize individuals' views because there is no one representing a balanced or opposing view and little social incentive to do so.

G. Many Jurors Have Strong Political Views

Political discourse infiltrates the jurors' mindsets. In a world of "identity politics," politics play an increasingly pervasive role in how individuals define themselves, function, and view the world. Notions of socialism, social justice, wealth and income disparities, and wealth distribution that abound on the airwaves and in social media and other political discourse foster an environment that plays into the hands of plaintiffs.

H. Jurors Are Less Inclined to Follow Jury Instructions

Jurors are more inclined to render awards with less emphasis on fault, greater emphasis on company reputation and safety practices, and based upon the perceived ability of corporate defendants and their insurers to absorb losses. Millennials and Generation Z jurors appear to be more inclined to this direction. A national survey conducted by Sound Jury Consulting in 2019 found three-quarters of respondents eligible for jury service stated they would decide a case based on their personal beliefs of right or wrong if those beliefs conflicted with the law as instructed by the judge. The civil justice system places great importance on jury instructions, and the rule of law depends, in large part, upon jurors following the judge's instructions. Although "limiting instructions" have been known to be of questionable utility, the inclination to ignore court instructions on the law is very troubling and threatens the fair administration of justice.

According to the 2019 Sound Jury Consulting study, 57 percent of respondents say they would ignore a judge's instructions to avoid internet research on the case if they believe they could obtain important information. 52 percent say they would not take the time to look at the jury instructions during deliberations if they believed they understood the issues in the case. 75 percent say they would disregard the judge's instruction to ignore inadmissible testimony if they believed the testimony was important. In some states, such as New York, Washington, California, Massachusetts, and Minnesota, efforts are being considered to update pattern jury instructions. Given jurors' increasing proclivity to ignore jury instructions, it is far from clear whether additional or more specific instructions will be followed. In any event, defendants and their insurers must address concerns about jurors not following instructions—the plaintiffs' bar will not.

I. Access to Information From Sources Outside the Courtroom

The influence of social media and the information age makes it much more likely that jurors receive information outside of the courtroom. Limiting jurors' access to evidence only admitted at trial has always been a challenge. However, absent complete sequestration, it is virtually an impossible undertaking in the information age with instant access to the internet and social media. The Sound Jury Consulting Study shows that jurors are not above the lack of self-discipline permeating our society today—they often refer to outside materials.

J. The Increasing Number and Normalization of Nuclear Verdicts

The growing number of nuclear verdicts is alarming. A report from the U.S. Chamber of Commerce Institute of Legal Reform examined verdicts of $10 million and more from 2010 to 2019, and found that nuclear verdicts have increased in both amount and frequency. U.S. Chamber Of Commerce Inst. For Legal Reform, Nuclear Verdicts: Trends, Causes, and Solutions at 2 (Sept. 2022), available at https://instituteforlegalreform.com/wp-content/uploads/2022/09/NuclearVerdicts_RGB_FINAL.pdf. The median nuclear verdict increased by 27.5 percent over that period, which far outpaced inflation. *Id*. The study reported that "[p]roduct liability, auto accident, and medical liability cases comprise[d approximately] two-thirds of the reported nuclear verdicts." *Id*. at 3. Juries in state court actions produced the vast majority of nuclear verdicts. Unsurprisingly, California, Florida, New York, Texas, Pennsylvania, and Illinois formed the epicenter of 63 percent of the nuclear verdicts, while accounting for 41 percent of the United States population. *Id*. Post-pandemic, juries have rendered numerous large nuclear verdicts.

Frequent media reports of multi-million and multi-billion dollar verdicts have desensitized jurors and, to some extent, have normalized such awards. Jurors have been exposed to information regarding large jury awards long before being empaneled in the jury box.

Nuclear verdicts also implicate the second prong of social inflation aimed directly at insurers. For example, nuclear verdicts have the potential to give rise to bad faith claims against insurers, however meritless such claims may be and notwithstanding the fundamental exorbitant nature of nuclear verdicts, based upon a policyholder's motivation to divest itself of the financial burden associated with an excessive verdict.

Plaintiffs, attempting to capitalize on the atmosphere of fear perpetuated by nuclear verdicts, are increasingly utilizing time and policy limit demands to obtain a settlement above the inherent value of a case. Insurers are well-served by engaging coverage counsel to assist in evaluating and responding to such demands. Coverage counsel can: evaluate whether the demand complies with the legal requirements in the controlling jurisdiction, identify areas of non-compliance to take into account in the insurer's evaluation and response to the demand, evaluate and assist in reducing the potential for bad

faith claims, opine on and evalue of the claim and assist in evaluating defense counsel's valuation, help in proper documentation, prepare the appropriate response to the demand, and negotiate a resolution.

K. Nuclear Rulings by Courts and Nuclear Legislation

Although attention understandably has been directed at nuclear jury verdicts, there also are unwarranted and excessive rulings by judges that lead to nuclear verdicts. Also, legislative bodies sometimes produce nuclear legislation that fosters or even encourages the rendering of verdicts unfair to corporate defendants and insurers.

Unwarranted expansion of liability theories such as public nuisance (*e.g.*, the California lead paint and opioid litigation), state legislation suspending or abolishing statutes of limitation (*e.g.*, for sexual abuse and assault cases), and the abolition of or limitation on nondisclosure agreements add jet fuel to social inflation. Reviver statutes produced an onslaught of lawsuits by sexual misconduct victims against their alleged abusers and the various institutions alleged to be responsible for allowing the sexual misconduct to take place (*e.g.*, religious and educational institutions, sports teams, and social groups). There are sound reasons for statutes of limitation. Defending stale claims can be very challenging considering witness deaths, aged and infirm witnesses, faded or distorted memories, lack of surviving physical and documentary evidence, and the supercharged nature of the allegations.

