



February 27, 2003

Doctors Leaving their Practices: the Medical Liability Crisis

(This is the second in a series of RPC papers focusing on frivolous lawsuits and their impact on health care providers and the patients they serve.)

Doctors and the patients they serve face a new crisis as more and more medical liability insurers deem the practice of medicine an uninsurable risk. With the growing number of jury awards in excess of \$1 million,¹ many insurance carriers are evaluating whether they can continue underwriting physicians and other health care professionals for liability claims. In some cases, insurers have exited the medical liability insurance market entirely; others have withheld renewal of certain policies; and others have raised premium rates dramatically. The result: patients in many communities now are being deprived access to crucial medical care as hospitals, obstetricians, trauma surgeons, and other providers are being forced to curtail or eliminate services.²

Republicans are committed to solving this crisis by controlling frivolous lawsuits and ensuring patients have access to vital medical services. On January 28, President Bush called on Congress to protect America's patients, doctors and hospitals from the staggering costs of runaway lawsuits. On February 11, the Senate Committee on the Judiciary and the Committee on Health, Education, Labor and Pensions held a joint hearing, and now are working on bipartisan legislation to address this problem. The House of Representatives also is expected to begin consideration of medical liability legislation in early March.

The Problem: Increased Liability Costs, Not Poor Investment Decisions

Medical liability insurance premiums have skyrocketed because of the growing amount of excessive litigation and related costs, not poor management as some allege. While today's medical liability crisis is reminiscent of the 1970s, one significant difference is the increase in large jury awards. According to the Physician Insurance Association of America (PIAA), it is the amount paid per claim and its unpredictable size that brings new challenges for the liability insurance system. Recent PIAA data

¹Physician Insurance Association of America Data Sharing Project, May 2002.

²First-hand stories are included in "Confronting the New Health Care Crisis: Improving Health Care Quality and Lowering Costs by Fixing Our Medical Liability System," U.S. Department of Health and Human Services, July 24, 2002.

shows a four-fold increase in the percentage of jury awards in excess of \$1 million between 1991 and 2002, as well as an increase in the average malpractice indemnity payment (awarded by jurors or settled out of court).³

Trend analysis shows a deteriorating financial picture for the medical liability insurance industry *due to the rapidly rising cost of medical liability claims*. For every premium dollar collected in 2001, the industry incurred \$1.53 in losses, that is the dollars set aside to pay judgments and settlements for claims filed. Ten years earlier, for every premium dollar collected, the loss was \$1.03.⁴ This is a clear sign that claims payments for judgments and settlements are rising faster than incoming premium payments.

A recent report released by Tillinghast-Towers Perrin, an actuarial firm, found similar liability-related losses, leading to a 15-percent reduction of medical underwriting capacity from the marketplace over the past three years.⁵ Those insurers who left the medical underwriting market include St. Paul Companies (formerly the largest medical liability carrier in the United States), PHICO, Frontier Insurance Group, Doctors Insurance Reciprocal, and MIXX (except for policies issued in New Jersey). As a result, patients are finding it increasingly difficult to obtain affordable quality health care, and those who can afford it are paying more in the form of costlier health insurance.

The Insurance Debate: Myth vs. Fact

Opponents of federal medical litigation reform argue that the legal system is not to be blamed for rising premiums. Instead, they prefer to perpetuate myths: that poor investment decisions and inadequate regulation of insurers are the primary factors for increased liability premiums.⁶

Data from the National Association of Insurance Commissioners (NAIC) disproves the myth that investment decisions are precipitants in the crisis. NAIC data indicate that stock market investments remained fairly constant over the past five years for medical liability insurers, representing just 9 percent of their investment portfolio in 2001.⁷ That 9 percent is considerably smaller than the equity allocations for other insurance sectors, such as home and farm, property and casualty, or product liability. Rather, the majority of investment assets for malpractice carriers are in more conservative fixed-income instruments such as treasury, municipal, and corporate bonds which have offset declining stock market values in recent years.

