US CASUALTY INSURANCE REVIEW

OCTOBER | 2022

MARKET OVERVIEW

Following three years of steady rate increases, the commercial casualty market remains firm, but the pace of rate increases is reportedly beginning to moderate to some extent. The ***Business Insurance*** **September 13, 2022, article** reports that “firm rates and capacity constraints are likely to continue...into 2023”, however, the market, while still being firm, is more stable now than in recent years. Overall, though, casualty carriers are maintaining discipline and continuing to push for pricing increases, especially on accounts with challenging risk profiles. Certain classes of risk continue to be more impacted than others, but the high volatility of the prior two years has to some extent subsided. The underlying issues driving up casualty claim severity continue to include social inflation, increasing litigation costs, and plaintiff-friendly judgments resulting in “nuclear” verdicts. Due to the pandemic and resultant shutdowns and staff shortages, the court systems are continuing to work through significant backlogs.

Increased labor, material, and associated medical costs, fueled by the rapid jump in the general economic inflation over the last year, have also become significant drivers in the continued rise of casualty claim settlements and judgments. Additionally, geopolitical threats like the current Russian and Ukrainian conflict remain long-term challenges with unknown consequences. Finally, pandemic-specific and related claims, which have the potential for developing very large claims and loss reserves, remain an important consideration, although they have not been as significant as some initially feared.

Within certain classes of business and geographies, policy language restrictions and overall tightening terms and conditions continue to be emphasized. Examples include assault and battery, sexual misconduct / molestation, residential construction, and wildfire-exposed risks. COVID-19 and communicable disease exclusions remain a high priority for insurers, and we expect that restrictive policy language and endorsement wordings will continue to be emphasized.

As reported in our last **US Casualty Market Review**, more casualty carriers have been shifting towards a growth strategy, placing a greater emphasis on account retention and achieving new business goals. This approach has allowed underwriters to reconsider their previously declined accounts and offer more favorable terms on renewals. Even with this improvement in overall market stability and certainty, we are seeing a conservative and selective underwriting approach with high-risk categories and accounts with poorer loss histories. These individual risks, along with certain challenging industry sectors, continue to exist in a casualty insurance environment with higher pricing pressure and more limited capacity offerings.

Recent renewals for umbrella and excess liability lines are also showing signs of rate increase moderation. Nonetheless, capacity constraints do remain, resulting in higher premiums and the need to place added layers to reach the requested program limits on larger risks. Several excess carriers have also raised their attachment points and retention levels, requiring restructuring on renewals. Program design strategies include adding buffer layers or stretching the primary limits to reach the higher umbrella and excess liability attachment points. In some cases, the umbrella carriers will leverage their positions to also obtain the primary coverages. Larger accounts have seen even greater rate increases and capacity constraints, in comparison to the lower or more muted adjustments occurring in the smaller commercial market. Compared to the very high volatility and excess pricing and capacity reductions from previous years, this year’s renewals have started to show some relative stability and moderation.

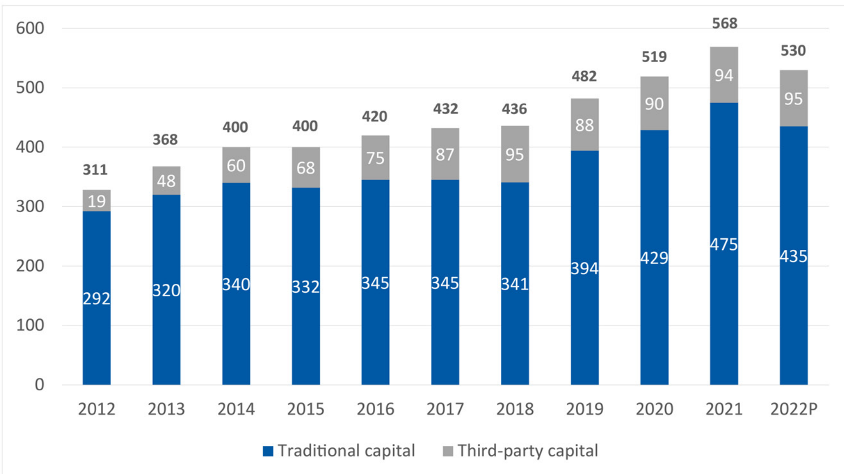
New entrants supported by both domestic and global market capacity continues to enter the market and are creating some competition. This is another contributing factor keeping the price increases in moderation and lowers the volatility as compared to 2020, 2021 and the first half of 2022. All combined, the overall casualty market is expected to continue at more moderate price increases as we move into the last quarter of 2022 and start into 2023.