The tort of public nuisance was the basis for the imposition of a $1 billion award against lead paint manufactures, which was later reduced to approximately $400 million. Coverage issues associated with the same underlying judgment were litigated in three separate coverage actions. Insurers prevailed at the trial court and on appeal in California in the *ConAgra* case based on California Insurance Code Section 533, as the insured's predecessor had actual knowledge of the harms associated with lead paint when it promoted lead paint for interior residential use. Conversely, in the *Sherwin-Williams* and *NL Industries* cases, the policyholders prevailed in the intermediate appellate courts in New York and Ohio.

Public nuisance has figured prominently in opioid litigation. A 2022 bipartisan congressional report found that the opioid epidemic costs the United States approximately $1 trillion annually. More than 3,000 state and local governmental entities have sought to recover the costs of public services associated with opioids from drug manufacturers and distributors. The $26 billion settlement a coalition of state attorneys general reached with Johnson and Johnson and three distributors in 2021 grabbed the headlines.

In what some would characterize as a nuclear judgment, a California federal judge ruled that Walgreens, a drug store chain, substantially contributed to the public nuisance in San Francisco associated with opioids. The court indicated a subsequent trial would be held to determine the extent to which Walgreens must abate the public nuisance it helped to create. The tort of public nuisance is a growing concern in some states, including California.

Illinois' Biometric Information Privacy Act has fueled litigation and given rise to damages awards far above any actual damages sustained. The $228 million jury award against BNSF will encourage additional claims.

The number and amounts of nuclear verdicts have increased since court houses have reopened for business post-pandemic.

L. Government Regulator and Agency Involvement in and Pursuit of Money Through the Civil Justice System

An expanding universe of government entities as plaintiffs seeking recovery on tort theories has impacted social inflation. In this environment, it is not surprising that jurors are willing to view their mission as extending beyond the case before them. Too often, governmental entities extend well beyond their role as regulator and seek to use litigation proceeds to reduce government deficits and expand their domains.

In a report discussed further below, the American Tort Reform Foundation (ATRF) pointed out that the focus of the National Association of Attorneys General (NAAG) has shifted from promoting collaboration to promoting entrepreneurial litigation. It reports that NAAG has primarily turned into an organization with the goal of suing businesses for profit. NAAG has played a significant role in mass tort litigation, including opioids and tobacco. For instance, NAAG was involved in and received $15 million from last year's McKinsey & Co. opioids settlement.

When governmental entities act in concert with the plaintiffs' bar, questions may be raised regarding their regulatory and enforcement activities, undermining the public's confidence in the agency. Improper encroachment into the civil justice system also can foster unfairness.

M. Judicial Hellholes–The Home of Nuclear Verdicts– Are Super Highways of Social Inflation

Many cases have the potential to produce nuclear verdicts, but some jurisdictions are worse than others for defendants. The most dangerous jurisdictions have earned the reputation of being "judicial hellholes." Corporate policyholders and their insurers seek to avoid judicial hellholes wherever possible, but one characteristic of a judicial hellhole is that it allows carpet-bagging plaintiffs in and will not let defendants out.

The American Tort Reform Foundation (ATRF) recently released its report "Judicial Hellholes" (2022-23), in which it identifies judicial hellholes across the country. The full report is worth reading and can be found at: https://www.judicialhellholes.org/wp-content/uploads/2022/12/ATRA_JH22_FINAL-2.pdf.

The ATRF lists Georgia, Pennsylvania (the state supreme court and Philadelphia Court of Common Pleas), California, New York, Illinois (Cook County), South Carolina (for asbestos litigation), Louisiana, and Missouri (St. Louis) as "judicial hellholes." *Id*. at 1–2. Florida's Legislature, New Jersey, and Texas' Court of Appeals for the Fifth District (Dallas) were placed on the "watch list." *Id*. at 2. "Dishonorable mentions" included: the American Law Institute's adoption of the Restatement of "Consumer Contract" Law, Madison and St. Clair Counties in Illinois (plaintiffs' lawyers preferred jurisdictions for asbestos litigation), the Montana Supreme Court ruling that an insurer waived Montana's statutory cap on damages by providing excess coverage, and a Wisconsin Appellate panel's decision affirming a judgment despite unreliable expert testimony. *Id*. at 2, 66–68.

The report answers the simple question of what makes a jurisdiction a judicial hellhole: the judges. The report explains what characteristics make jurisdictions problematic. This serves as a useful checklist for defendants and their insurers.

> What Judicial Hellholes have in common is that they systematically fail to adhere to core judicial tenets or principles of the law. They have strayed from the mission of providing legitimate victims a forum in which to seek just compensation from those whose wrongful acts caused their injuries.

Weaknesses in evidence are routinely overcome by pretrial and procedural rulings. Judges approve novel legal theories so that even plaintiffs without injuries can win awards for "damages." Class actions are certified regardless of the commonality of claims. Defendants are targeted not because they may be culpable, but because they have deep pockets and will likely settle rather than risk greater injustice in the jurisdiction's courts. Local defendants may also be named simply to keep cases out of federal courts. Extraordinary verdicts are upheld, even when they are unsupported by the evidence and may be in violation of constitutional standards. And Hellholes judges often allow cases to proceed even if the plaintiff, defendant, witnesses and events in question have no connection to the jurisdiction.

Not surprisingly, personal injury lawyers have a different name for these courts. They call them "magic jurisdictions." Personal injury lawyers are drawn like flies to these rotten jurisdictions, looking for any excuse to file lawsuits there. When Madison County, Illinois was first named the worst of the Judicial Hellholes last decade, some personal injury lawyers were reported as cheering "We're number one, we're number one."

Rulings in Judicial Hellholes often have national implications because they can: involve parties from across the country, result in excessive awards that wrongfully bankrupt businesses and destroy jobs, and leave a local judge to regulate an entire industry.

Judicial Hellholes judges hold considerable influence over the cases that appear before them. Here are some of their tricks-of-the-trade:

PRETRIAL RULINGS

Forum Shopping. Judicial Hellholes are known for being plaintiff-friendly and thus attract personal injury cases with little or no connection to the jurisdiction. Judges in these jurisdictions often refuse to stop this forum shopping.

Novel Legal Theories. Judges allow suits not supported by existing law to go forward. Instead of dismissing these suits, Hellholes judges adopt new and retroactive legal theories, which often have inappropriate national ramifications.

