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The Myths of the Medical Malpractice Insurance "Crisis"

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In the recent debates concerning medical malpractice insurance rates nationwide, the following saying comes to mind: "In this world, there are liars, damned liars, and statistics." Insurance companies, and the doctors they insure, are at the forefront of a comprehensive push to establish California MICRA limits nationwide. Such groups have endless statistics to prove their points. They cite four-to-five-fold increases in rates for high-risk specialties as evidence of a tort system out of control. A commonly-cited fact is the malpractice insurance rate for obstetricians in Florida being $200,000 per year.1 These groups also cite the average jury award in Nevada for medical malpractice increasing from $40,000 to $200,000 in five years.2

Not to be left out of the battle, consumer groups and attorneys have their own statistics upon which to impale the other side. They cite the fact that California’s average cost of malpractice insurance is $7,200 per year,3 which is only $400 less than the national average.4 They cite to the "bath" insurance companies took on stock investments and the need to cover their losses as the reason the cost of malpractice insurance is what it is.

With all these statistics flying back and forth, the question is, where does the truth lie? This article will examine many of the claims being made by all sides to this debate and finish with a proposal that best addresses these issues.

EFFECT OF MICRA IN CALIFORNIA

A. What is MICRA?

Any discussion of national medical malpractice issues must start with California for the simple reason that California is the model touted by doctors, legislators, and insurance interests for use on a national scale.

In 1975, California instituted the limitations on recovery and fees in medical malpractice actions. The legislation is referred to as the Medical Injury Compensation Reform Act (MICRA).5 MICRA focused on four basic issues: time limitations,6 damages,7 attorney fees,8 and arbitration.9 MICRA did not, however, change the types of actions plaintiffs can bring against doctors. Stated another way, MICRA’s changes with respect to medical malpractice litigation were procedural and economic, not substantive.10

As part of MICRA, California Code of Civil Procedure section 1295 allows for periodic payments of future damages awarded at trial, which end if the plaintiff dies. In other words, total future damages are not based on a lump sum payment, but rather on the cheapest annuity the defendant can buy to pay the future payments. With a severely injured plaintiff, an annuity often can be purchased for a small fraction of the total award since all payments will end if the plaintiff dies.

The predominate changes, however, which tort deformers now seek to implement nationwide, involve the limitation on the damages recoverable and the reduction of attorneys fees. California Civil Code section 3333.2 applied a $250,000 cap on all non-economic damages (approximately $838,926 in 2002 dollars11).

B. How MICRA Affects Litigation in California

These changes in California have the following effect:

(1) The most seriously injured people are disproportionately affected by this legislation. Although insurers claim that MICRA-type limitations are needed to avoid "frivolous lawsuits," MICRA itself effects no substantive changes. Nothing whatsoever in MICRA prevents frivolous medical malpractice lawsuits. The only limitations are on suits that by definition have merit: e.g., a jury finds liability and awards in excess of $250,000 for general damages. But women, children and the elderly – the groups that traditionally have the most minimal economic damages – are the hardest hit by this limitation.

(2) Limitations on damages and attorneys fees make trials more likely. One statistic that most agree is accurate is that 70% of medical malpractice trials result in defense verdicts12 because such cases are difficult for plaintiffs to prove. This statistic alone makes trials more likely. When MICRA limitations are added to the picture, and a defendant knows its maximum exposure is substantially limited, that defendant is even more likely to roll the dice in court.

(3) These changes make it much more difficult for medical malpractice victims to get representation. With recovery substantially limited, and a limitation on the fees recoverable on those limited damages, MICRA’s effect is to direct attorneys toward other cases where these limitations do not apply. As any person who has suffered from malpractice would agree, finding representation in a medical malpractice case is very difficult.13 As one case has noted: "[T]he effect of limiting attorney fees is, quite intentionally, to discourage use of attorney time in prosecuting malpractice claims."14 Even insurers acknowledge that attorneys reject the vast majority of malpractice claims they see,15 a fact which was confirmed in Consumer Attorneys of California’s own internal member survey.

C. How MICRA Affects Insurance in California

1. How Do California’s Medical Malpractice Rates Compare to the National "Average"?

While the effect of MICRA on litigation is not really in dispute, the effect that MICRA has on malpractice insurance rates is hotly disputed. According to the Americans for Insurance Reform, a consumer oriented group, "[t]he 2000 average premium per doctor in California was only 8.2 percent below that of the nation ($7,200.61 vs. $7,843.75)."16 This figure is fairly strong evidence that California, overall, does not have rates that are much lower than the nation as a whole, despite the stringent damage limitations imposed by MICRA.

