Vanderbilt Law Review

Volume 41
Issue 5 *Issue 5 - October 1988*

Article 2

10-1988

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I. INTRODUCTION

A perceived crisis in the nation's liability insurance system erupted in 1986.[1] Some businesses saw their insurance premiums double in a period of two years, and others found the coverages they required totally unavailable.[2] While trial lawyers and consumer groups asserted

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The research that forms the basis for much of this Article was conducted while the Authors were members of the research team of the Academic Task Force for Review of the Insurance and Tort Systems, an agency within the Executive Office of the Governor of the State of Florida, which was established and funded by the Florida Legislature. The Authors wish to express their appreciation to Marshall M. Criser, Chairman of the Academic Task Force, the other members of the Task Force, and Executive Director Carl S. Hawkins, for their support and encouragement. The Authors also wish to thank system programmer Michael Kelly, research assistant Cally Smith, and administrative secretary Noreen Fenner for their contributions to this Article.

1. *See, e.g.*, INSURANCE SERVICES OFFICE, 1985 A CRITICAL YEAR: A STUDY OF THE PROPERTY/CASUALTY INSURANCE INDUSTRY (1985); Church, *Sorry, Your Policy is Cancelled*, TIME, March 24, 1986, at 16; Willard & Perlman, *The Lawsuit Crisis: Two Perspectives*, 47 INS. REV., May 1986, at 58 (Richard K. Willard's perspective); *Liability Insurance: A Growing Crisis*, N.Y. Times, Feb. 20, 1986, at B3, col. 4.

2. ACADEMIC TASK FORCE FOR REVIEW OF THE INSURANCE AND TORT SYSTEMS, FINAL FACT-FINDING REPORT ON INSURANCE AND TORT SYSTEMS 29-66 (March 1, 1988) [hereinafter FINAL FACT-FINDING REPORT] (copy on file with Authors); ASSOCIATED INDUSTRIES OF FLORIDA, LEGISLATIVE LETTER (April 23, 1986) (copy on file with Authors). Liability premiums for retail store owners and

that insurance company investment and pricing practices, as well as huge profits, had caused the crisis,[3] others alleged that an increased "claims consciousness" among the American public had spawned the liability insurance affordability and availability problems. Richard Berman, a national representative of the United States Chamber of Commerce, proclaimed that the judicial system had "gone berserk" and that litigation was "America's equivalent of a national lottery."[4]

The sparse academic literature available on the issue of claims frequency addresses solely those claims that result in litigation.[5] This type of analysis is incomplete and potentially misleading because it does not reflect the larger number of liability claims against insureds that are paid or otherwise closed without litigation. The frequency of litigated cases is not exclusively a function of claims consciousness, but is instead a product of both claims consciousness and the willingness of insurers to avoid litigation by paying claims without a battle. In other words, any observed increase in litigation might result as much from insurers' and defendants' refusing to pay claims without litigation as from increased claims consciousness. In any event, the literature available regarding litigation statistics does not suggest that there has been a litigation "explosion" in the civil justice system.[6]

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others purchasing Owners, Landlords, and Tenants' coverage increased 169% from the third quarter of 1984 through the first quarter of 1986. FINAL FACT-FINDING REPORT, *supra*, at 38. Premiums for obstetricians and gynecologists increased 245% during the period from the first quarter of 1984 through the third quarter of 1986. ACADEMIC TASK FORCE FOR REVIEW OF THE INSURANCE AND TORT SYSTEMS, PRELIMINARY FACT-FINDING REPORT ON MEDICAL MALPRACTICE 30 (August 14, 1987) [hereinafter PRELIMINARY FACT-FINDING REPORT] (copy on file with Authors). A survey conducted by Associated Industries of Florida, a trade organization, showed an average increase in premiums during a one year period of 128.7%. ASSOCIATED INDUSTRIES OF FLORIDA, *supra*, chart 3, at 443. Further, 16.3% of the respondents indicated they had difficulties obtaining coverage. *Id.* chart 5, at 445.

3. *See* Perlman, *Don't Confuse Me With The Facts*, 22 TRIAL, January 1986, at 5; *Nader Charges Insurers With Price-Gouging: Urges Tighter Regulation*, Wash. Post, January 7, 1986, at D1, col. 6. Robert Hunter, former Federal Insurance Administrator during the Carter and Ford administrations and currently president of the National Insurance Consumer Organization, charges that the crisis is primarily a liability insurance problem caused by "cash-flow underwriting." Hunter & Borzilleri, *The Liability Insurance Crisis: Insurers Put the Squeeze on Consumers*, 22 TRIAL, April 1986, at 42, 43.

