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Final Comment: Unintended Consequences of New York Structured Settlement Laws

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In our original paper, "The Unintended Consequences of Tort Reform: Rent Seeking in New York State's Structured Settlements Statutes" (2000; henceforth SS) and the follow-up response along with Frederick Floss (2002; henceforth SSF) the operative words are "unintended consequences." There does not appear to be any disagreement between Thomas Ireland in his current comment and Anthony Riccardi (2001) or us as to the intention of the original 50-A and 50-B legislation. The provisions to New York law were made in an attempt to reduce litigation costs under the spirit of tort reform that was sweeping the nation in the 1980's. Originally we stated

> State tort reforms may have unintended consequences, in particular, overcompensating plaintiffs *relative to the true present value of future damages*. [emphasis added] Such reforms may result in an increase, rather than a decrease in litigation. (SS, 2000, p. 30)

From the beginning SS clearly define a benchmark for what constitutes overcompensation: the present value of the actual loss stream. The SS paper deals with the unintended consequences of the law. Furthermore, we have never failed to mention the intended consequences of the law that work against plaintiff overcompensation:

> While the structure of 50-B contains several pro-plaintiff provisions, there are provisions of 50-B that benefit the defendant as well.[1] Riccardi (1996) discusses how terminating the payment for non-economic losses upon the death of creditor reduces the value of the structured judgment to the plaintiff. Additionally, 50-B further restricts the collateral source rule and permits offsets against future plaintiff recoveries. (SS, 2000, p. 32)

We reiterate this point in our later comment as well (SSF, 2002, p. 306). Ireland suggests (2004, p. 299) that we ignore these issues and that he for the very first time raises the issue of the collateral source rule as offsets (p. 302) This is not correct as the above quote clearly shows.

The purpose of the original SS paper is to show mathematically how the unintended consequences arise from the structure of damage awards mandated

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[1]The latest case on this issue is *Bryant* (1999) where Chief Judge Kaye discusses how defendants benefit by "paying a judgment in periodic installments..." She also discusses how stopping certain payments upon death of the plaintiff may also benefit the defendant.

under the law. As stated above there may be offsets that negate the bias (we call it a pro-plaintiff bias) in part or totally, but the bias (prior to any offsets) is a mathematical certainty.[2] Ireland suggests (pp. 299-300) that there are two reasons causing the overcompensation relative to the true present value, however SS clearly show how four features of 50-B *may* cause the overcompensation. In summary they are:

(1) The $250,000 lump sum payment,
(2) smoothing the future loss stream over the expected worklife,
(3) 4% *additur* on top of any testimony about inflation, and
(4) averaging the pain and suffering award over a maximum 10-year period.

Thus, before any considerations of life-contingency or the collateral source rule are made, we have a mandated structure that inflates the damage award relative to the present value of the actual loss stream. This has been and continues to be our key premise.

As to the concept of rent seeking, we again (SSF, p. 309) suggest the reader examine Osborne (2002), Farmer and Pecorino (1999), Rubin, Curran and Curran (2001) and Parisi (2002). Clearly, we do not agree with Ireland as to the concept of rent seeking in the litigation process and the readers can decide for themselves.[3]

Ireland (2004) raises concerns over the lack of empirical evidence, noting that "….no empirical evidence was provided by SS or SSF to show that the present value of average damages awards in tort actions in New York were any higher than in any other states." (p. 300) At no time do we claim that average damage awards have risen in New York State when compared to the rest of the nation. We clearly define overcompensation as the difference between the 50-B structure and the present value of the actual loss stream. Not only are average damage awards not the issue in our original paper, but we are clear that relying only on damage awards to make conclusions of this nature is misleading. In addressing empirical research we said the following:

> Empirical research on the affect of 50-B on tort filings will clarify whether these reforms have actually increased the cost of litigation. However, such research would require data on pre- and post-

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[2]It is important for the reader to know that this entire debate only affects a very small number of cases. First the case has to go to trial. Then the plaintiff has to win and an award has to be made. The award for future damages must be more than $250,000, and then the litigants must not be able to negotiate an agreement thus requiring the purchasing of the annuity. Consequently, not many cases actually go through a 50-B hearing where an annuity is actually purchased.

[3]In the traditional labor economics literature (Ehrenberg and Smith, 2003, p. 50), economic rent is the amount that an individual's wage exceeds his reservation wage. If individual's own wage does not exceed the reservation wage then there is no economic rent. When an economist testifies to lost income, that income is *at least* equal to a plaintiff's reservation wage, given that plaintiff was in the labor force at the time of injury or death. Thus if 50-B mandates a structure that results in an economic damage award that is larger than the present value of actual economic damages, then this difference can be considered economic rent. Plaintiffs seeking to capitalize on this structure to maximize damage awards are engaging in rent-seeking behavior.

> trial settlements. Much of that data is proprietary and thus unavailable, and any subset of available data may not be representative. (SS, 2000, p. 43)

Ireland also suggests that the focus of the SSF argument emphasizes losses to younger persons in looking at damage awards: "For example, they dismiss life contingent aspects of pain and suffering damages by assuming that these injuries were to a younger person." (p. 301)

However, we only refer to a person living longer than the 10-year maximum for pain and suffering. This could be a person at 55 living past the age of 65, or a person at 62 living beyond age 72. Nowhere do we attribute this to only a younger person nor do we even mention a younger person.