Insurance companies and doctors, however, refer to their own statistics that paint a much different picture. According to an article in the San Francisco Business Times:

In California, the base rates are cheap. A California obstetrics physician will pay between $35,000 and $40,000 a year. The same doctor in Pennsylvania, one of the highest cost states would pay between $80,000 and $120,000.17

Similar numbers are given explaining rate increases in Florida and Nevada where stories report that obstetricians in these states must pay between $100,000 to $200,000 for the same coverage.18 This is compared to a national "average" of approximately $56,500 for the same coverage for the same areas of practice.19 These numbers do show that certain high risk practices are much cheaper in California than in other geographic locations. This discrepancy is attributed to the MICRA caps in California by the insurance industry. However, this view is far too simplistic and likely wrong.

2. Effect of Proposition 103 on Malpractice Insurance

When analyzing the difference between rates in California and rates in certain pockets of this country, the effect of Proposition 103 must be considered. MICRA was introduced in 1975. All sides agree that for ten years following its enactment, rates in California increased quite substantially. The Foundation for Taxpayer and Consumer Rights reported recently that from 1975 until 1988 malpractice insurance rates in California tripled.20

In 1988, the voters of California enacted Proposition 103, which placed limits on the right of insurance companies to raise rates in California. Proposition 103 required insurance companies to seek approval from the state for increases and to document the reasons for those increases. Significantly, following this enactment malpractice insurance rates dropped 20% by 1991.21

Insurers, not surprisingly, claim that the drop in rates has nothing to do with Proposition 103, but rather with a series of California Supreme Court decisions in

1985 that affirmed the MICRA limitations, taking away any uncertainty on the issue. The Consumer Federation of America prepared a chart (Chart 1), which was cited in a March 5, 2003 New York Times article on the subject showing the premiums in constant 2001 dollars in relationship to payouts of medical malpractice claims in California in constant 2001 dollars.

The chart shows a clear strong upward spike in insurance rates following the passage of the MICRA limitations that took effect in 1975. Premiums then took a substantial rise again in the late 1980s. This chart also negates the insurance industry's argument that any Supreme Court decisions in 1985 affirming MICRA caused a reduction in insurance rates. As can be seen, the rates dramatically increased from 1985 until 1988, when California voters implemented Proposition 103. Significantly, this chart also demonstrates that the spikes in premiums do not relate to any spikes in payouts on malpractice claims.

INSURANCE CYCLES

The debate concerning malpractice insurance rates nationwide cannot be separated from the debate over insurance cycles nationally. Over the last three decades, the insurance industry has clearly experienced periods of "boom" and "bust" that have little or nothing to do with the number of claims filed. While a major catastrophe such as Hurricane Andrew in 1992 can cause a temporary dip in revenues, institutional changes play a much larger role in creating an "insurance crisis." During times of increased economic expansion, insurers are able to invest the premiums and enjoy a high rate of return on their investments, more than compensating for the payouts made. Additionally, because insurers can make money on their investments, it creates a "soft" market for insurance – insurers will reduce rates to attract new business in order to gain the premiums for investment.

However, as soon as the stock market goes south and interest rates drop dramatically, two things happen: (1) insurers can no longer reap large returns on their investments which means premiums have to rise; and (2) soft insurance markets end because the insurance companies must recover all losses almost solely through increased premiums.

The next chart (Chart 2) was prepared by the Consumer Federation of America, based on data from A.M. Best and Co. Aggregate Averages, 2001 edition. It tracks the highs and lows of profit in the insurance industry as a whole.

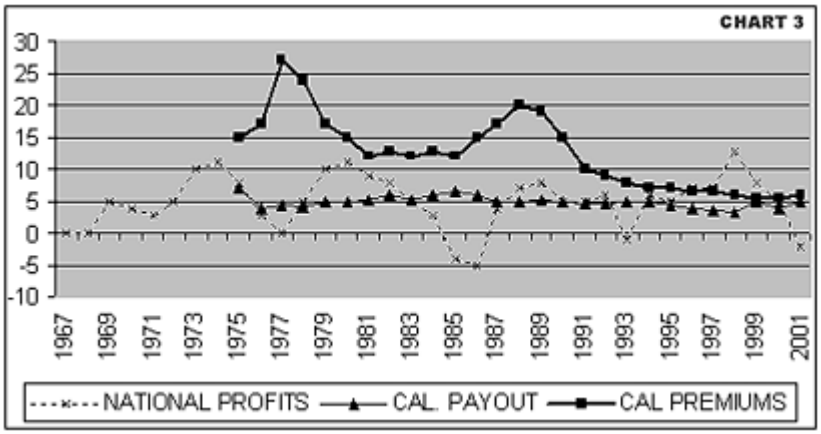
This chart shows the 10-year cycle of profitability with substantial lows in the late 60's, late 70's, late 80's and 2001.22 It is also important to note that this chart is

industry-wide, including all types of insurance. The current downturn of profitability affects all insurance sectors. According to the Council of Insurance Agents and Brokers (CIAB), the average increases in premiums for construction insurance are 46% nationwide. Umbrella Liability policies will rise 56% this year. Property insurance will rise 47%, with similar rises in all other types of insurance.23 Just ask any attorneys practicing in California how much their malpractice insurance has risen in the past year and they will relate similar increases.