CONTACT

For more information contact your local RT Casualty broker or underwriter.

FIGURE 1: GLOBAL REINSURANCE

Estimated total dedicated reinsurance capital



Source: Guy Carpenter, A.M. Best

THIRD-PARTY LITIGATION FUNDING (TPLF)

Third-party litigation funding (TPLF) continues to rise and has become a multibillion-dollar global industry. TPLF allows hedge funds and third-party financiers to invest in lawsuits in exchange for receiving a percentage of the settlements and judgments. This has become a significant concern for commercial insurers. Currently, there are limited disclosure requirements or other similar safeguards in place. Third-party funding has a direct impact on increasing the insurance carrier's defense costs and creates the potential for larger monetary settlements and litigation awards, in addition to increasing the number of frivolous lawsuits. Litigation funding is becoming a growing contributor to the social inflation issue and could potentially affect all major commercial liability lines of business.

REINSURANCE

The primary challenges affecting the overall casualty market (social inflation, plaintiff-friendly judgments / "nuclear" verdicts, and general economic inflation) are the same for the casualty reinsurance sector. The insurance treaty renewals through 2022 have been generally orderly and continue to reflect a cautious approach. Capacity remains sufficient, with deployment and price increases remaining highly dependent upon the loss experience and performance of each carrier portfolio. There has been an increased need for cedent insurers to differentiate their underwriting approaches from the others who have been impacted by poorer loss results. Tighter underlying policy terms for clash cover are required and the loss-impacted excess of loss programs remain challenging and highly scrutinized.

Strong capitalization continues to support the reinsurance market. Guy Carpenter's latest published estimates state that the total dedicated reinsurance capital continues to grow across the reinsurance market, meeting industry needs despite some reduction from 2021 to the projected 2022 figure. See Figure 1.

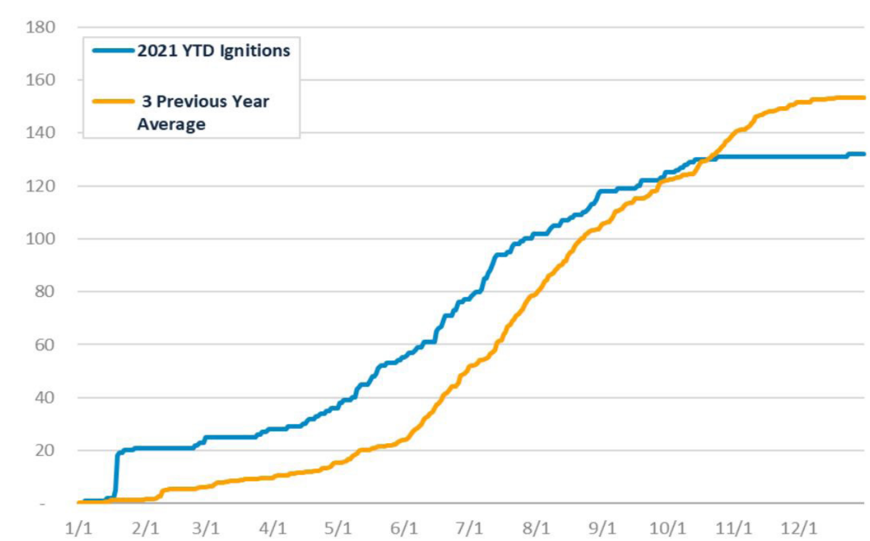
SPOTLIGHT

WILDFIRES IN CALIFORNIA

Historically, significant parts of California would burn annually, especially during the warm, dry months of the year. Many species native to California adapted to these regular, low- and moderate-intensity wildfires. These regular fires played an important role in keeping the state's forests and landscapes healthy by periodically clearing underbrush and contributing to regrowth of native plant species. While wildfires have potential benefits, they can also be highly problematic when they are much more severe than historically encountered and more often threaten lives and property.