The main contention we have with both Ireland's current comment and Riccardi's (2001) reply is the focus on mortality adjustments to lower the present value of a damage award. The fact remains that during a 50-B hearing (which is independent of a collateral source rule hearing) the economist is not allowed by law (see SSF, p. 307) to use life contingent mortality adjustments. Both *Rodgers v. 72nd Street Associates* and *Desiderio* v. *Och* (also cited in SSF) forbid these types of mortality adjustments and we do not see any case law cited by Ireland or Riccardi to contradict this.

We believe the real difference between Riccardi, Ireland and ourselves is how an economist is used during the 50-B hearing itself and the actual purchasing and pricing of an annuity from insurance companies. An annuity must be purchased after a 50-B hearing, unless both sides agree to another type of payment plan. It is during the purchasing of the annuity that insurance companies, when costing out the annuity, will take the life contingent issues into account. This is why the courts in *Lieberman v. Perez-Veridiano* and *Molinari v. City of New York* urge the parties to shop the annuity around to obtain the best price. The shopping for an annuity to the specifications of the structure is not part of the 50-B process. Purchasing a life insurance policy, equal to all or some prorated portion of the non-economic damages solves the problem of a plaintiff dying before his life expectancy. An economist with the proper actuary skills can become active in advising attorneys during this shopping process. However, this is not part of the 50-B hearing per se and unless Ireland or Riccardi can cite cases that allow an economist to take life contingency into account during the 50-B hearing, the rulings by courts that disallow it continue to hold.

Ireland also introduces the concept of household services as a non-pecuniary award for damages and claims that "SS and SSF have generally ignored the life contingent nature of how damages are awarded for household services...." (p. 299) In New York State household services are considered economic damages and thus will continue upon the death of the plaintiff. There is no life contingent nature of lost household services. The appellate division of the Supreme Court of New York in *Edbauer v. Board of Education of North Tonawanda City School District* specifically says "plaintiff's loss of household services will not cease upon the death of plaintiff." (p. 1002)

Ireland also suggests that we ignored the life contingent nature of pain and suffering. A significant amount of space in SS and SSF is devoted to the actual legislation limits on pain and suffering awards to a 10-year payout, even if the jury stipulates a longer payout. The intent of this truncation was to offset the life contingent nature of pain and suffering awards. In fact, this limitation to an arbitrary 10 years in most cases over-adjusts for life contingency and creates a pro-plaintiff not pro-defense bias.

Ireland also suggests that SS and SSF ignore attorney fees in our estimates of overcompensation. The entire 50-B process is to determine attorney fees so it would be impossible to ignore them. Nevertheless, our definition of overcompensation (50-B relative to present value) does not consider disbursements of any type. Jury verdicts, not jury-verdicts-net-disbursements, are what are usually reported. Nevertheless, in SS we discussed how attorneys will report the gross amount of an award versus the discounted amount.

The collateral source rule in New York is very complicated and could be a research project itself. In both SS and SSF we mentioned the offsetting aspects of this rule but this rule is not the focus of the original paper.

SS dealt with Civil Practice Law & Rules (CPLR 5041-5049 and 5031-5039) articles 50(a) and 50(b). We are unsure what Riccardi's current comment on CPLR 4545 has to do with SS or SSF beyond the offset we already discussed.

The collateral source rule and any subsequent collateral source hearings (which are independent of a 50-B hearing) are very complex. New York first dealt with this issue with regard to the perceived medical malpractice crisis in 1975. *Oden v. Chemung County* has an excellent review of the legislative history of collateral source rules in New York. It also discusses how the collateral source must correspond only to the specific economic damages awarded by the jury, not the aggregate economic damage. Thus, if the jury does not award damages for lost pensions but awards damages of $1 million for lost earnings and the plaintiff receives a pension for $1 million (that would normally be considered a collateral source) there is no offset. (*See also Hayes v. Normandie.)* *Shue v. Red Creek Central School District*, further supports this:

> The damages awarded for economic loss in the instant case, however, compensated plaintiff and the children not only for lost earnings, but also for loss of household services and parental guidance resulting from decedent's death. Absent an itemized verdict specifying the amount assigned to each element of loss, there is no direct correspondence between the award for economic loss and the Social Security survivor benefits to which plaintiff and the children are entitled. (pp. 900-901)

As the above discussion indicates the collateral source rule in New York is very complicated and could be a research project itself. In both SS and SSF we mentioned the offsetting aspects of this rule but this rule is not the focus of the original paper.

Riccardi correctly points out other changes to medical, dental or podiatric malpractice actions commenced on or after July 25, 2003. This change was discussed on page 303 in SSF. For a detailed discussion of these changes see Moore and Gaier (2003a, 2003b)

A substantial amount of disagreement between Ireland, Riccardi, and us appears to stem from a basic misunderstanding of the original SS premise: that NYS law mandated a structure that distorts the present value of the loss stream and these distortions, which may or may not be offset by other features, lead to inefficiencies and needless complexity. We continue to hold that good law should not introduce such distortions. Empirical research has the potential to shed much light on the actual consequences of 50-B, intended or not. However, the distortion exists as a matter of law in the structure mandated by 50-B, regardless of data on actual damage awards, which themselves are a small and non-representative sample of tort cases. The real disagreement between authors centers on mortality adjustments. While both Ireland and Riccardi seem to suggest these adjustments are necessary for determining a discount rate, the courts have thus far disallowed these adjustments.

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