4. *Availability and Cost of Liability Insurance: Hearings Before Senate Comm. on Commerce, Science, and Transportation*, 99th Cong., 2nd Sess. 49, 52, 53 (1986) (statement of Richard B. Berman, representing United States Chamber of Commerce).

5. *See, e.g.*, Galanter, *The Day After the Litigation Explosion*, 46 MD. L. REV. 3 (1986) [hereinafter Galanter, *The Day After*]; Galanter, *Reading the Landscape of Disputes: What We Know and Don't Know (And Think We Know) About Our Allegedly Contentious and Litigious Society*, 31 UCLA L. REV. 4 (1983) [hereinafter Galanter, *Reading the Landscape*]; Gifford & Nye, *Litigation Trends in Florida: Saga of a Growth State*, 39 U. FLA. L. REV. 829 (1987).

6. Galanter, *The Day After*, *supra* note 5, at 7; Gifford & Nye, *supra* note 5, at 831; Roper, *The Propensity to Litigate in State Trial Courts, 1981-1984, 1984-1985*, 11 JUST. SYS. J. 262, 268-69 (1986). Galanter concludes that the "evidence of current American litigation rates does not

This Article examines national trends in total liability insurance loss payments in recent years and assesses the impact of claims frequency on these figures. To measure claims frequency, the Authors have developed and applied a new methodology that directly addresses the issue of claims propensity. Any increase in the absolute number of liability claims does not necessarily compel a conclusion of increased claims propensity unless the exposure base, the basis upon which the number of claims is measured, is held constant; otherwise increased claims simply might reflect an increased number of insureds, or additional coverages.

This Article's analysis of claims frequency does not support the notion that there was an "explosion" in claims frequency from 1981 through 1984, the period immediately preceding the precipitous increases in liability insurance premiums. Other factors, such as increased defense costs and higher payments per claim, appear to have been more important to the increase in total loss costs than increases in claims frequency. Data presented in this Article, however, does suggest that since 1984 increases in both the frequency and severity of claims have caused the continuing rise in total claim costs.

Part II of this Article analyzes trends in the total amount of losses paid by liability insurance carriers from 1975 through 1986. Part III discusses the role that increased claims frequency has played in the rise in total claims costs. Finally, Part IV summarizes the primary conclusion of this Article: That total claims costs for liability insurers increased dramatically from 1975 through 1986, but that these increased costs were not significantly attributable to an increased number of claims against insured parties during that period.

II. Trends in Total Paid Losses

Even when figures for the total amount of paid losses from 1975 through 1986 are adjusted for price changes and inflation, there remains substantial "real" growth in the total amount of paid losses nationwide.[7] Table 1[8] presents national totals for the aggregate amounts of all

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suggest that rates of civil court filings are dramatically higher than in the recent past." Galanter, *The Day After*, *supra* note 5, at 7. Robert Roper, Senior Staff Associate of the National Center for State Courts, similarly finds no evidence of a national litigation explosion in state trial courts during the period from 1981 through 1986. Roper, *supra*, at 268-69, 272-81.

7. These growth rates most likely understate the true increase in loss payments because the data exclude liability claims paid by self-insured entities. Recent years have seen an increased use of self-insurance for liability expenses by medium to large corporations, so the degree of understatement of total loss payments may be increasing. The conclusions presented in this Article are not affected by this missing data because the frequency trends discussed are adjusted for changes in the amounts of insurance coverage.

8. Table 1 is based upon data obtained from the A.M. Best Company. The A.M. Best Com-

claims *paid* by liability insurers and the aggregate amounts of all claims *incurred* by liability carriers for each year from 1975 through 1986.[9] Total loss payments are listed for two categories of liability coverages: "Other Liability" is a separate "line"[10] that includes premises and products liability as well as professional liability (excluding medical malpractice); "Commercial liability" is a broader grouping of different types of liability insurance that includes not only the Other Liability line, but also medical malpractice and commercial automobile liability.

