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Defense Costs Dropped in 2014, While Claim Filings, Dismissal Rates, and Indemnity Dollars Remained Steady

Snapshot of Recent Trends in Asbestos Litigation: 2015 Update

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Each year, we conduct an annual review of asbestos-related liabilities reported in companies' Securities and Exchange Commission (SEC) filings. This information can assist companies in benchmarking their own data against trends observed for other defendants, which can help to forecast asbestos-related liabilities. Analyzing the 2014 data, we observed, on average, that dollars per claim remained high and filings have not yet begun to fall, although defense costs fell a dramatic 33%.

Specifically, we observed for companies, on average, that:

- After almost doubling in 2011, dollars per resolved claim have remained at these high levels;
- Filings have shown no decline in the last seven years, a finding that is perhaps inconsistent with predictions of epidemiological models;
- Dismissal rates remained steadily high;
- Although total indemnity payments remain within historical ranges, defense spending dropped substantially for the second year in a row, falling 33% last year after a 22% decline in 2013, for a cumulative decline of almost 50% over the two-year period;
- Reserves continued with the steady decline that began in 2010.

These trends point to a period of relative stability in the asbestos litigation environment, as filings, average dollars, and total indemnity spending remain steady. Falling defense costs may also be a reflection of this stability, as companies may need to spend less on developing legal strategies while continuing to manage existing litigation.

Last year, we noted that one source of uncertainty moving forward was the impact of Judge George Hodges' January 2014 decision in *In re Garlock Sealing Technologies, LLC*, the bankruptcy case that highlighted discrepancies in exposure evidence provided by claimants. Courts and legislatures are still wrestling with what information should be made available to defendants regarding potential claims against the asbestos Trusts, with defendants advocating for full disclosure. To date, we have observed no substantial changes in filing or settlement patterns. But given that defendants may not yet have access to data from the Trusts, it may be too soon to tell what the ultimate impact on settlement values and filings will be.

Methodology

This study represents our seventh annual assessment of trends in asbestos-related liabilities of asbestos defendants and extends our analysis one year to include 2014.

To analyze these trends, we compiled publicly available data from over 150 asbestos defendants' Form 10-K filings with the SEC, from 2001 through 2014. We tracked six key metrics related to asbestos liability²:

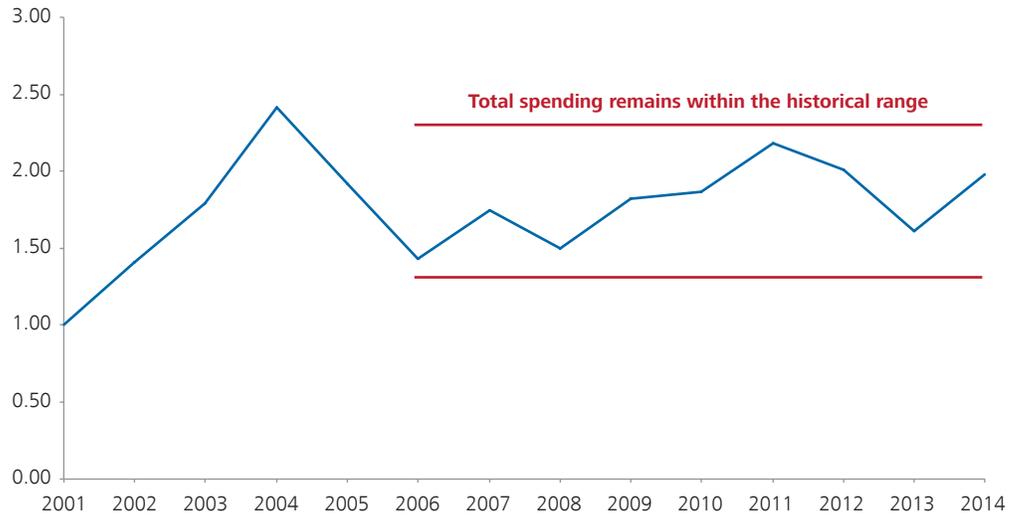
- *Total indemnity paid*: the aggregate amount a company pays to resolve claims each year;
- *Total defense paid*: the aggregate amount a company pays in legal fees and expenses each year;
- *Number of claims resolved*: how many claims a company closes each year either by settling or obtaining dismissals;
- *Average settlement paid per resolved claim*: the total indemnity paid divided by the number of claims resolved each year;
- *Percent of claims dismissed*: the fraction of claims a company closes without payment; and
- *Annual filings*: the number of new claims a company receives each year.