In recent years, California has experienced a growing number of these problematic wildfires. The recent increase in destructive wildfires has been attributed to a few key factors,

FIGURE 2: CPUC REPORTABLE IGNITIONS IN HFTDs



Source: California Office of Energy Infrastructure Safety, 2022 Wildfire Mitigation Plans including climate change, poor forest and land management practices, and increased development in fire-prone areas. The state has responded in kind by increasing the California Department of Forestry and Fire Protection (CalFire's) total funding for fire protection, resource management, and fire prevention to $3.7Bin 2021—22 up from $800M in 2005-06.

In California, the investor-owned utilities (IOUs) are subject to a strict application of the law of inverse condemnation. Quickly translated, they are liable for all property damage associated with fires started by their equipment. That, along with California Public Utilities Commission (CPUC) General Order 95, has put increased wildfire prevention and safety at the forefront of everyone's minds including the State Government, IOUs, public-owned utilities (POUs), and essential contractors performing work. It's been an all-hands-on-deck approach to mitigating and reducing the wildfire risk factors, and it seemingly has paid dividends.

Per the **Pacific Gas & Electric (PG&E) 2022 Audit Report on Compliance with their 2021 Wildfire Mitigation Plan**, their wildfire mitigation efforts resulted in a 10% reduction of ignitions caused by electrical infrastructure in 2021 compared to previous years. Specifically, enhanced powerline safety settings (EPSS) and public safety power shutoff (PSPS) events successfully decreased ignitions of electrical infrastructure in high fire threat districts by 80% vs. the past 3-year average. See Figure 2.

The good news for the casualty market is that a majority of these large wildfires are caused by lightning, arson, or human-related activities. Per CalFire, of the top 20 most destructive wildfires over the past 10 years in California, 2 were attributable to utility powerlines. See figure 3. Further, in 2020-21, per the CalFire Redbook, 4 of the top 5 wildfires by acreage burned were caused by lightning, with the other one being undetermined. Those 5 wildfires accounted for 2,491,323 acres burned, along with 5,015 structures destroyed. While the 2020-21 wildfire season saw an 8% increase in the number of wildfires and a 976% increase in the number of acres burned from 2019-20, almost all of that increase is attributable to lightning-caused fires. See Figure 4.

The above data points are just one example of how RT Specialty brokers leverage data, analytics, and their deep understanding of the wildfire-exposed risks in California. Our casualty experts have been successful in placing some of the largest wildfire-exposed California utilities and utility contractors and continue to be leaned on by the underwriting community for our expertise and knowledge in this complex arena. As the state continues its wildfire resilience, insuring casualty lines in wildfire-exposed areas continues to be an option to help mitigate exposure.

AUTO / TRANSPORTATION

The commercial auto exposure has rebounded with the total miles driven increasing over the last year. Auto loss frequency and severity are returning to pre-pandemic levels. Coupled with the rapid rise in general economic inflation and the automakers' chip shortages and supply chain disruptions, claim costs and auto insurance rates are increasing along with the high demand for new and used cars. There is new primary and excess liability capacity coming into the market, allowing preferred commercial auto risks to stay within more moderate level rate changes on renewals.

Transportation and accounts heavily weighted with large fleet exposures continue as a significant underwriting concern. Increasing loss severity has been driven by social inflation and the high proportion of litigated claims and "nuclear" verdicts. Over the past two years, the excess liability carriers that continue to specialize in transportation have been steadily raising their attachment points. Companies with poorer loss experience, in addition to taking on much higher self-retentions, have also needed to accept / lower liability program limits with the lack of available excess capacity at reasonable pricing levels.