Discovery Abuse. Judges allow unnecessarily broad, invasive and expensive discovery requests to increase the burden of litigation on defendants. Judges also may apply discovery rules in an unbalanced manner, denying defendants their fundamental right to learn about the plaintiff's case.

Consolidation & Joinder. Judges join claims together into mass actions that do not have common facts and circumstances. In situations where there are so many plaintiffs and defendants, individual parties are deprived of their rights to have their cases fully and fairly heard by a jury.

Improper Class Action Certification. Judges certify classes without sufficiently common facts or law. These classes can confuse juries and make the cases difficult to defend. In states where class certification cannot be appealed until after a trial, improper class certification can force a company into a large, unfair settlement.

Unfair Case Scheduling. Judges schedule cases in ways that are unfair or overly burdensome. For example, judges in Judicial Hellholes sometimes schedule numerous cases against a single defendant to start on the same day or give defendants short notice before a trial begins.

DECISIONS DURING TRIAL

Uneven Application of Evidentiary Rules. Judges allow plaintiffs greater flexibility in the kinds of evidence they can introduce at trial, while rejecting evidence that might favor defendants.

Junk Science. Judges fail to ensure that scientific evidence admitted at trial is credible. Rather, they'll allow a plaintiff's lawyer to introduce "expert" testimony linking the defendant(s) to alleged injuries, even when the expert has no credibility within the scientific community.

Jury Instructions. Giving improper or slanted jury instructions is one of the most controversial, yet underreported, abuses of discretion in Judicial Hellholes.

Excessive Damages. Judges facilitate and sustain excessive pain and suffering or punitive damage awards that are influenced by prejudicial evidentiary rulings, tainted by passion or prejudice, or unsupported by the evidence.

UNREASONABLE EXPANSIONS OF LIABILITY

Private Lawsuits under Loosely-Worded Consumer Protection Statutes. The vague wording of state consumer protection laws has led some judges to allow plaintiffs to sue even when they can't demonstrate an actual financial loss that resulted from an allegedly misleading ad or practice.

Logically-Stretched Public Nuisance Claims. Similarly, the once simple concept of a "public nuisance" (e.g., an overgrown hedge obscuring a STOP sign or music that is too loud for the neighbors, night after night) has been conflated into an amorphous Super Tort for pinning liability for various societal problems on manufacturers of lawful products.

Expansion of Damages. There also has been a concerted effort to expand the scope of damages, which may hurt society as a whole, such as "hedonic" damages in personal injury claims, "loss of companionship" damages in animal injury cases, or emotional harm damages in wrongful death suits.

JUDICIAL INTEGRITY

Alliance Between State Attorneys General and Personal Injury Lawyers. Some state attorneys general routinely work hand-in-hand with personal injury lawyers, hiring them on a contingent-fee basis. Such arrangements introduce a profit motive into government law enforcement, casting a shadow over whether government action is taken for public good or private gain.

Cozy Relations. There is often excessive familiarity among jurists, personal injury lawyers, and government officials.

Id. at 79–80 (bold omitted).

N. ESG/Sustainability

This author has written extensively about environmental, social, governance (ESG) factors– sometimes called sustainability–and the profound impact on insurers and policyholders. *See, e.g.,* Scott M. Seaman & Jason R. Schulze, "Allocation of Losses in Complex Insurance Coverage Claims" (11th Ed. Thomson Reuters 2023) at Chapter 19; Scott Seaman, "*Insurers Take the Lead on ESG/Sustainability*

Initiatives,}"JD Supra (Oct. 1, 2021), available at https://www.jdsupra.com/legalnews/insurers-take-the-lead-on-esg-6954367/. ESG fuels social inflation. For instant purposes, we will make three points.

First, the "all of government" approach to ESG contributes to social inflation in a number of ways, including generating new claims and claim types (such as greenwashing claims).

Second, it is important to understand that the ESG pressures are not only being applied by external forces, but increasingly internal forces also are seeking to exact change. The reality is that millennials, and Generation Z individuals are now dominant members of the workforce and management as they replace baby boomers. The educational, experiential, methodological, and demographic differences between generations are undoubtedly having a large influence on internal decision-making. Not only have corporations adjusted to create a workplace that attracts and retains this talent, but these workers are also increasingly becoming corporate decision-makers. Thus, corporations are now becoming entities that will effect change, rather than resist change. The "great resignation" and "great attrition" following the pandemic have impacted the insurance industry workforce, making companies more responsive to employee values and providing employees with greater leverage. Simply stated, companies are not opposing ESG forces and other various factors fueling social inflation in the same way or with the same intensity as they had previously.

Third, insurers are reviewing policyholder ESG policies and performance with increasing frequency and in greater depth. Many believe that policyholders with ESG awareness have a better risk profile than those not focused on ESG or policyholders with poorly conceived ESG policies or strategies. Insurers also should recognize that, when a policyholder's ESG awareness becomes ESG activism, it could result in additional risks resulting in claims against the policyholder. Examples are securities actions and greenwashing claims with respect to the "E" of "ESG" and different constituencies and members of the same constituency may have different notions of what is proper and improper in the areas of "S" and "G."

O. COVID-19 Pandemic

Court closures and litigation delays associated with COVID-19 and governmental shutdown orders were a short-term social inflation reduction or delaying factor, as progress in cases had been hampered, and the number of verdicts had been reduced. Data released in January 2022 shows that the number of bench trials dropped by 39 percent and jury trials dropped by 64 percent in 2020. Cara Salvatore, Pandemic Put Deep Freeze On State Trials, New Data Show, Law360 (Jan. 12, 2022), available at https://www.law360.com/articles/1454943. At least some antidotal reports suggest the delay in cases moving forward has resulted in some plaintiffs' settlement demands being more reasonable. In such instances, justice delayed may actually be justice achieved. Undoubtedly the impact has been short-lived, as there has been a backlog of cases and a flurry of post-pandemic nuclear verdicts.