Additionally, for those firms reporting asbestos-related reserves, we tracked the average reserve amount.

Despite an Increase in 2014, Which Reversed a Decline in the Prior Year, Total Indemnity Payments Remain within the Historical Range

- In 2014, total indemnity payments rose 23% on average, reversing a decline in 2013.
- Since 2006, average total indemnity has ranged from 1.4 to 2.2 times 2001 levels, as annual averages have fluctuated with no clear upward or downward trend. The 2014 increase continues this pattern and remains within the historical range.

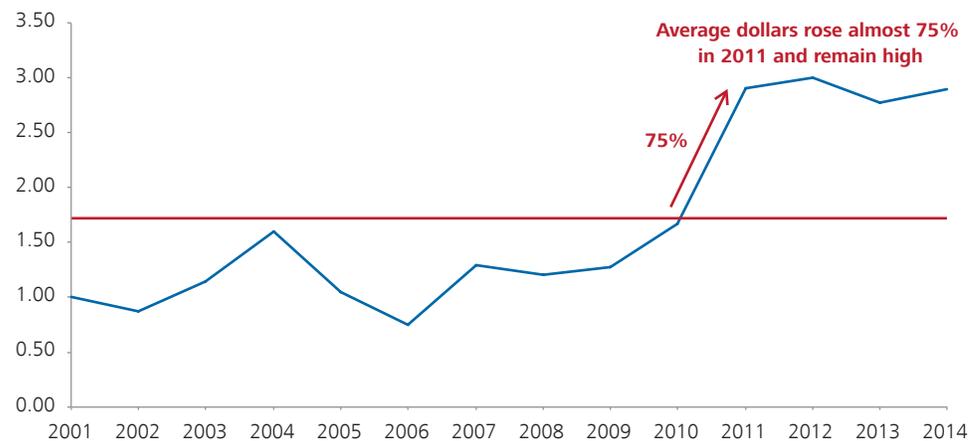
Figure 1. **Total Indemnity Payments Per Defendant**
Indexed to 2001



Average Dollars per Resolved Claim Remain at Post-2010 Elevated Levels

- 2014 saw a slight uptick in average dollars, reversing the small drop observed in 2013.
- The biggest change in average resolution values occurred in 2011 when dollars per claim rose approximately 75%, on average. Since then, values have remained at these higher levels, with 65% of companies reporting resolution values above their 2010 levels.

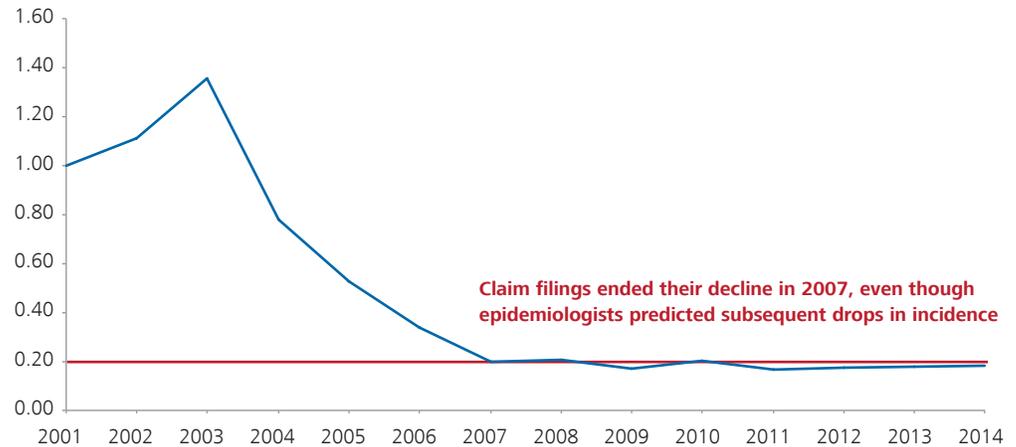
Figure 2. **Average Dollars Per Resolved Asbestos Claim**
Indexed to 2001



Filings Continue Their Plateau

- On average, filings in 2014 were unchanged from the prior year.
- After increasing in the early 2000s, annual filings declined mid-decade to only 20% of 2001 levels and have remained steady since.