Table 1
Aggregate Claim Data: United States

	Other Liability				Commercial Liability*			
Year	Claims Paid	% Change	Claims Incurred	% Change	Claims Paid	% Change	Claims Incurred	% Change
	$000,000		$000,000		$000,000		$000,000	
1975	$1,093		$1,265		$4,618		$5,614	
1976	$1,217	11.3%	$1,487	17.5%	$4,885	5.8%	$6,409	14.2%
1977	$1,387	14.0%	$1,824	22.7%	$5,477	12.1%	$7,181	12.0%
1978	$1,535	10.7%	$2,758	51.2%	$6,299	15.0%	$9,694	35.0%
1979	$1,776	15.7%	$3,216	16.6%	$7,780	23.5%	$11,806	21.8%
1980	$2,090	17.7%	$3,444	7.1%	$9,330	19.9%	$13,184	11.7%
1981	$2,460	17.7%	$3,435	−0.3%	$10,713	14.8%	$14,633	11.0%
1982	$2,857	16.1%	$3,782	10.1%	$12,741	18.9%	$16,771	14.6%
1983	$3,377	18.2%	$4,089	8.1%	$14,199	11.4%	$18,647	11.2%
1984	$4,445	31.6%	$5,878	43.8%	$17,879	25.9%	$23,934	28.4%
1985	$5,458	22.8%	$10,678	81.7%	$20,484	14.6%	$33,543	40.1%
1986	$7,845	43.7%	$16,128	51.0%	$21,984	7.3%	$36,636	9.2%
Average Increase Per Year:		19.6%		26.0%		15.2%		18.6%

*Includes commercial auto liability, commercial auto no-fault, commercial multiperil, other liability, and medical malpractice.

Source: A.M. Best & Co.

Total paid claims for Other Liability increased from slightly more than one billion dollars in 1975 to almost eight billion dollars in 1986, growing at a cumulative annual rate of approximately twenty percent

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pany is an independent data gathering and data analysis organization that examines virtually all types of insurance organizations. Published financial information is compiled by A.M. Best Company from individual company financial statements, which are prepared in accordance with uniform state standards.

9. The distinction between claims paid and claims incurred is important to understanding the economics of the property-liability insurance industry. Claims paid refers to the actual amount of dollars paid out by the insurance industry in a given time period. Claims incurred reflects both claims paid arising during a designated period, plus amounts which the insurance industry estimates will be paid in the future, the latter amounts being loss reserves. Insurance premium rates are based upon incurred claims rather than paid claims.

10. A "line" refers to a grouping of similar insurance coverages for data gathering and financial reporting purposes.

per year. Incurred claims grew at an annual compound rate of twenty-six percent per year for the same time period. The comparable figures for annual compound increases in the broader measure of liability, Commercial Liability, were somewhat lower—approximately fifteen percent for paid claims and nineteen percent for incurred claims.

The dramatic growth in total paid claims during the period 1975 through 1986 expressed in absolute dollars, however, may constitute neither convincing evidence of dramatically greater societal claims propensity nor a crisis in the liability insurance system. That growth might be attributable solely to increases in population and inflation; for example, an increase in the total number of claims would be expected as population increases. Moreover, the total dollar amount of paid claims increases as the cost of living increases. Together these factors might explain the increase in the absolute number of dollars spent on liability claims without any increase in claims propensity.

Table 2, however, demonstrates the dramatic growth in the total amounts of paid claims even after adjusting for increases in population and the cost of living. Total claims payments for Other Liability claims have grown at an average annual rate of eleven percent since 1975, with most of the growth occurring between 1982 and 1986. Incurred claims costs have exhibited higher growth rates, but year to year changes have been more erratic because of changes in loss reserves.[11] Similar, but less dramatic growth patterns emerge from the Commercial Liability data.

Figure 1 illustrates the relationship between incurred and paid claims. While paid claims have exhibited a steady upward trend, incurred claims have fluctuated significantly as insurers adjusted reserve levels.

III. Trends in Claims Frequency

What role has increased claims frequency played in the increase in total paid claims costs? Has there been a substantial increase in the frequency of paid claims, or must the increase in total claims costs be attributed to other factors, such as increases in the severity of claims payments or in defense costs? In other words, are Americans more

11. Greater year to year fluctuations in incurred losses, compared to fluctuations in paid losses, are observed because of periodic changes in insurers' reserve estimates. Reserve estimates represent amounts of future liabilities as determined by company management. The size of the reserve depends on both the number of claims upon which some amount will be paid and the amount of each claim. Court decisions can affect estimates of both the number and amount of claims. For example, court decisions on latent diseases could cause insurers to revise upward the number of cases upon which they expect to make payments. Similarly, an unexpectedly high jury verdict in a personal injury case may cause insurers to revise upward the probable payout on similar cases.