The COVID-19 business interruption coverage litigation has produced thousands of cases and some policyholder victories. Still, insurers have done very well to date, with most courts refusing to create an unwarranted expansion of coverage by watering down the steadfast requirement of direct physical loss or abrogating exclusions. Also, none of the bills attempting to create business interruption insurance by abrogating applicable exclusions and requirements in first-party property policies by legislative fiat have become law. For a detailed discussion of the impact of COVID-19 on social inflation, *see* S.M. Seaman & S. Anderson, "The State Of COVID-19 Coverage Litigation In The United States: Insurers Are Prevailing In Coverage Cases, But COVID-19 Still Is Contributing To Social Inflation" *Mealey's Litigation Report Catastrophic Loss, Vol. 17, #10 (July 2022).*

V. The Dangerous Double Barrel of Social Inflation Coupled With Economic Inflation

Social inflation had been raging on—with various ebbs and flows—until the court closures and delays associated with the COVID-19 pandemic provided a temporary abatement in 2020. Since emerging from pandemic-related shutdowns and court closures, insurers and their corporate policyholders have confronted something they have not encountered previously to any *significant* extent—social inflation coupled with substantial price-level inflation.

Indeed, the United States recently has experienced the highest price level inflation in more than 40 years. On July 13, 2022, the U.S. Department of Labor reported that consumer prices increased 9.1 percent compared with a year earlier, representing the largest yearly increase since 1981. The next day, the U.S. Department of Labor reported that the U.S. producer price index increased 11.3 percent — 18 percent for goods and almost 8 percent for services. Paul Wiseman, *Wholesale inflation in June surged 11.3% from a year ago*, AP News (July 14, 2022), available at https://apnews.com/article/inflation-wholesale-prices-surge-b24934f32f965f43c9ebb888a730543c. Although price level inflation has slowed, it is clear that earlier reports claiming that price level inflation was transient have turned out to be inaccurate. To make the times more challenging, many economists believe the United States' economy is teetering on the edge of "stagflation" or recession, or may already be there.

A. Price Level Inflation Is Likely to Fuel Additional Social Inflation

All other things being equal, price level inflation increases the costs of defending cases, increases settlement values, and produces higher jury verdicts. As Julian James, Sompo International's CEO of EMEA, recently pointed out:

> Looking at the economy, we're entering a period of high inflation and if we think about what that means, it means the cost of claims is going to increase, it means the cost of rebuilding basic things is going to increase, and it means that companies themselves are going to have to weather the impact of those inflationary demands.

Sompo Intl's James: Aggregation of systemic risks and inflation present ongoing challenges for industry, The Insurer (June 7, 2022), available at https://www.theinsurer.com/leading-voices/sompo-intls-james-aggregation-of-systemic-risks-and-inflation-present-ongoing-challenges-for-indus/. James also noted the impact inflation will have on insurers themselves in terms of their reserves, assets, solvency requirements, and capitalization in times of high inflation.

Supply chain constraints have produced shortages of lumber and other building materials, driving up the costs of property repairs. Shortages of microchips have also increased the costs to build and repair the property and other goods that incorporate chips. The Medical Consumer Price Index has outpaced the overall Consumer Price Index, and medical costs for injured plaintiffs influence liability insurance losses. Although recent advances in medical treatments for trauma victims (such as skin grafts for burn victims, robotic exoskeletons, and advanced prosthetics) have extended longevity and improved patients' quality of life, they have also been known to increase the cost of care. Shortages impose a reduction in supply and put upward pressure on prices. Shortages of numerous items such as baby formula, food items, and other consumer and producer goods have been widely reported. In addition, some insurance policies, by their express terms, increase limits based upon increases in price levels.

There likely is a synergistic effect between many of the factors driving social inflation and price level inflation. For example, an inflationary environment likely will increase nuclear verdicts and create jurors' expectations of large and continuing price increases, which can be expected to be factored into their awards. As previously noted, media reports of multi-million and multi-billion dollar verdicts have desensitized jurors and, to some extent, have normalized large awards. Similarly, media reports of significant price increases likely will result in even larger verdicts to account for jurors' inflationary expectations.

Many economists subscribe to John Maynard Keyes' view that some wages and prices are "sticky" downwards, meaning that prices increase quickly when demand is increasing, but decrease slowly when demand is decreasing. *See generally,* The General Theory of Employment Interest and Money (Houghton Mifflin Harcourt 2016). It is not unreasonable to believe that jury verdicts will rise quickly to keep up with and even outpace inflation. A surge in defense costs, settlement values, and jury verdicts may result from the combination of price inflation and social inflation. One may suggest that social inflation is "sticky downwards" in line with Keynesian economics.

B. High Inflation Increases the Costs of Claims

The most direct effect of high inflation on insurance is upward pressure on claims verdicts and settlements, potentially leading to losses beyond those contemplated by insurers when issuing policies and setting premiums.

Greater precision will be required to account for inflation in connection with reserving and pricing, as elevated price levels increase the stakes of accurately accounting for the impact of inflation. It is likely more complicated than simply plugging in a new number for the inflation rate or the proper discount rate.

Inflation can impact claims frequency and severity. The rising cost of claims can erode underwriting profits in the current year and increase liability through reserve or INBR deterioration. Inflationary concerns—both price level and social inflation—require careful scrutiny to ensure the adequacy of reserves. Proactive claims evaluation and resolution are imperative.

Inflation impacts each line of insurance differently. Property insurers and aviation insurers, for example, have to pay attention to the accuracy of declared values. There can be a large delta between declared values and replacement costs attributable to inflation.

Inflation will increase defense costs and, as such, presents particular concern for lines of insurance that contain defense obligations. Directors and officers liability, professional indemnity, auto, and general liability policies, for example, are particularly susceptible to inflationary pressures through rising legal defense costs as well as higher settlement values and nuclear verdicts.

Law firms are required to increase rates to attract and retain the caliber of attorneys needed to provide the expected level of service to clients. Similarly, internal law departments are required to pay more for legal talent in this highly competitive and mobile market. Top legal talent and even mediocre talent is more expensive in the current market. Simply stated, the costs of defense may continue to rise.