Figure 3. **Average Number of Asbestos Claims**
Indexed to 2001

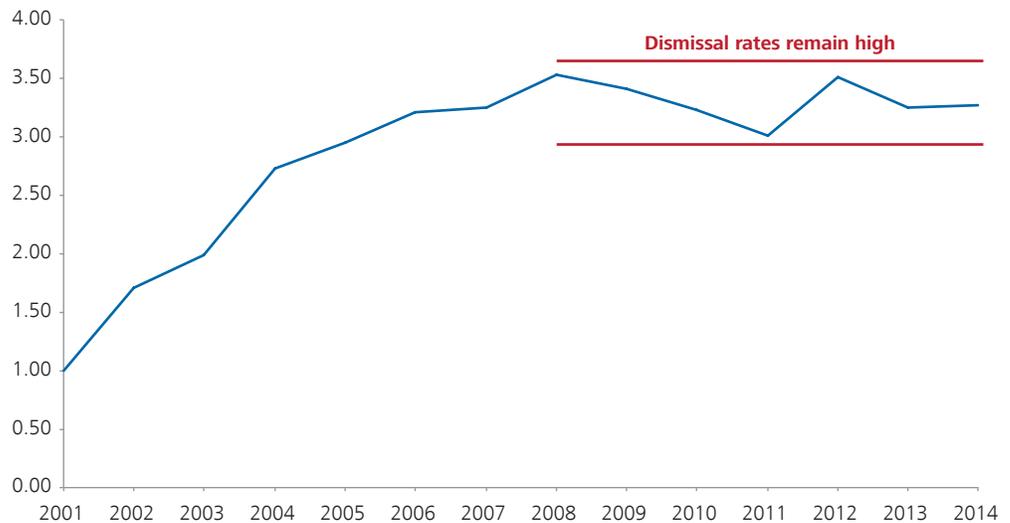


- As discussed in prior reports, this mid-decade decline followed Judge Janice Graham Jack’s decision in *In Re Silica Products Liability Litigation*, which questioned the medical documentation of non-malignant disease claimants. The drop in claim filings was likely a decline in non-malignant filings, as it was medical evidence related to these filings that was central to Judge Jack’s decision.
- Moreover, for companies that report the disease mix of their pending claims, this mix has been more heavily malignant compared to the early 2000s.
 - The malignant share of claims pending in 2014 was more than twice as high as the malignant share in earlier years.
 - For example, Honeywell, Duke, and Ingersoll Rand reported that 20% to 40% of their 2014 pending claims were malignant filings. In contrast, malignant filings for these firms comprised only 10% to 20% of pending claims prior to 2012, and 5% to 10% of pending claims prior to 2008.³
- Epidemiologists have predicted that the incidence of asbestos-related malignant diseases in an occupationally exposed population would begin to decline by the late 2000s.⁴ Such a decline is not detectable in this publicly available data, as the filings have remained constant. From this data source, it is difficult to unwind filing patterns by disease. Moreover, even for companies reporting the disease mix of their current claims, we do not have the breakdown of the type of malignant claims, and therefore cannot determine which type of cancer may be driving the filings. Anecdotally, however, there has been a discussion of the increase in lung cancer-related filings in several jurisdictions.

Dismissal Rates Remain High

- In 2014, dismissal rates increased slightly, on average, compared with 2013 rates.
- Over the 2002 through 2008 period, dismissal rates increased steadily, on average, before declining over the next three years. This declining trend stopped with the 2012 increase.