Table 2
Inflation - Adjusted Claims Per Person:
Nationwide

	Other Liability				Commercial Liability*			
Year	Claims Paid	% Change	Claims Incurred	% Change	Claims Paid	% Change	Claims Incurred	% Change
1975	$5.06		$5.86		$21.38		$25.99	
1976	$5.28	4.3%	$6.45	10.1%	$21.18	−0.9%	$27.79	6.9%
1977	$5.59	6.0%	$7.36	14.1%	$22.09	4.3%	$28.96	4.2%
1978	$5.69	1.7%	$10.22	39.0%	$23.35	5.7%	$35.93	24.1%
1979	$5.85	2.9%	$10.60	3.7%	$25.63	9.8%	$38.90	8.3%
1980	$5.99	2.4%	$9.88	−6.8%	$26.76	4.4%	$37.81	−2.8%
1981	$6.33	5.6%	$8.84	−10.5%	$27.56	3.0%	$37.64	−0.4%
1982	$6.86	8.3%	$9.08	2.7%	$30.58	10.9%	$40.25	6.9%
1983	$7.78	13.4%	$9.42	3.8%	$32.70	7.0%	$42.95	6.7%
1984	$9.73	25.1%	$12.87	36.6%	$39.14	19.7%	$52.40	22.0%
1985	$11.43	17.5%	$22.37	73.8%	$42.91	9.6%	$70.27	34.1%
1986	$15.95	39.5%	$32.78	46.5%	$44.69	4.1%	$74.47	6.0%
Average Increase Per Year:		11.0%		16.9%		6.9%		10.0%

*Includes commercial auto liability, commercial auto no-fault, commercial multiperil, other liability, and medical malpractice.

Source: A.M. Best & Co.
U.S. Bureau of the Census

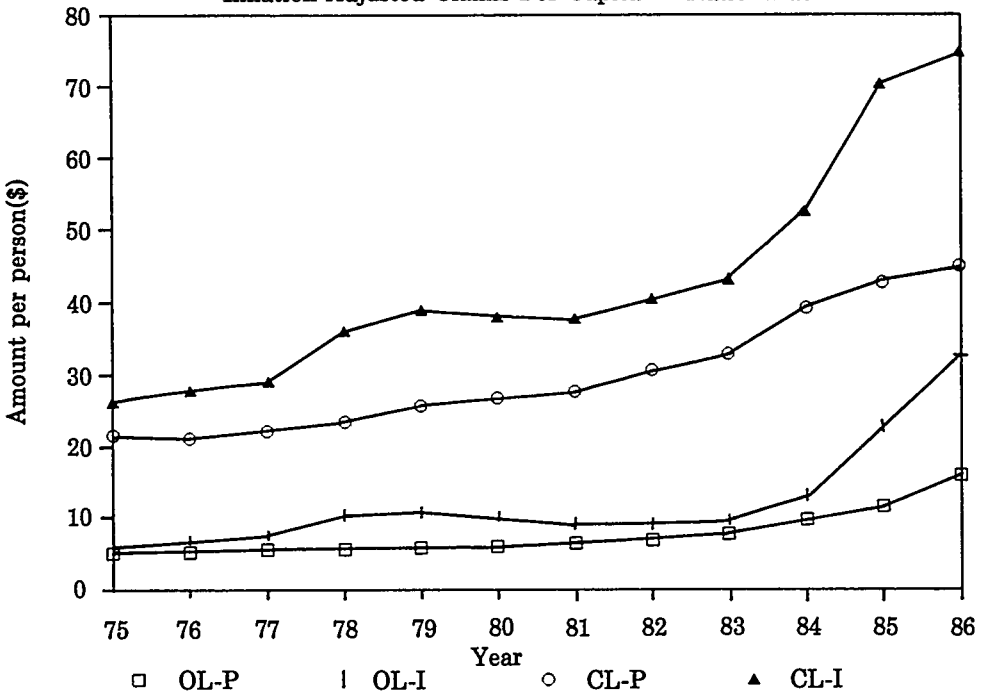
prone to file claims against insured parties than they were a decade ago?