When there is a nationwide downturn in profits, premiums rise. We are currently in a strong economic downturn that is right on schedule for the insurance industry. Rates are going up tremendously fast in all sectors of insurance.

COMPARISON OF CALIFORNIA WITH NATIONAL MODEL

The final chart (Chart 3) combines the first two charts to show how California fits into the national picture. The dotted line shows the national rate of return for insurance companies, the thin line shows the payouts of all California cases, and the thick line shows the cost of premiums in California.



While payouts have been consistent in California, based on 2001 dollars, rate increases for medical malpractice insurance followed the major dips in revenue in both 1977 and 1986. While there has been continued volatility since 1988 in the insurance market as a whole, California's medical malpractice rates are slowly dropping. Therefore, Proposition 103 appears to have a much greater effect on the rates than MICRA, which still allowed wild rate fluctuations. Given the foregoing analysis, some method must be in place to prevent, or at least reduce, the "boom or bust" mentality of the insurance industry as a whole. Such a proposal will be discussed in the final section of this article.

STATES WITH A MEDICAL MALPRACTICE INSURANCE "CRISIS"

The call for caps on damages is currently the loudest in a few states: Nevada, Pennsylvania, and Florida. While the national downturn in the insurance market undoubtedly affects these states, other factors are apparently at work and need to be examined. In each of these states, the main increases are in the "high risk" professions, such as obstetrics and neurosurgery. This is for the obvious reason that when things go wrong in these areas, people can be permanently and horribly injured for life. Nevada reported "skyrocketing malpractice premiums, some jumping to $200,000 annually from about $40,000."24 Most of the highest cost premiums were for the high-risk providers.25 Pennsylvania reported that obstetricians incurred between $80,000 and $120,000 in coverage costs.26 Florida also reports costs for such high-risk professions increasing up to $200,000 for obstetricians and up to $279,000 for neurosurgeons.27 No one can dispute that insurance costs at this level are prohibitive to most practitioners.

You might expect an increase in jury verdicts to justify an increase in rates; however, there is no evidence that jury verdicts in any of these states have increased four-fold in the last few years to match the four-fold increases in the insurance rates. In fact, in Florida the average payment for a medical malpractice claim is currently about $249,000.28 In current dollars, these payments have gone down approximately 14% since 1991 from a high of almost $300,000.29

These out-of-control increases in insurance costs must be taken in context with a national trend toward lower insurance rates in constant dollars. Dividing the total medical malpractice premiums by the number of doctors in America produces an interesting result. In constant 2000 dollars, the average premium in 1991 was $11,614. In 2000 that same premium was $7,843.30 It should also be noted that California’s average under the same method of accounting was $7,200 in 2000.31 Therefore, in the context of a national average, insurance rates have been dropping since 1991.

Taken together, this information shows a fairly constant declining average over time, but with certain geographic areas in our country, as well as certain medical practice areas, experiencing huge upward spikes that are out of line with the general trends. The question then is how to prevent wild gyrations in these pockets of the country without limiting all medical malpractice cases given no evidence of an insurance "crisis" but rather simply a ten-year insurance cycle downturn that is predictable and will end.

PROPOSAL BY THE CONSUMER FEDERATION OF AMERICA

In testifying before Congress, Travis Plunkett of the Consumer Federation of America presented a workable plan to address these concerns. First, he stated the need for a nationwide review of insurance rate increases similar to that found in Proposition 103. Increases of 50% to 70% in present dollars cannot ever be justified on the basis of increased payouts in litigation because the payout numbers

remain relatively constant over time adjusted into present dollars. Such oversight will likely prevent huge gouging increases in areas like Florida, Pennsylvania, and Nevada.