Figure 4. **Average Asbestos Claim Dismissal Rate**
Indexed to 2001

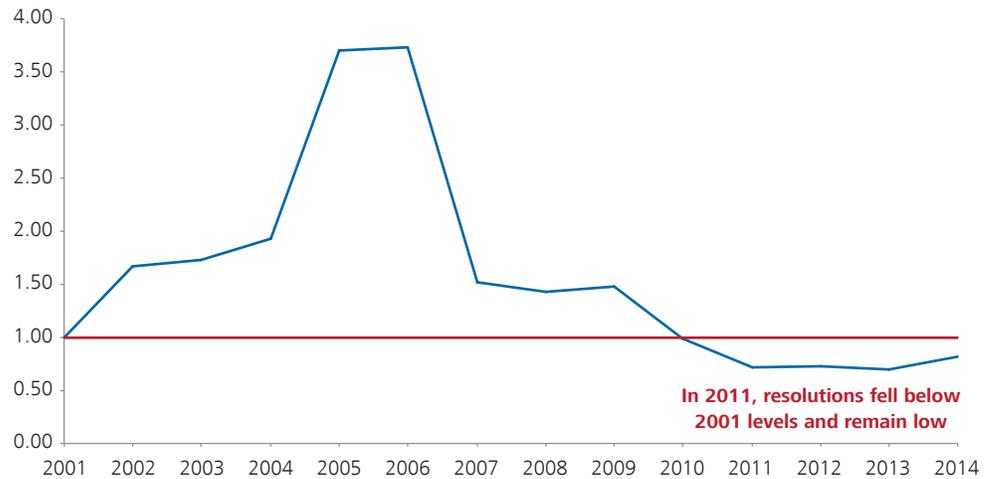


- As with claim filings, resolution values, and total settlement costs, dismissal rates appear to have stabilized, with some annual variability but without an upward or downward trend. Since 2008, average dismissal rates have ranged from 3.0 to 3.5 times 2001 levels. Companies continue to resolve most of their claims without payment, dismissing on average more than 85% of claims resolved.

Number of Claims Resolved Each Year Remains Constant

- The number of resolutions each year increased, on average, in the early 2000s, following a jump in annual filings in 2003. However, resolutions began falling in 2007 and returned to 2001 levels by 2010.
- Since 2010, the average number of resolutions has ranged from 70% to 80% of 2010 (and 2001) levels, with a small uptick in resolutions in 2014.

Figure 5. **Average Number of Resolved Asbestos Claims**
Indexed to 2001

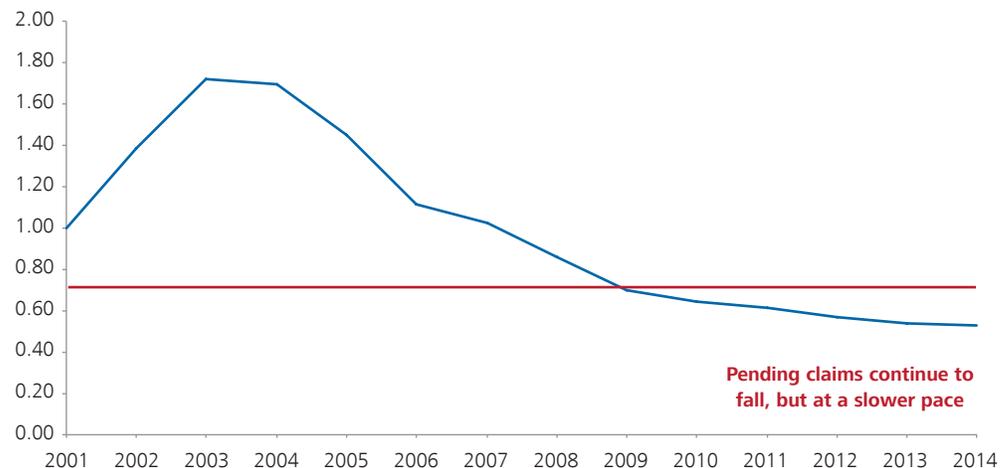


- As claim filings have stabilized (as noted above), we would expect that annual resolutions would also be fairly consistent year-over-year.