Frequency refers to the number of claims paid or incurred in a year and has meaning only if the number of claims can be related to an appropriate base, such as the number of insured units. For example, even a dramatic increase in the absolute number of claims for the Other Liability line provides little information about society's claims propensity unless one knows something about the amount of insurance coverage that produced the claims (*i.e.*, the number of insureds and the amount of exposure for each insured). Part III discusses the problem of measuring the number of insured units and then describes a new procedure that holds constant the number of insured units to determine trends in loss frequency per exposure unit. To perform this analysis, two categories of data are required: (1) data measuring the level of exposure to claims; and (2) the total number of claims.[12]

12. The Authors obtained these data from the Insurance Services Office, Inc. (ISO), the major nonprofit, independent, national service organization providing rating, statistical, actuarial, and other policy writing services for fifteen lines of insurance to 1,300 member companies in the United States. ISO collects premium, loss, and exposure data from member companies and uses this information to carry out its various service activities. Incurred claim and exposure data provided by

Figure 1

Inflation-Adjusted Claims Per Capita — Nationwide



OL-P = Other Liability - Paid Claims Per Person
OL-I = Other Liability - Incurred Claims Per Person
CL-P = Commercial Liability - Paid Claims Per Person
CL-I = Commercial Liability - Incurred Claims Per Person

Source: Table 1

A. Adjustment for Exposure Changes

In some specific areas of liability insurance, the frequency of claims per exposure unit is relatively easy to determine. For example, the number of medical malpractice claims for each insured physician is a better measure of claims propensity than is the total number of medical malpractice claims.[13] Any attempt to establish a common exposure unit

ISO are representative of the entire market. ISO carriers account for a substantial percentage of the total premium volume for liability carriers in the United States.

13. *See* Nye, Gifford, Webb & Dewar, *The Causes of the Medical Malpractice Crisis: An Analysis of Claims Data and Insurance Company Finances*, 76 GEO. L.J. 1495, 1540-44 (1988). Even with medical malpractice insurance, the number of insured doctors is not a perfect proxy for liability exposure because this number does not take into account the differences between full- and part-time physicians, or other differences in the amount of exposure per physician, such as the varying number of treatment procedures per physician.

for insurance coverages in the troubled commercial lines, however, is futile because the exposure bases differ depending on the more than 1300 "risk classes"[14] into which the insured may fall. For example, the price of liability coverage for retail drugstores is determined by using an exposure base of square footage in the store, but the exposure units for most other types of retail establishments are based on dollar receipts. Widely differing exposure units make it impossible to aggregate exposure units or to determine the frequency of claims per exposure unit for any significantly large category of insureds. In addition, the significance of frequency trends within any particular risk class is limited because trends within a narrowly defined group of insureds may be based upon a sample that is too small to provide statistically valid trends over time.

To circumvent these methodological problems, the Authors determined that claims frequency per exposure unit could be compared over time by using a premium volume data series, known as "premium at present manual rates," as a broadly based proxy for exposure units. Premium at present manual rates data have been developed and used over the years by actuaries at Insurance Services Office, Inc. (ISO)[15] to test the adequacy of rate levels by placing the exposures of all companies on a comparable basis. No one previously recognized, however, that the premium at present manual rates data series provides an opportunity to trend claims frequency by adjusting for changes in the exposure base.

Premium at present manual rates is an aggregate amount of premium found by multiplying the premium rates in effect on a given date by the number of exposure units insured in a given risk class in a particular year.[16] The results for all risk classes then can be aggregated to determine the premium at present manual rates for the entire Other Liability line. In this study, 1984 premium rates were multiplied by the number of exposure units insured in 1984.[17] Similarly, the number of exposure units insured in 1983 was multiplied by 1984 rates, as were the numbers for 1982 and earlier years. The result is a series of total premium figures for each year in which any change in total premium volume expressed in dollars is attributable entirely to changes in the number of exposure units insured rather than to price changes.

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14. A "risk class" refers to a grouping of insureds with similar loss propensities to produce a fair relationship between the premium charged and the exposure to loss presented by the insured.

15. *See* discussion *supra* note 12.

16. A description of the exposure unit measure for different types of businesses is provided in INSURANCE SERVICES OFFICE, COMMERCIAL STATISTICAL PLAN, pt. VI, § D (1978-80).

17. Rates in effect in 1984 were used because this was the latest year for which premium at present rate data were available.

Table 3
Index of Claim Frequency
for Products Liability Property Damage: Nationwide

Year	Premium at Present Manual Rate (PPR) ($000) (1)	Number of Incurred Claims (2)	Number of Incurred Claims per $1,000 PPR (3)=(2)÷(1)	Index of Claim Frequency
1975	$37,119	18,913	0.5095	100.0
1976	51,528	19,102	0.3707	72.8
1977	72,335	18,032	0.2493	48.9
1978	94,908	21,965	0.2314	45.4
1979	92,205	20,511	0.2224	43.7
1980	91,686	21,673	0.2364	46.4
1981	125,681	23,432	0.1785	35.0
1982	107,794	31,922	0.2961	58.1
1983	108,143	33,387	0.3087	60.6
1984	118,680	36,705	0.3093	60.7

Source: Insurance Services Office, Inc.