The carriers' primary concerns for the industry continue, with high driver-turnover rates, large frequency of claims with an increased number

FIGURE 3: TOP 20 LARGEST CALIFORNIA WILDFIRES

	FIRE NAME (CAUSE)	*DATE*	*COUNTY*	*ACRES*	*STRUCTURES*	*DEATHS*
1	**AUGUST COMPLEX** *(Lightning)*	August 2020	Mendocino, Humboldt, Trinity, Tehama, Glenn, Lake, & Colusa	**1,032,648**	935	1
2	**DIXIE** *(Powerlines)*	July 2021	Butte, Plumas, Lassen, Shasta & Tehama	**963,309**	1,329	1
3	**MENDOCINO COMPLEX** *(Human Related)*	July 2018	Colusa, Lake, Mendocino & Glenn	**459,123**	280	1
4	**SCU LIGHTNING COMPLEX** *(Lightning)*	August 2020	Stanislaus, Santa Clara, Alameda, Contra Costa, & San Joaquin	**396,624**	222	0
5	**CREEK** *(Undetermined)*	September 2020	Fresno & Madera	**379,895**	853	0
6	**LNU LIGHTNING COMPLEX** *(Lightning/Arson)*	August 2020	Napa, Solano, Sonoma, Yolo, Lake, & Colusa	**363,220**	1,491	6
7	**NORTH COMPLEX** *(Lightning)*	August 2020	Butte, Plumas & Yuba	**318,935**	2,352	15
8	**THOMAS** *(Powerlines)*	December 2017	Ventura & Santa Barbara	**281,893**	1,063	2
9	**CEDAR** *(Human Related)*	October 2003	San Diego	**273,246**	2,820	15
10	**RUSH** *(Lightning)*	August 2012	Lassen	**271,911 CA / 43,666 NV**	0	0
11	**RIM** *(Human Related)*	August 2013	Tuolumne	**257,314**	112	0
12	**ZACA** *(Human Related)*	July 2007	Santa Barbara	**240,207**	1	0
13	**CARR** *(Human Related)*	July 2018	Shasta County & Trinity	**229,651**	1,614	8
14	**MONUMENT** *(Lightning)*	July 2021	Trinity	**223,124**	50	0
15	**CALDOR** *(Human Releated)*	August 2021	Alpine, Amador, & El Dorado	**221,835**	1,003	1
16	**MATILIJA** *(Undetermined)*	September 1932	Ventura	**220,000**	0	0
17	**RIVER COMPLEX** *(Lightning)*	July 2021	Siskiyou & Trinity	**199,343**	122	0
18	**WITCH** *(Powerlines)*	October 2007	San Diego	**197,990**	1,650	2
19	**KLAMATH THEATER COMPLEX** *(Lightning)*	June 2008	Siskiyou	**192,038**	0	2
20	**MARBLE CONE** *(Lightning)*	July 1977	Monterey	**177,866**	0	0

There is no doubt that there were fires with significant acreage burned in years prior to 1932, but those records are less reliable, and this list is meant to give an overview of the large fires in more recent times.
This list does not include fire jurisdiction. These are the Top 20 regardless of whether they were state, federal, or local responsibility.
*Numbers not final.

1/13/2022

Source: CalFire Top 20 Largest California Wildfires of young and inexperienced drivers, and overall deteriorating driver quality from having to accept less preferred drivers. There continues to be a significant emphasis on telematics and other innovations by the trucking industry, which has become a necessary component to detail and highlight the underwriting submissions for large fleet exposures.

Another positive development has been the recent and rapid development of program carriers. There are currently 24 program carriers in comparison to only 3 a few years ago. Many of these will be trucking specific and available through MGUs, giving new options to replace previous programs that have been evaporating or withdrawing their market capacity in recent years.