Mr. Plunkett also realizes that certain high-risk professions require special attention. The risks associated with performing obstetrical or neurosurgical procedures are undeniably great. One error can lead to many millions of dollars in economic damages alone. However, our society needs and must encourage physicians to work in these areas. Mr. Plunkett's suggestion is to create a national reinsurance vehicle whereby a fixed amount of all insurance proceeds is placed into reinsurance for catastrophic claims (for example anything over $2,000,000). This premium for reinsurance would not fluctuate over time. In other words, this reinsurance must be paid into during the good as well as the bad economic times. The concept is to create a cushion immune from industry cycles. In good times, the reinsurance will rise to protect against future losses. When future losses occur, it will be there to cover payments for claims.

Another benefit of such a system is that it spreads the cost of high-risk professions among all doctors in a small amount. At the same time, it also protects all doctors from catastrophic claims. While not nearly as exciting as loudly complaining about out-of-control jury awards, this suggestion has a lot of merit.

CONCLUSION

The foregoing analysis shows that a boom-and-bust cycle coupled with a lack of oversight in insurance rate increases are likely responsible for huge increases in some high-risk medical professions' insurance rates in some states. All types of insurance are experiencing dramatic rises in costs that have nothing to do with paid claims, but rather with a "bust" investment cycle. When these "bust" cycles exist, unregulated insurance companies will increase rates dramatically regardless of claims paid. As California proves, oversight of these practices, such as accomplished with Proposition 103, will go much farther in preventing these problems than limitations on damages recoverable for the worst injuries due to medical malpractice.

1 Dade County Medical Association (DCMA), available at http://www.miamimed.com (last visited on 3/19/03) (including under "Articles of Interest" an article by staff writer Ken Lewis, entitled "Rising med insurance rates creates local crisis").

2 Joelle Babula, "Legislative Review: Tort Reform Studied, Lawmakers look at medical malpractice insurance crisis," Las Vegas Review Journal, May 14, 2002, available at http://www.reviewjournal.com.

3 This figure averages total cost of all premiums divided by total number of doctors. This number includes all doctors whether they are covered by insurance or not. The actual cost of any particular policy is closer to an average of $40,000. See Americans for Insurance Reform Fact Sheet [hereinafter Americans for Insurance Reform], "California Restrictions On Malpractice Victims Have Not Affected Malpractice Premiums," available at http://www.
insurance-reform.org/issues/carestrictions.
html (last visited on 3/19/03).

4 Americans For insurance Reform, supra, note 3.

5 See Stats. 1975, Second Ex. Sess., ch. 1, § 25.5, p. 3970.

6 See Cal. Code Civ. Proc., §§ 340.5, 364-365.

7 See Cal. Civ. Code, §§ 3333.1-3333.2; Code Civ. Proc., § 667.7.

8 See Cal. Bus. & Prof. Code, § 6146.

9 See Cal. Code Civ. Proc., § 1295.

10 Myers v. Quesenberry (1983) 144 Cal.App.3d 888, 893.

11 Charles Ornstein, "Verdict Not In on Malpractice Caps," LA Times, Aug. 3, 2002.

12 Examining the Work of State Courts, A National Perspective from the Court Statistics Project (2001), p. 94.

13 Ornstein, supra, note 11.

14 Roa v. Lodi Medical Group, Inc. (1985) 37 Cal.3d 920, fn 9, quoting Contingent Fees, at 215.

15 See, e.g., Malpractice Digest, "Criteria Lawyers Use in Accepting or Rejecting Medical Malpractice Cases," Sept./Oct. 1978, at 2. (published by St. Paul Fire and Marine Insurance Company for its medical liability insurance policyholders).

16 Americans for Insurance Reform, supra, note 3.

17 Brendan Doherty, "California’s low malpractice rates are no medical error for docs," SF Business Times, Oct. 12, 2001.

18 "Over 800 doctors walk out over malpractice insurance costs" ABC action news report, January 27, 2003; Babula, supra, note 2; Ornstein, supra, note 11.

19 Richard Oppel, Jr., "With a New Push, Bush Enters Fray Over Malpractice," NY Times, Jan. 17, 2003.

20 Scott Finn, "California Caps or Proposition 103," Charleston Gazette Mail (Jan. 19, 2003).

21 Finn, supra, note 20.

22 The low in 1992 is attributed to large losses as a result of Hurricane Andrew, and not cyclical features.

23 Exhibit A to the testimony of Travis Plunkett [hereinafter Plunkett testimony], Legislative Director for the Consumer Federation of America before the subcommittee on Health, June 17, 2002 (citing a 4th Quarter 2001 Survey released Jan. 2002).

24 Joelle Babula, Legislative Review, supra, note 2.

25 Id.

26 Doherty, supra, note 17.

27 Dade County Medical Association, supra, note 1.

28 2001 Florida Dept. of Insurance Closed Claim Data.

29 Id.

30 Plunkett Testimony, supra, note 23.

31 Americans For Insurance Reform, supra, note 3.

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