C. Underwriting Pressures Associated With Price Level Inflation

On the underwriting side, inflation likely will impose upward pressure on premiums. This is particularly true as risks and uncertainties make policyholders unlikely to self-insure.

Insurers likely will be called upon to examine contract language and evaluate whether changes in contract language are warranted, or whether the terms of coverage otherwise should be changed to account for

inflation. High inflation may alter the volume mix of policy types issued by an insurer and impact the industries or individual policyholders an insurer is willing to underwrite.

Increases in the costs of reinsurance cannot be ignored. Inflation may impact the type of reinsurance cover to secure as well as reinsurance pricing and availability. Some suggest that excess of loss cover may limit exposure to significant inflation in terms of an increase in claims severity. Others point out that aggregate covers can more effectively manage inflation associated with claims frequency.

D. Price Level Inflation Impacts Other Insurer Operations

High price level inflation impacts other aspects of insurer operations and activities. Inflation may result in real and even nominal reductions in investment income and may impact the availability and cost of capital. Elevated price inflation will likely impact insurers' investment strategies and investment portfolios.

Insurers—like many other companies—are facing challenges in retaining a vibrant workforce. Insurers have experienced difficulties in attracting millennials and younger workers to join the insurance industry workforce. These dynamics present a problem given the number of people expected to retire near term. Doug Bailey, *Inflation Hitting The Insurance Industry With No Letup In Sight*, Insurance Newsnet (May 5, 2022), available at https://insurancenewsnet.com/innarticle/inflation-hitting-the-insurance-industry-with-no-letup-in-sight. Rising gross wages and shrinking net wages may exasperate these issues and fuel additional turnover and position vacancies.

E. The Emergence of Greenflation

With the recent intense focus on ESG/sustainability, insurers and their corporate policyholders are now looking down a "triple barrel" of social inflation, price level inflation, and greenflation. The "E" or environmental component of ESG has several facets, perhaps the most significant of which is the effort to reduce greenhouse gas emissions and reach carbon neutrality.

Greenflation reflects the increasing costs associated with "transitioning" to a green economy and striving to reach carbon neutrality. Many believe that greenflation, like price level inflation, will be neither insignificant nor transitory. In actuality, greenflation is not an additional form of inflation, but a component of price-level inflation. In other words, the increasing costs of energy and the resulting increases in the costs of many products are significant components of price-level inflation. Since greenflation is a term gaining traction and in view of the focus on ESG, it is worth highlighting.

There are benefits associated with "E," but greenflation represents a cost. Some argue that greenflation may or should cause a rethinking or slowing down of the energy transition, but there remains strong commitment by the Biden administration and many sectors of the economy to reduce the carbon blueprint. With the Biden administration's "all of government" approach to ESG, and Europe continuing to focus on ESG, it is unlikely that greenflation will end or slow anytime soon.

According to an article published by Beasley, 42 percent of companies in the United States rated inflation as their biggest concern, compared to 33 percent of business leaders in the U.K. Moreover, 65 percent of U.S. business leaders (55 percent globally) believe they are not prepared to meet the challenge of inflation. *Inflation worries businesses – and their insurers*, Beazley.com (July 18, 2022), available at https://www.beazley.com/en-us/articles/inflation-worries-businesses-and-their-insurers. It appears that price-level inflation—like social inflation and greenflation—will continue to present challenges to insurers.

Part 2: Countering and Controlling Social Inflation

The impact of social inflation has been felt across multiple lines of coverage, including commercial auto, medical malpractice and professional liability coverages, primary, umbrella and excess general liability coverage, and directors and officers liability coverage. *See* Bethan Moorcraft, What is social inflation, and why is it hurting insurance?, Insurance Business America (Jan. 3, 2020), available at https://www.insurancebusinessmag.com/us/news/breaking-news/what-is-social-inflation-and-why-is-it-hurting-insurance-195626.aspx.

Insurance plays a vital role in the economy—fostering entrepreneurial risk-taking, research, product development, the availability of goods and services, and risk sharing. The unavailability of insurance would bring the economy to a halt. Yet, this critical sector of the economy constantly is under siege from claimants, policyholders, courts, governmental regulators, and media.

I. Employing the Talents of Insurance Professionals to Contain Social Inflation

Fortunately, insurers endeavor to employ bright and talented people who find ways to meet the challenges presented. Insurers have several tools to address social inflation. On the underwriting side insurers may: assess and better quantify the risks, raise premiums to account for the risks, lower limits, include sub-limits (where appropriate), draft policies with appropriate terms, conditions, and exclusions to contain the risks, exercise underwriting discipline, employ artificial intelligence and technology, identify macro-factors that can influence underwriting strategy and exploring new and non-traditional data sources such as economic, public, and proprietary data.

Insurers are recognizing that social inflation is a multifaceted problem that requires the expertise of claims, legal, underwriting, actuarial, data analytics, loss control, and marketing to understand and formulate appropriate responses. Social inflation is dynamic and requires continual attention.

On the claims side, artificial intelligence, data, and technology can also be employed. Earlier and better use of mock juries and jury research can help in valuing cases, evaluating potential outcomes, selecting jurors, and formulating arguments and strategies to counter or neutralize applicable social inflation factors in the courtroom**.** When employing mock juries, it is important to consider appropriate variables and make sure that the realities of the jurisdiction are taken into account, as well as fairly portraying the evidence and arguments likely to be adduced by plaintiffs. Care must be used to ensure that views and beliefs of defense counsel do not undermine or bias the results. There are several options that can be used in addition to or in lieu of full mock jury trials, such as focus groups, shadow juries, surveys, and polls to test themes, arguments, and evidence and to create successful narratives and counternarratives for trial.

Insurers are relying upon an expanding scope of data to include current and historical activity by examining internet activity and social media trends that shed light on behavioral activity. Insurers are often well-served by involving coverage counsel to: address social inflation drivers such as policy limit demands and bad faith risks, evaluate the impact of covered versus non-covered claims, and identify issues and protect the interests of the insurer throughout the pendency of the litigation.