³PIAA Data Sharing Project, May 2002.

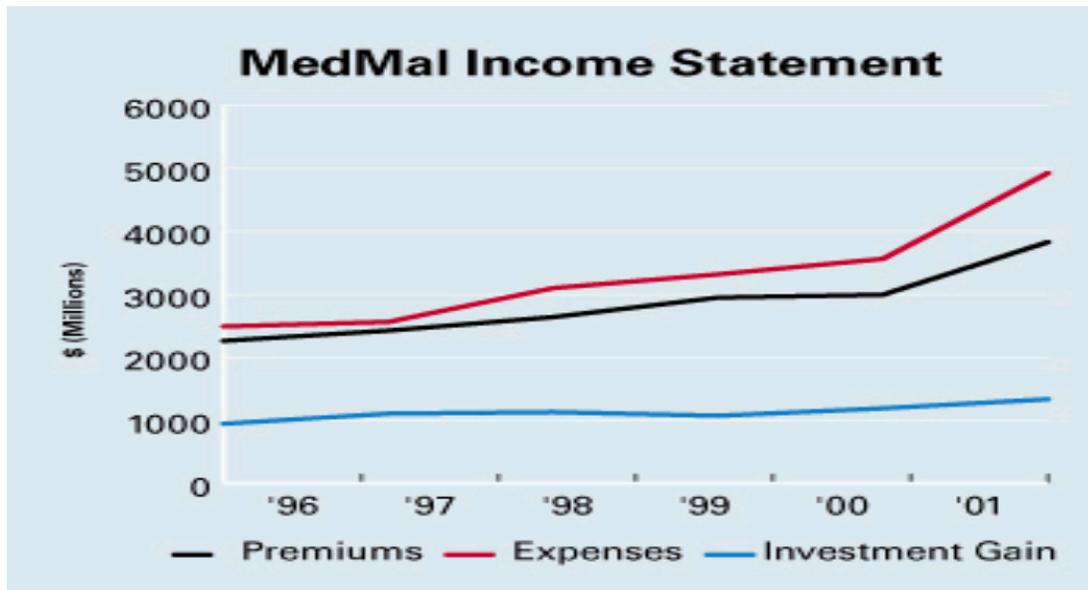
⁴"Medical Malpractice, Combined Ratio," AM Best.

⁵"A New Crisis for the Med Mal Market?" Tillinghast-Towers Perrin, February 11, 2003.

⁶"Myths and Facts About Medical Malpractice," Democratic Policy Committee, January 16, 2003.

⁷"Did Investments Affect Medical Malpractice Premiums?" Brown Brothers Harriman Insurance Asset Management Group, January 2003.

In fact, the medical liability insurance market has seen a slight overall investment gain, as demonstrated in the following chart from Brown Brothers Harriman, an insurance investment research company. In reviewing income statements for the industry, analysts confirmed that investments did not precipitate the current crisis; rather, the problem is caused by a significant increase in claims payments for judgments and settlements.⁸ The chart further confirms the correlation between liability premium rate increases and the growing trend of medical liability awards as previously discussed.



Moreover, even if medical liability insurers had a higher degree of exposure to the stock market, state insurance regulations prohibit insurers from recouping previous investment losses. For instance, during a hearing before the Governor’s Task Force on Professional Liability Insurance, Florida insurance regulators testified that if carriers lost money in the stock market, those losses would be paid from insurance company surplus funds, not from policyholders’ rates. State and national actuary standards “prohibit carriers from recouping losses since premium rates are developed prospectively projecting future underwriting losses.”⁹ In short, it is the increase in runaway medical litigation expenses driving today’s premium rate prices.

A second myth put forth by opponents is that insurance companies are collectively engaged in anti-competitive behavior through various forms of “price-fixing, bid rigging and market allocations,” and,

⁸“A Note on Investment Income of Medical Malpractice Companies,” Brown Brothers Harriman Insurance Asset Management Group, February 2003.