Note: Figures are for monoline (single line coverages) and multiline (multiple line coverages) data combined.
Number of Claims Incurred includes all claims anticipated.

Thus, the changes in premium at present manual rates are proportional to changes in the number of exposure units.

To establish changes in frequency of claims over time, the premium at present manual rate figures can serve as a proxy measure for changes in the number of exposure units. In Table 3, Column (1) shows premium at present manual rates for bodily injury coverages for products liability.

B. Number of Incurred Claims

The first figure required for determining frequency per exposure unit is premium at present manual rate; the second figure is incurred claims for the same policy year.[18] To determine claims per exposure unit per year, incurred claims data, rather than paid claims data,

18. These figures are maintained by individual companies and reported to ISO (if the companies are members) on a periodic basis. ISO retrieved these figures and reported them to the Authors in their capacity as members of the research staff of the Academic Task Force for Review of the Insurance and Tort Systems. The Authors believe this Article is the first in law review literature to report and analyze this type of information.

should be used.[19] The incurred claims data, as previously described,[20] include both paid and reserved claims and, therefore, are a more complete measure of claims frequency for the policy year. Incurred claims data for several liability lines were obtained from ISO; examples of these data are presented in column (2) of Table 3.

C. *Trends in Frequency Adjusted for Exposure Units*

The number of incurred claims for each policy year was divided by the premium at present manual rate figure for the same year to determine the number of claims per one thousand dollars of premium. These figures, displayed in the third column of Table 3, were used to develop an index of frequency. The results are shown in the last column of Table 3.[21] The basis of "100" for this index represents a starting value for the number of incurred claims per one thousand dollars of premium at present manual rate (using 1984 premium figures).[22] The entry of "60.7" for the year 1984 in the "Index of Claim Frequency" column means that 1984 had only 60.7 percent of the 1975 level of incurred claims per exposure unit for product liability property damage coverage. Thus, the index can be used to measure changes in the frequency of liability insurance claims for a given level of risk exposure over time.

Table 4 presents claim frequency results for other categories of liability insurance in the United States. It shows both the number of claims per year and the index of claim frequency, described above, which reflects the frequency of claims adjusted for changes in the exposure base.[23]

For every type of liability coverage examined, the absolute number of incurred claims increased during the period 1975 through 1984 at rates in excess of population growth. These increases ranged from a 2.9 percent compound average annual increase in claims covered under

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19. Incurred claims for a particular year means all claims attributable to an occurrence in that year regardless of when the claims are reported or paid.

20. *See* discussion *supra* note 9.

21. This methodology was developed by the Authors as members of the research staff of the Academic Task Force. ISO staff reviewed the procedure and acknowledged its validity for the purpose of establishing claim frequency trends.

22. The starting value of 100 was arbitrarily selected as a reference point. The value of the index rises and falls as the number of claims per exposure unit rises and falls. The index approach is used because it more effectively illustrates changes in claims frequency.

23. Owners, Landlords, and Tenants' liability insurance provides coverage for the ownership, use, or maintenance of the insured premises, as well as for all operations necessary or incidental to these premises. Manufacturers and Contractors' liability insurance provides similar coverage but the contract is tailored to meet their specific needs (*e.g.*, the exclusions relating to structural alterations, construction, and demolition are removed for contractors). A more detailed discussion of liability coverage is provided in C. WILLIAMS & R. HEINS, RISK MANAGEMENT AND INSURANCE 352-54 (5th ed. 1985).