Prompt and accurate claims and case evaluation by claims examiners and counsel is critical. The practice of some attorneys to maintain that a claim is lacking in merit or fully defensible for months or years only to advocate paying large settlement amounts or caving late in a case is always troubling. Still, it is

particularly dangerous in times of social inflation. It is important to encourage a culture of no surprises and candid evaluation and to avoid adopting a kill-the-messenger mentality.

On both the claims and underwriting sides, training personnel and retaining skilled counsel and experts remain important. Internal communication plays a pivotal role in quickly identifying social inflation factors and formulating strategies to address them. Policyholders similarly employ bright and talented people to evaluate their exposures, limit or eliminate them, and work on strategies to minimize exposures. Insurers will continue to work with policyholders to employ cogent loss control, safety, and best practices to avoid and limit liability even in an environment supercharged with social inflation.

Educating policyholders and seeking ways for insurers and policyholders to work together in identifying and responding to social inflation can be helpful. Insurers are emphasizing active safety and quality control programs and loss control.

Insurers and defense organizations have created and participated in seminars and training programs to promote awareness of social inflation and to develop ways to combat it. For example, DRI's Center for Law and Public Policy recently created a social inflation task force.

In terms of the reinsurance market, the general wisdom appears to be that, all other things being equal, social inflation causes reinsurers to have a greater affinity for reinsuring commercial risks on a proportional as opposed to non-proportional basis.

II. The Continual Pursuit and Battle for Tort Reform

Insurers, corporate defendants, and their advocates must continually seek tort or legislative reform to limit various aspects of social inflation and curb litigation abuses.

A couple of examples of recent, meaningful tort reform are worth noting. The first is a commercial auto tort reform bill (H.R. 19) passed in Texas effective September 1, 2021, aimed at curbing reptile theory and other abuses in commercial vehicle cases. *See* Tex. Civ. Prac. & Rem. Code Ann. §§ 72.001, *et seq*. (2022). The act provides, among other things, that on a defendant's motion, courts must bifurcate a trial into two phases. *Id*. at § 72.052. In the first phase, the trier of fact determines liability for the accident and compensatory damages. *Id*. If and only if the trier of fact finds the defendant driver liable can the trial proceed to consider vicarious liability against a motor carrier and exemplary damages in the second phase. The legislation limits the admissibility of evidence of a defendant's failure to comply with a regulation or standard in Phase 1 of a bifurcated action and contains other provisions. *Id*. at § 72.053.

The most recent example of meaningful reform was a property insurance reform bill signed into law on December 16, 2022 in Florida. The bill was designed to help stabilize the property insurance market. Florida Senate Bill 2-A:

- eliminates the one-way attorney fees recovery on property insurance claims that ran in favor of policyholders;
- addressed policyholder assignment of post-loss benefits abuse that has plagued the state, enhanced the Office of Insurance Regulation's ability to complete market conduct examinations of property insurers following a hurricane to hold insurance companies accountable and prevent abuse of the property appraisal process;
- reduced timelines for insurers to pay policyholders;
- specified conditions to mandatory binding arbitration; and

- committed additional funding to provide temporary reinsurance support, building upon legislation (S.B. 2-D) passed earlier in the year.

See News Release, Gov. Ron DeSantis, Governor Ron DeSantis Signs Two Bills to Support Disaster Relief and Help Stabilize Florida's Property Insurance Market (Dec. 16, 2022), available at https://www.flgov.com/2022/12/16/governor-ron-desantis-signs-two-bills-to-support-disaster-relief-and-help-stabilize-floridas-property-insurance-market/.

As discussed above, requiring disclosure of litigation funding and limiting or eliminated litigation funding also is something that should be pursued to control social inflation. There are many tort and litigation reforms needed. For an interesting list, *see generally, 101 Ways to Improve State Legal Systems A User's Guide to Promoting Fair and Effective Civil Justice,* U.S. Chamber Inst. For Legal Reform, (6th ed. Sept. 2019), available at https://instituteforlegalreform.com/wp-content/uploads/2020/10/101_Ways_to_Improve_State_Legal_Systems_A_Users_Guide_2019.pdf.

III. Defeating Reptilian Tactics and Containing Social Inflation in the Courtroom

Corporate policyholders, insurers, and their counsel—at least to some extent—hold the ability to limit nuclear verdicts and reduce social inflation in their own hands. Fundamentally, ensuring that a stable of highly qualified counsel and firms are engaged to protect and promote their interests through reasonable, competitive compensation and devoting the resources needed to adequately evaluate and defend cases—including providing for reasonable budgets, jury research, and scientific studies are fundamental requirements. Simply stated, allowing the plaintiffs' bar to possess an economic advantage is not a sustainable state of affairs.

We have written about reptilian tactics and the steps corporate policyholders, insurers, and their counsel may take to limit the effectiveness and ultimately defeat reptilian tactics employed by the plaintiffs' bar. *See*, *e.g.*, Scott M. Seaman & Jason R. Schulze, Allocation Of Losses In Complex Insurance Coverage Claims (11th ed. 2023) at Chapter 20. More broadly, many of these efforts can help to contain social inflation.

Reptile theory is based, in large part, upon asking the jurors to consider their interests in safety, the interests of society in safety, and to be the conscience of society. In its early years, reptile theory provided plaintiffs' counsel with the advantage of surprise. Defendants were caught off guard and sometimes even unaware of its use at first. Once defendants caught on to the use of reptile theory, there was still a delay in effectively responding to the tactics. The defense bar appears to have caught up with and become more adept at countering reptile theory. Remarkably, many judges were unaware that reptilian tactics were being unleashed in their courtrooms for a long time, and some judges still may not be fully cognizant of reptile theory. Accordingly, exposing the strategy and educating courts about the impropriety of reptilian tactics remain important functions for defense counsel.

There is no one-size-fits-all solution to limit reptilian tactics or social inflation, but there are many things defendants and their counsel can do to contain them. Defendants must identify and be prepared to address the strategy and tactics in the pretrial, discovery, and trial phases, employ the traditional tools available to defendants in civil litigation, adapt their strategies, and apply these tools to succeed.

