Expanding Child Victim Compensation Laws Could Adversely Affect Insurers

New York State Governor Andrew Cuomo signed the Child Victims Act of 2019 (CVA) into law on February 14, 2019. The CVA, which took effect immediately upon Governor Cuomo's signature, covers sexually based offenses and may lead to an onslaught of civil lawsuits against academic institutions, religious institutions, municipal entities, and other employers in New York State.

The CVA amends several New York laws governing sexual offenses committed against children. The CVA:

- Extends the time to bring felony charges by five years (until the victim turns 28)
- Allows victims to seek civil relief against abusers and enabling institutions until they turn 55 (expanding the earlier five-year statute of limitations [SOL] significantly)
- Opens up a one-year, one-time window, beginning on August 14, 2019, for victims to seek compensation regardless of the abuse date
- Removes the 90-day notice of claim requirement for bringing child sexual abuse claims against municipalities and school districts

Exhibit 1
Recent Legislative Activity — Statutes of Limitations for Child Sexual Abuse Cases

Notes: Governor of New Mexico vetoed bill that had passed legislature. Colors represent status of legislative activity; laws vary widely by state. Source: https://www.childusa.org/2019sol/
In addition to New York, 16 other states and the District of Columbia have SOL reform laws taking effect in 2019. Three additional states passed legislation in 2019, but New Mexico’s Governor vetoed the bill on his desk. Overall, reform legislation has been actively addressed in almost 80% of all states in 2019 (Exhibit 1).

Emerging Risk Highlights Importance of Modeling Casualty Catastrophes
During its April 18, 2019, first quarter earnings call, The Travelers Companies noted that first quarter results included net unfavorable prior year loss reserve development of $21 million for its Business Insurance segment on a pretax basis, compared to net favorable prior year development of $66 million pretax in the first quarter of 2018. The year-over-year change resulted primarily from the enactment of the CVA in New York during the first quarter and the potential exposure to claims in the general liability line.

Chubb Limited noted that, for its New York exposures specifically, it was too early to predict the outcome of any claims. During the fourth quarter of 2018, however, the company recorded additional Incurred But Not Reported (IBNR) loss reserves in response to “the difficult legal environment around molestation and abuse.”

The expansion of child victim compensation laws in New York and other states is likely to adversely affect the reserve positions of insurers with general liability exposure (on a primary or excess basis) to schools, religious institutions, and municipal entities. Insurers will have to deal with marked increases in frequency of claims, which may lead to significant increases in defense cost containment expenses. This emerging situation emphasizes the need to carefully manage latent risk in casualty lines of business through appropriate underwriting language, exclusions, prudent reserving, and overall risk controls in an insurer’s enterprise risk management (ERM) framework.

Casualty catastrophe scenarios are harder to model given the unpredictable nature of risks (liability risks could range from asbestos, talc, Chinese dry wall to changes in legislation), and the long-tail nature of these liabilities. However, we would consider an insurer’s ERM practices more favorably if they consider the impacts in strategic decisions, including underwriting, pricing, reserving, and reinsurance.

The potential increase in claims and litigation could significantly affect insurers that specialize in providing coverage to these entities. Depending on the degree to which the operating performance or the business profile of rated insurance companies becomes impaired, the fallout from the CVA and similar laws could negatively affect the ratings or rating outlooks of companies with past and present exposure to these types of risks in states that have approved laws extending statutes of limitations. To the extent AM Best perceives the impacts to be outside of risk tolerances, it could be a factor in our rating considerations.

The one-year and two-year look-back periods instituted in some states may cause challenges in reserving for various reasons, including uncertainty in the amount of claims, potential false claims, and claims brought against alleged perpetrators who are no longer alive.

Potential Adverse Effects on Performance
We expect the CVA and similar laws to increase civil litigation, exposing academic, religious, daycare, and municipal entities, as well as other employers, to claims alleging negligence with respect to hiring, supervising, and retaining alleged perpetrators. Although the exposure base may be different, the similarities with asbestos & environmental (A&E) coverage are informative. Both areas have very long latency periods, extending decades, significantly
increasing the risk of litigation. The settlement amounts awarded are unpredictable, leading to uncertainty and challenges in establishing reserves. The CVA has a longer latency period and the interplay between the latency period, social inflation, and behavioral dynamics will affect ultimate losses.

Reinsurers with exposure to primary carriers through traditional arrangements, excess of loss reinsurance, adverse development covers, loss portfolio transfers of general liability books, or umbrella policies without exclusions may need to reevaluate their exposures accordingly and work with their cedents proactively.

Reflecting on the potential claim and legal consequences wrought by the possibilities connected with the CVA, on June 6, 2019, AM Best downgraded the Long-Term Issuer Credit Rating (ICR) to “a” from “a+” and affirmed the Financial Strength Rating (FSR) of A (Excellent) for New York Schools Insurance Reciprocal (NYSIR). The outlook for these credit ratings was revised to negative from stable. The downgrade of the Long-Term ICR reflected the new and emerging challenges associated with the company’s single-state orientation in New York and a customer profile seen as the target of the new state law. Despite the challenges related to the CVA, NYSIR’s underwriting and operating performance has been historically strong and the company’s management quality is considered superior to the industry. Loss control initiatives and the company’s conservative reserving approach are expected to have a positive impact on results in the long term, despite the company’s limited business profile and negative outlook brought on by the near-term uncertainty of the CVA’s impact on the company.

The CVA will likely have a more acute effect on New York-centric insurers that specialize in providing insurance covering sexual abuse or molestation claims. Insurers will face operational challenges locating exposures that go back decades, given the technology and data storage changes. AM Best will continue to monitor developments in legislation and litigation and continue its discussion with insurers and reinsurers on this developing issue.
Commentary Child Victims Act

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