Table 4
Trends in Liability Claims: Nationwide

Policy Year	Manufacturers & Contractors' Bodily Injury # of Incurred Claims	Index Value	Manufacturers & Contractors' Property Damage # of Incurred Claims	Index Value	Owners, Landlords, & Tenants' Bodily Injury # of Incurred Claims	Index Value	Products Liability Bodily Injury # of Incurred Claims	Index Value	Products Liability Property Damage # of Incurred Claims	Index Value
1975	15,251	100.0	73,011	100.0			9,048	100.0	18,913	100.0
1976	15,189	104.5	69,666	100.3	34,782	100.0	9,978	68.4	19,102	72.8
1977	13,821	79.3	67,704	80.4	33,711	86.3	10,701	64.6	18,032	48.9
1978	14,533	69.5	70,362	71.1	33,819	50.2	8,299	40.8	21,965	45.4
1979	14,872	62.7	70,304	63.1	33,876	99.6	8,121	42.4	20,511	43.7
1980	17,218	67.6	85,224	75.0	52,830	103.5	13,221	62.0	21,673	46.4
1981	17,090	58.3	86,112	66.8	63,658	105.7	14,648	55.6	22,432	35.0
1982	20,146	66.2	103,201	76.9	77,827	132.8	16,835	63.5	31,922	58.1
1983	18,866	60.6	109,119	79.4	81,228	145.9	14,197	49.2	33,387	60.6
1984	19,799	61.9	118,335	82.0	83,220	157.5	14,002	46.9	36,705	60.7
Average Annual Growth	2.9%	−5.2%	5.5%	−2.2%	11.5%	5.8%	5.0%	−8.1%	7.7%	−5.4%

Source: Calculated from data supplied by Insurance Services Office, Inc.

Manufacturers and Contractors' Bodily Injury Coverage, to an 11.5 percent compound average annual increase in claims for the Owners, Landlords, and Tenants' Bodily Injury Coverage.

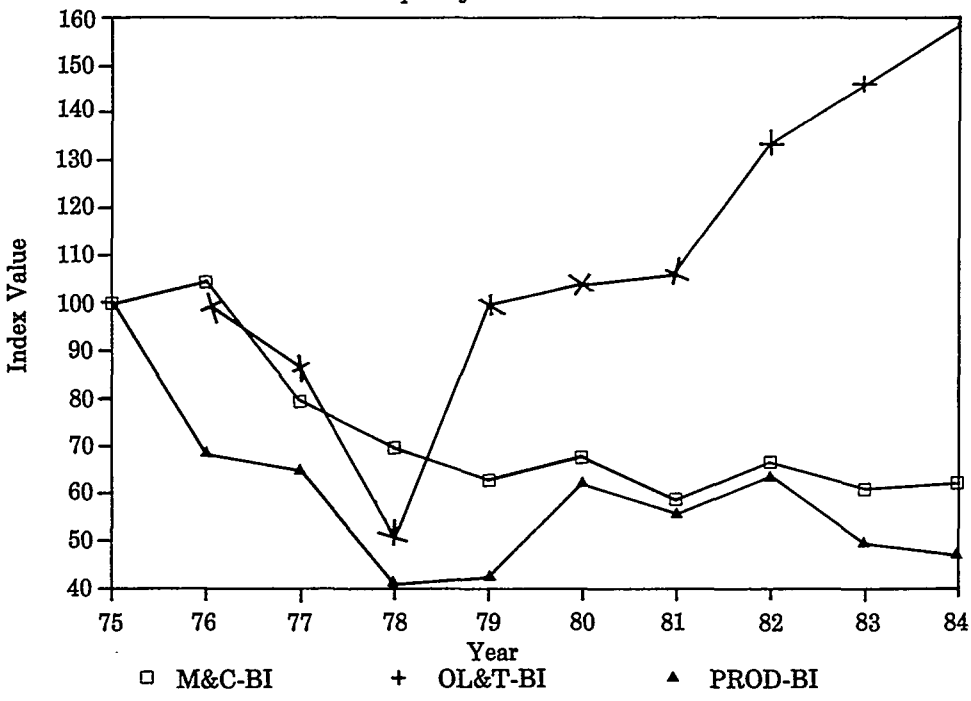
When adjustments are made for changes in the amount of exposure faced by liability insurers, however, a dramatically different picture emerges. The number of incurred claims actually *declined* from 1975 through 1984 in Product Liability coverages and in Manufacturers and Contractors' coverages. Only the frequency of bodily injury claims against Owners, Landlords, and Tenants' coverage increased when the figures were adjusted for exposure units. Figure 2 illustrates these trends.

The results of this analysis provide no evidence of an "explosion" in claims frequency during the decade ending in 1984. This study covers precisely the period during which many have claimed that society became increasingly claims conscious. Increased claims frequency during the decade of 1975 through 1984 was not, therefore, in most cases a substantial cause of the dramatic increases in the cost of liability insurance coverage during this period. In fact, the downward trend in claims frequency probably offset increased costs in other areas, such as higher defense costs and larger average claims payments.[24]

24. FINAL FACT-FINDING REPORT, *supra* note 2, at 92-106, 394-401. The average amount of paid claims in Florida for the Other Liability line increased at an average annual compound rate of 14.4% from 1981 through 1986, a rate substantially in excess of inflation; the average amount paid, however, declined in 1985 and 1986. *Id.* at 92-106. During the past decade, legal fees and other