Here are some overarching themes and strategies that defendants may deploy, as appropriate, in a particular case.

A. Prompt Case Evaluation

Prompt case evaluation and early identification of cases with high nuclear verdict potential are more critical activities than ever. Early settlements of such cases on terms acceptable to defendants and their insurers, where achievable, often provide the most cost-effective resolution—even though the wisdom of such settlements may not be fully appreciated because the verdict alternative will never be known and because the parties move on to other cases and claims. Strive to put a dollar value on a case or claim early and revisit it as the matter evolves. Proper "post-mortem" analysis of other cases involving nuclear verdicts may also yield a better understanding of them.

B. Take Appropriate Actions to Keep Out Inflammatory Evidence

The best way to defeat reptilian tactics is not to allow them into the courtroom. Motions to dismiss, motions to strike, motions *in limine*, objections to discovery, and motions for protective orders provide vehicles to limit the scope of discovery and evidence to the particular issues and incidents at issue in the case. They also foreclose or limit discovery on extraneous issues. During discovery, counsel may also object to reptile theory based discovery, prepare deposition witnesses for questions designed to further the plaintiff's use of reptile theory based tactics, and educate the court through briefs along the way so a judge will be aware of reptile theory by the time motions *in limine* are filed before a trial. To the extent a court nonetheless allows this type of evidence, a defendant can decide what affirmative or rebuttal evidence it wishes to adduce to counter the reptile theory-based evidence.

It is worth elaborating on the importance of filing motions *in limine* and zealously pursuing to exclude improper arguments, evidence, and anticipated misconduct by plaintiff's counsel in advance of trial. Motions *in limine* have the advantage of educating the judge and making arguments outside the presence of the jurors. Obtaining rulings will also assist defendants in preparing for trial and marshalling evidence to counter the reptilian theory to the extent it is allowed to enter the courtroom.

Delayed or deferred rulings usually are friends of plaintiffs' counsel because they open the door for plaintiffs to adduce evidence—recognizing it may be more difficult for defendants to make a full argument and less likely that a court may give full consideration to such arguments during the heat of trial with a jury empaneled.

Plaintiffs generally are not concerned with limiting instructions, as they know such instructions are not a panacea for venom already injected in jurors' minds. Also, courts and defendants may be more hesitant to interpose objections or interrupt arguments at trial before the jury.

Additionally, avoiding *in limine* rulings increases the chances that a plaintiff will be able to prevail on an appeal of a verdict that is the product of reptilian tactics based upon a defendant's failure to properly preserve an issue for appeal, notions of broad latitude at trial, and application of the harmless error doctrine. Some lost motions may be attributable to failing to educate the court on what reptile theory is or precisely explain what evidence or types of evidence should be excluded and why their admission would be improper. Generally, the more specific and detailed the motion, the more likely it is to be successful. Counsel with awareness and repeated experience with countering reptile theory-based tactics and strategy is invaluable.

C. Defendants Can Adduce Evidence to Activate the Reptile in Jurors

It is important to remember that defendants also can use reptile theory-based tactics in favor of the defense. Fear and survival instincts—particularly those of so-called "defense jurors"—can be triggered in ways favorable to the defense. For example, fears associated with lawsuits and large awards, such as undermining the quality and availability of health care, may be deployed in a medical malpractice action. In other cases, pointing out the harms of large awards on the economy, in terms of costing people jobs, increasing prices, and suppressing the introduction and development of products and services may be a beneficial approach.

D. Emphasize the Importance of Following the Law and Evidence

If the court improperly allows the plaintiff to argue the role of jurors in keeping society safe, be prepared to explain to jurors what their proper role is, the importance of jurors being objective triers of fact based upon the specific evidence in the case before them, and the harm to society that would emerge from jurors stepping outside their appropriate role.

Point out the societal problems that would be created by the conduct or rules advocated by plaintiffs in order to resonate with jurors. Be sure to get the defendant's theory of the case and the defense message out early and often.

Demonstrate throughout the trial that the plaintiff's reliance upon general notions of safety is nothing more than an attempt to deceive jurors and obfuscate the plaintiff's lack of evidence necessary to prove essential elements of the claim, such as failure to establish the standard of care, lack of evidence of any breach of the standard, and lack of causation and lack of damages. Jurors may not appreciate being manipulated by plaintiffs and may cause a plaintiff's plan to backfire.

Show jurors that abstract safety rules and notions of corporate responsibility are inadequate substitutes for the required proofs. Emphasize appropriate details of a case as well as the evidence. Hammer home the deception in the plaintiff's use of generalizations and oversimplification. Continually direct the focus of witnesses and jurors back to the defendant, the plaintiff, the issues in the case, and the proofs and lack of proofs in the case.

E. Humanize the Defendant

Remind jurors the defendant is compassionate and like them. It is important to humanize the company and its witnesses throughout the trial. Demonstrate the humanity of the defendant. Where appropriate, put the jurors in position to understand the attributes of the individuals and to view the actions and statements from the perspective of the individuals taking or making them. The more jurors relate to the defendant; the less susceptible jurors will be to reptilian tactics.

F. Place Jurors in the Defendant's Shoes

In the event that the court allows the plaintiff's improper use of reptilian tactics, attempt wherever possible, to have jurors place themselves in the shoes of the defendant. Show that rules of evidence, the burden of proof, meeting the burden of proof and proving elements of claims are important requirements to prevent jurors and others from being victimized.

Provoke anger or other emotions related to being falsely accused, wrongfully hauled into court, being subject to unfair or improper scrutiny, and being judged based upon generalizations or conduct of others. Distinguish between accusations and evidence, puffery and proof, and place the jurors in a position to challenge and evaluate the evidence.

It is important to present the defendant positively and project a tone of compassion and concern for safety. Speak about care demonstrated by individuals within the company. Emphasize the corporate responsibility and good corporate citizenship of the company. This should be reflected in the tone, words, and approach of the counsel and witnesses throughout the proceedings.