⁹Testimony before the Governor’s Task Force on Professional Liability Insurance by Steve Rodenberry, Florida Department of Financial Services, Office of Insurance Regulation, January 16, 2003.

thereby, need to be regulated by federal antitrust laws under the McCarran-Ferguson Act.¹⁰ Opponents of reform choose to ignore the fact that insurance companies are required by state law to justify their rates based on sound actuarial principles, preventing rates from becoming overly excessive, inadequate, or unfairly discriminatory.

A recent NAIC letter further confirmed that states have the ability to reject or modify rates, based on the standard that:

“No insurer shall agree with any other insurer or with an advisory organization to mandate use of any rate, prospective loss cost, rating plan, rating schedule, rating rule, policy or bond form, rate classification, rate territory, underwriting rule, survey, inspection or similar material, except as needed to facilitate the reporting of statistics to advisory organizations, statistical agents or [state insurance] commissioner.”¹¹

Thus, opponents’ assertion that insurers need new, federal regulatory oversight is unwarranted.

Solutions: Creating a Stable Medical Liability Market

Future papers will discuss specific solutions to the frivolous lawsuit crisis; meanwhile, as Congress considers reform, it should look at models like California’s Medical Injury Compensation Reform Act of 1975 (MICRA) as one example of the type of medical liability reform it may wish to adopt. The MICRA law includes a number of measures that have resulted in a more stable medical liability market that have kept liability premiums at a reasonable level. For instance, premiums in California rose at a much slower rate than premiums throughout the rest of the country during the past 25 years (167 percent vs. 505 percent.)¹² Lower premiums, in turn, have saved California consumers and taxpayers approximately \$5.8 billion per year in total health care expenses.¹³

One of the key ingredients to California’s success is the inclusion of a cap on non-economic damages. The MICRA law sets a sensible limit on non-economic damages at \$250,000. A 1998 study concludes that such a cap “discourages individuals with weak and marginal claims from filing suit without significantly reducing the number of individuals with strong claims that find it in their interest to pursue litigation.”¹⁴ The MICRA law also contains a number of other reforms, including: 1) a requirement that

¹⁰“Dear Colleague” letter by Senators Leahy, Kennedy, Durbin and Edwards, seeking cosponsors to the Medical Malpractice Insurance Antitrust Act of 2003, January 23, 2003.

¹¹Letter to Chairman Judd Gregg, Committee on Health, Education, Labor and Pensions, from the National Association of Insurance Commissioners, February 7, 2003.

¹²“Confronting the New Health Crisis.” endnote 69.

¹³“California MICRA Reforms: How Would A Higher Cap on Non-Economic Damages Affect the Cost of and Access to Health Care,” LEGG, Inc., Fall 1998.

¹⁴“California MICRA Reforms.”

lawsuits be filed within three years from the date of injury (with exceptions for cases concerning minors); and 2) a requirement that punitive awards be reserved for cases where there is clear and convincing evidence that the defendant acted with malicious intent or deliberately failed to avoid unnecessary injury to the patient.

Most importantly, the California law protects the right to go to court for those patients who have been wrongly injured. While MICRA's reforms have helped reduce the state's medical liability premiums, creating a more stable health care market for its residents, patients still have the ability to receive full compensation for economic losses such as wages, medical bills, rehabilitation and custodial care.

Keeping these protections in place, as well as setting sensible limits on unreasonable awards, will be an important first step toward improving access to quality medical care while making health care more affordable for patients and their families. As the medical liability debate begins, it is important to separate the myths – like poor management practices – from the real reason: runaway lawsuits. Addressing medical litigation reform is the surest way to reduce losses, control costs, and help doctors and hospitals continue to provide critical care.

RPC Contact: Diane Major, 224-2946