Figure 2

Claim Frequency Index — Nationwide



M&C-BI = Manufacturers and Contractors' — Bodily Injury
OL&T-BI = Owners, Landlords, and Tenants' — Bodily Injury
PROD-BI = Products Liability — Bodily Injury

Source: Table 4

D. Trends in Claim Filings

The analysis presented above covers the number of claims involving a payment to the claimant in a given policy year. The number of claims for damages made against insureds may possibly increase without any corresponding change in the number of incurred claims. This occurrence is possible if there was an increase in nonmeritorious or frivolous claims that ultimately were closed without payment, or if insurers undertook more vigorous defenses of claims and declined to pay claims that they previously would have paid. Some evidence suggests that this scenario may have occurred during the period from 1975 through 1986. One observable consequence of a more vigorous defense of claims is

litigation costs have increased at a rate substantially in excess of inflation. *Id.* at 394-401.

higher insurance company expenditures for legal defense and other expenses involved in investigating and defending cases; in fact, defense costs increased dramatically during this period of time.[25]

To determine whether the decrease in paid and other incurred claims during the period from 1981 through 1984 corresponded with a decrease in filed claims during the same period, the Authors examined data provided by fourteen of the largest liability insurers or groups of insurers.[26] These data included both the number of policies in force for the Other Liability line during a calendar year and the number of claims filed against insureds under these coverages. The number of policies in force is used in this analysis to provide the measurement of the degree of exposure or the number of insured units.[27] The measure of claim frequency is the claims filing rate, found by dividing the number of claims filed in a given year by the average number of policies in force during the year. The resulting ratio is another method of calculating an approximate measure of society's claims propensity.

The first entry in Table 5 shows that the proportion of Other Liability claims filed nationwide in 1981 to the number of Other Liability policies in force was thirty percent. This ratio fluctuated during the subsequent three years, reaching thirty-four percent in 1984, and then dramatically increasing to forty-one percent in 1986.

The claims per policy analysis confirms that Other Liability claims were relatively stable in the years immediately prior to 1984 and corroborates the suggestion that the decade of 1975 through 1984 was a period marked by declining claims propensity, not by a claims explosion. Table 5 also shows, however, that the generally stable trend in claims per policy reversed in 1984 and that the number of claim filings per policy accelerated dramatically in 1985 and 1986.

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25. *See* sources cited *supra* note 24.

26. The research staff of the Academic Task Force undertook a massive data collection and analysis effort as part of its investigation of the causes of the liability insurance crisis. Important sources of information were individual insurers, who were asked to complete a lengthy questionnaire (167 pages) on their operations. The questionnaire was sent to the top thirty liability insurers in the country. All responded in some fashion, with either fully completed questionnaires or responses to those questions for which data were available. Fourteen individual companies or groups submitted usable responses that permitted the calculation of claim filing rates. These fourteen companies or groups represented approximately 43% of the premium volume of the Other Liability line in 1985.

27. In the absence of a specific measure of the number of exposure units (as defined in Part II of this Article), the number of policies in force is the next best measure of exposure to the number of claims which may be filed.

Table 5
Liability Insurance Claims Filing Rates
Ratio of Claims Filed/Policies in Force: Nationwide

	1981	1982	1983	1984	1985	1986
Average Policy Inventory (000's)	1,066	1,011	1,065	1,087	1,059	1,010
Number of Claims Filed (000's)	315	337	333	367	418	413
Claims Filed/ Average Policy Inventory	30%	33%	31%	34%	39%	41%

Source: Calculated from insurance company responses to a questionnaire distributed by the Academic Task Force for Review of the Insurance and Tort Systems in Florida.

IV. Conclusion

The dramatic price increases in liability insurance lines that occurred from 1984 through 1986 spawned a variety of assertions concerning the cause of the perceived crisis. This Article supports the proposition that total claims costs for liability insurers increased dramatically during the period from 1975 through 1986. These increased costs, however, were not significantly attributable to an increased number of claims against insured parties during that period. When the number of claims against insureds is adjusted for changes in the risk assumed by insurers because of variations in both the number of insureds and the level of the insureds' activities, the number of incurred claims in Other Liability insurance coverages actually declined during the period from 1975 through 1984. Comparable data for later years is not available, but an analysis of claim filings (as opposed to paid claims) indicates that a major increase in claims propensity occurred in 1985 and 1986. It is too soon to know what proportion of these filings will actually result in paid claims.