Pending Claims Continue to Fall

- In 2014, pending claims fell 2% on average, continuing a decline that began in 2004.
- After increasing during the early 2000s, the number of pending claims dropped sharply from 2005 through 2009. Since 2009, pending claims have continued to decline, but at a more gradual pace.
- Average claims pending in 2014 are 50% of 2001 levels.

Figure 6. **Average Number of Pending Asbestos Claims**
Indexed to 2001

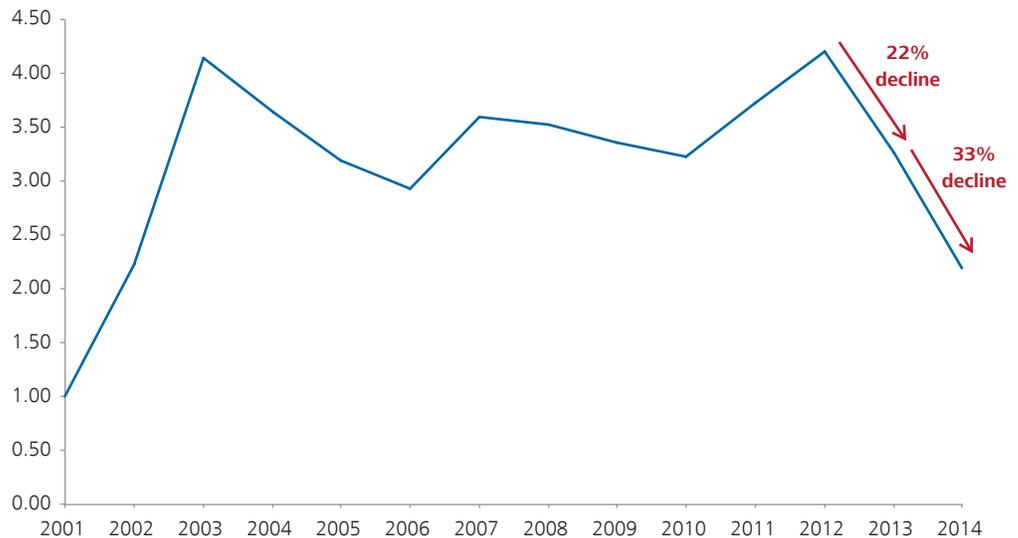


- As discussed above, based on observations for those companies that report disease information (most do not), the disease mix is likely more heavily malignant than in the early to mid-2000s.
- The shift in disease mix towards more malignant filings, if consistent across all defendants, suggests that the 2011 increase in average resolution values will likely persist in the future.

Defense Spending Dropped 33%, Deviating from Recent Trends

- Legal costs dropped in 2014, on average, for the second year—falling 33% in 2014 after dropping 22% in 2013, for a cumulative decline of almost 50% over the two-year period.

Figure 7. **Average Dollars Spent on Legal Costs to Resolve Asbestos Claims**
Indexed to 2001