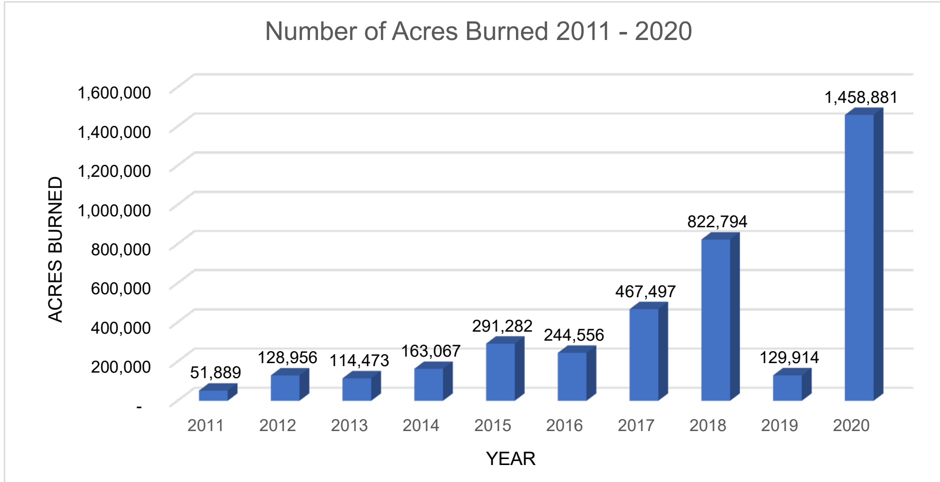
The implementation and adoption of telematics technology, and an increased focus on driver training, are expected to improve insurability and start to bring back more market capacity.

CONSTRUCTION

The Infrastructure Investment and Jobs Act passed in late 2021 is expected to have a large impact on the construction sector for transportation (roads, bridges, highways, rail, EV infrastructure), clean energy transmission and upgrades to the electrical grid, water infrastructure, public-private projects, and much more. Overall, primary and excess liability capacity (although not necessarily rate) is stabilizing, with pricing pressure continuing to be most aggressive on the lead excess layers. The general economic rise in inflation has also played a significant factor in higher insurance pricing, especially on a per-project basis.

Specific areas that continue to be constrained with firm pricing and very few market participants include Florida residential construction (now exacerbated by Hurricane Ian), New York construction, and framed condo projects in the construction defect states. Outside of these challenging areas, new capacity is starting to enter the construction excess market to increase competition with the potential for moderating price increases.

FIGURE 4



Source: California Department of Forestry and Fire Protection (Cal Fire) | Department of Toxic Substances Control

REAL ESTATE

Several carriers have traditionally supported the casualty lines in the real estate sector but are now re-evaluating their habitational insured portfolios. This has resulted in several carriers non-renewing or reducing their limit offerings, which is contributing to the rate increases and capacity restrictions. Some new participants are starting to come into the market, but these insurers remain selective and cautious. Umbrella towers continue to get built with short blocks of limits in the first $10M, but with new entrants into the space, we are now seeing some signs of pricing increases slowly tapering. Older Florida condo properties have been very challenging following the Surfside collapse in 2021. These underwriting submissions will require significant levels of loss control analysis and historical construction detail to be considered.

Overall, the portfolios that include multi-family have been most heavily impacted in comparison to commercial and retail sectors, which have been keeping pricing and capacity on those renewals more competitive. Properties inside the portfolios with poor crime scores or violent crime losses continue to require insureds to accept more restrictive terms. This can result in stricter policies being renewed with exclusions such as firearms or only offering small sub-limits for assault and battery (A&B) and / or abuse and molestation (A&M). Real estate owners and property managers need to differentiate their risk and highlight strong risk management protocols, operational controls, and thorough claims management processes.

SUMMARY

Although rates generally continue to increase, the casualty insurance market has recently shown signs of moderating. There is some reduced volatility with notable exceptions for certain industry segments such as transportation, construction, and habitational real estate, where the market remains highly challenging. New carriers and programs are entering the market and there continues to be strong reinsurance support.

The RT Casualty team has been built with the necessary expertise and teamwork to fully assist its retail brokers in the preparation for renewals and new business negotiations. We understand each account is unique and has different risk characteristics. The goal of our advanced planning is to best differentiate the account's risk profile for presentation to the casualty markets. In coordination with the retail agent and the insured, your RT Casualty team will assist in the development and implementation of a renewal strategy in order to evaluate viable alternatives and help provide competitive renewal outcomes.