Where general safety rules or information on violations are admitted, counter with evidence of the defendant's systemwide safety processes, safety policies, and training regimen. Use handbooks, guidelines, signs, posters, memoranda, and other evidence demonstrating the defendant's positive actions and their concern and focus on safety. Point out the company's hiring and retention of experienced, qualified people.

Place safety rules in the appropriate context. Demonstrate that safety rules are not absolute and show why other considerations should influence actions. Show that any alleged violation was inadvertent, rare, minor or reasonable, or did not actually cause any harm. Show why the generic safety rule that plaintiffs advocate for presents dangers.

Demonstrating the defendant's conduct promotes societal interests, whether safety or otherwise, is a way to counter reptilian tactics and prevent nuclear verdicts.

G. Put the Proper Resources and Preparation Into Defending the Case

There is no substitute for having an adequate budget to prepare for trial, to test themes and theories and likely juror reactions. Use mock trials and jury research to properly value cases, develop themes, test theories, and evaluate evidence. Mock trials and juror research should be directed at damages as well as liability and defenses.

Proper preparation of witnesses for deposition and trial testimony is critical. Educate witnesses on reptile theory and prepare them to respond to reptile theory-based questions at deposition and trial. Prepare for questions that allow plaintiffs to flesh out and support the following reptile theory-based propositions: safety should always be the *top* priority; companies should not put profits over people; products should be *safe* for *all* consumers; businesses should not make or sell a product that *could* hurt people; cost should not be a factor when it comes to safety; policies and procedures are needed to *ensure* people do not get injured; a company should warn of *any* dangers with their products; and documentation must be thorough to ensure safety policies are followed.

Educating witnesses on how to properly address hypothetical questions is essential. Preparing witnesses to address the reptile theory-based questions will prevent the types of evidence the defendant seeks to exclude from existing in the first place. Remember to prepare the witnesses on the wording and tone, the content of responses, and the importance of proper demeanor.

Failure to adequately prepare creates portfolio problems for defendants that could extend beyond a particular case, including res judicata and collateral estoppel, showing an inability to try a case or vulnerability to particular arguments, claims, and jurisdictions that could add to a company's litigation burden.

H. Finger Pointing and Comparative Fault

A defendant does not necessarily have to outrun the reptile. Instead, it may often avoid the reptile's bite simply by outrunning other potential prey. Do not let reptilian tactics prevent you from focusing on the contributory negligence or comparative fault of the plaintiff or other defendants or utilizing an empty chair defense.

To defeat it, defendants must recognize reptilian tactics for what they are—an attempt by plaintiffs' counsel to circumvent traditional rules of evidence and adduce evidence and arguments that are traditionally barred. The use of traditional weapons and arguments can go a long way in defeating reptilian theory-based strategies.

I. Take Advantage of Traditional Evidentiary Rules

Remember the importance of proper jury instructions and spending time during closing arguments reviewing key jury instructions with the jurors and explaining in detail how the instructions apply to the evidence.

Further, Federal Rule of Evidence 403 and state equivalents can be effective reptile slayers. Reptile theory implicates all the countervailing considerations warranting the exclusion of even relevant evidence under Rule 403. Reptilian tactics are riddled with engendering unfair prejudice, confusing the issues, misleading the jury, interposing undue delay, and wasting time. Reptile theory also runs counter to the prohibition of Federal Rule of Evidence 404 of admitting evidence of any other crimes, wrongs, or acts to prove a defendant's character or to show that, on a particular occasion, the defendant acted in accordance with the character. Keep in mind that Rule 103(d) admonishes that, to the extent practicable, the court must conduct a jury trial so that inadmissible evidence is not suggested to the jury by any means.

The exclusion of "golden rule" arguments should apply to reptilian evidence and arguments. Reptile theory is based, in large part, upon asking the jurors to consider their interests in safety, the interests of society in safety, and to be the conscience of society. As such, reptile theory violates the almost universal prohibition against asking jurors to place themselves in the shoes of another person and/or encouraging jurors to decide the case based on their personal interests or bias.

J. Start Conditioning the Jury During *Voir Dire*

Depending upon the jurisdiction and judge, defense counsel may begin the process of conditioning the jury and exposing plaintiffs' tactics during *voir dire*. *Voir dire* should at least provide an opportunity to identify potential jurors that are reptile-friendly and to exercise peremptorily strikes and challenges for cause accordingly.

Questioning can include the traditional line of inquiry about whether or not jurors can agree to leave their personal views and experiences aside and instead follow the evidence as presented in the courtroom and the law as the trial judge will instruct them in reaching a decision. Their promises to follow the law at the beginning can be revisited in closing, along with showing that there is no place for the reptile in their decision-making.

K. Mount a Vigorous Defense on Damages

In a world of nuclear verdicts, defendants can ill afford to ignore damages. Deemphasizing damages out of concern that it will make jurors more likely to find liability can be a risky strategy. Defendants must be

aggressive in conducting discovery on damages and in challenging plaintiffs' damage proofs. Plaintiffs have been inclined to set higher damage anchors recently, even at the risk of seeming unreasonable, based on studies showing that jury awards are increased by higher damages requests and decreased by lower damages requests. In many cases, defendants may be well-served by setting out their lower damage anchors earlier and more often at trial. Defendants should remember to present fact witnesses and experts to address damages issues.

L. Keep in Mind We Are in a Post-Pandemic World

Do not forget the impact of the COVID-19 pandemic on jurors. In selecting jurors and in trying cases, defendants must keep in mind the potential impact of the pandemic and related shutdowns on jurors who may have experienced physical, psychological, or emotional injuries themselves, suffered loss from the deaths of friends or family, and had their lives altered in a variety of ways. These events could make some jurors plaintiff oriented and particularly susceptible to reptilian tactics.

These are some of the strategies defendants and their counsel can employ in the courtroom to contain social inflation and limit nuclear verdicts. Outside the courtroom, insurers and their policyholders are well-served by developing and maintaining a culture of excellence, hiring, retaining, training, and promoting outstanding talent, and insisting upon excellence.

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