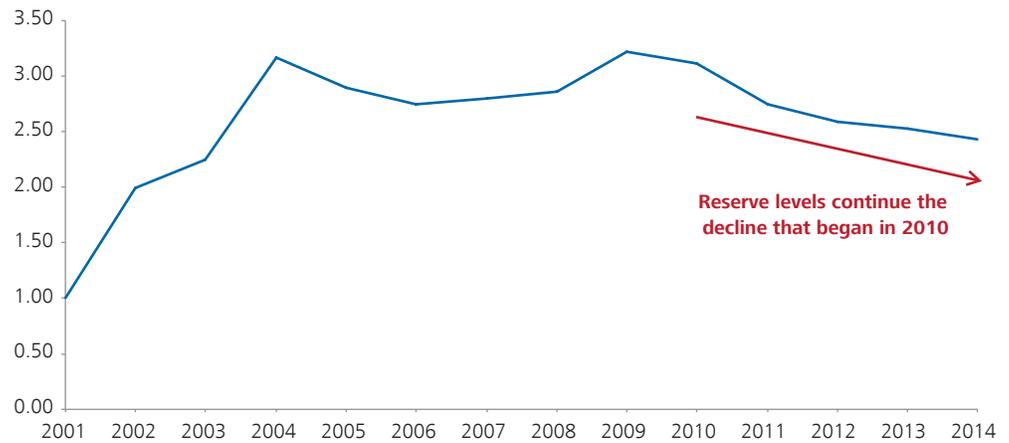


- For two-thirds of the firms reporting legal fees, defense costs in 2014 were equal to or less than average defense costs over the prior three years.
- The plateau in the mid-decade and recent drop in legal fees are both consistent with a stable litigation environment (as defendants may have already developed their legal strategies, and spending may be focused on day-to-day management of cases). However, it is too soon to determine whether the recent declines will continue.

Reserve Levels Continue to Decline

- In 2014, reserves declined 4%, on average, dropping for the fifth year in a row. Over 60% of companies reported reduced or unchanged reserves over the past year.

Figure 8. **Average Asbestos Reserves**
Indexed to 2001



- Companies reported reserves covering five to 50 years, with 70% reporting reserve periods of 20 years or fewer and 30% reporting reserve periods greater than 35 years. The median reserve period was 15 years.
- Given the fairly long periods over which companies are reserving, and the expectation that eventually annual liabilities will decline (as the potentially exposed workforce ages and dies of other causes), the falling reserve levels are another sign of a litigation environment that is not worsening for defendants.
 - For example, if a company maintains a 15-year reserve, then each year it will roll forward the reserve, reducing the reserve by payments made in the past year and increasing the reserve to incorporate forecasted payments in the new fifteenth year. Typically, the projected payments 15 years out are expected to be lower than payments in the past year. Unless a company forecasts worsening trends, its reserve would be expected to decline each year.

Summary of Trends Through 2014

- Results over 2014 are relatively unchanged from 2013—with aggregate settlement values falling within historical ranges, resolution values and dismissal rates remaining high, and filing levels remaining low. Moreover, the average number of pending claims has continued to decline. The only metric that differed from prior trends was the legal costs, which dropped, on average, for the second year. Together, these results point to a fairly stable litigation environment for defendants.

- One of the largest unknowns going forward continues to be the impact of the 2014 *Garlock* decision on solvent defendants. The decision may induce defendants to change their legal strategies and push for full disclosure of claimants' past and future claims against the Trusts. Additionally, courts and legislatures may open access to Trust information, as has been the case in several jurisdictions (e.g., Arizona, Ohio, Oklahoma, West Virginia, and Wisconsin).
- These changes may impact defendants' legal costs. If it becomes available, the additional exposure information—particularly in jurisdictions with substantial historical activity (California, Illinois, and New York)—may give defendants more leverage to obtain dismissals or put downward pressure on settlements. The resulting impact on filings is unknown.
- If these litigation changes come to fruition, defendants will need to reassess their forecast assumptions as well as any resulting impact on their reserve levels.

Endnotes

- ¹ The authors would like to thank Tanner Baker, Andrew Nguyen, Ryan Tang, and Yingtian Yang for their research. We also thank Dr. Stephanie Plancich for her comments and suggestions.
- ² Data from each firm's most recent Form 10-K were used whenever available. We included only data reported at the individual claim level for companies reporting at least two consecutive years in the period. The indexes shown below represent an average of trends observed at the company level. Each chart may contain different companies, depending on the data reported by each company, each year.

Data for prior years were updated if companies changed previously reported information. As a result, the graphs in the current update may differ from those in the previous update over the earlier period.
- ³ Honeywell reported its disease mix starting in 2002; Ingersoll Rand started in 2007; and Duke started in 2011.
- ⁴ See, e.g., W.J. Nicholson, G. Perkel, and I.J. Selikoff, "Occupational Exposure to Asbestos: Population at Risk and Projected Mortality – 1980-2030," *American Journal of Industrial Medicine*, 1982, pp. 3:259-311.

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