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Analysis of Medical Malpractice Reforms for the Insurance Division of the State of Hawaii

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EXECUTIVE SUMMARY

The Insurance Division of the State of Hawaii requested an analysis of the typical reforms of medical liability laws and those reforms' estimated impact on malpractice insurance premiums in Hawaii. Hawaii has very limited data in the area of medical malpractice insurance, and therefore it is necessary to consider comparable data from other jurisdictions to calculate an estimate of the effects of medical liability reforms in Hawaii. Based on an analysis of facts and data from Hawaii and other states, the typical medical liability reforms would result in reductions in premiums of 12 to 18%.

ANALYSIS

As the Hawaii Legislature witnessed during its motor vehicle insurance reforms of the mid-1990's, liability reforms can result in substantial decreases in the actuarially appropriate rates to be charged for the affected coverage. The Hawaii Legislature initially was confronted with this concept in the mid-1980's when liability reforms were passed, including mandatory reductions in the liability rates that were on file with the Insurance Division at the time the legislation passed. When liability insurance reform was addressed in the mid-1980's, that legislation excluded medical malpractice writers from the mandated rate reductions. During its 2007 session, the Hawaii Legislature requested that the Insurance Division provide an actuarial analysis of the rate-level effects that are expected to result from the passage of medical liability reforms applicable to Hawaii medical malpractice insurance.

Since it does not collect the actuarial data necessary to make such a determination, the Insurance Division sent a request to Hawaii's medical malpractice insurance providers.

Specifically, the request incorporated a series of medical liability reform measures that had been successful in other states, and asked for the insurer's actuarial determination of the reductions in loss costs that would result from the passage of such reforms in Hawaii. The request for actuarial pricing included the following reform measures enacted in Texas.

To combat the rising costs associated with medical malpractice insurance, several states are currently exploring ways in which to contain these costs which can affect all citizens in a given jurisdiction. Most notably, Texas has recently enacted several tort reform measures, including the following:

1) **NON-ECONOMIC DAMAGE CAP:**
Texas law now establishes a $750,000 stacked cap for non-economic damages in a health care lawsuit. The capped figure changes depending upon the variety of defendants in a suit. Physicians are capped at $250,000 exposure for non-economic damages. Hospitals have a $250,000 cap and an additional $250,000 non-economic damage cap applies if a second, unrelated hospital or health care institution is named in the suit. The cap is applied on a per claimant basis with no exceptions and no adjustment for inflation. Past and future medical bills, lost wages, custodial care and prejudgment interest remain uncapped.

2) **PERIODIC PAYMENTS**:
Texas law now requires periodic payment for future medical costs greater than $100,000 and gives the judge the option of allowing periodic payment for other future damages.

3) **APPEAL BONDS**:
In the past, appeal bonds had to be purchased for the full amount of the judgment against defendants plus two years post-judgment interest at 10 percent per year. That made the option of appealing jury awards prohibitive. The new law excludes the requirement to bond any punitive damage portion of the judgment and caps the amount required for bonding to $25 million or 50 percent of the defendant's net worth.

4) **DEATH CAP CHANGES:**
Total damages in a wrongful death case are capped at $1.5 million plus medical bills. Punitive damages and prejudgment interest are included within the cap. The death cap applies per claimant thus reducing or eliminating the "stacking" of multiple death caps by suing multiple defendants.

5) **SETTLEMENT CREDITS**:
Current law allows defendants to have their judgment reduced by claiming a "credit" for payments made by settling co-defendants. The non-settling defendants may elect either a dollar-for-dollar credit or a percentage reduction based on the percentage of fault attributable to the settling defendant.

6) **INADMISSIBILITY OF NURSING FACILITY SURVEYS AND REPORTS:**
Deficiency reports, surveys and other findings by state agencies against nursing homes are now admissible as evidence in a civil lawsuit only when the evidence relates to the patient, incident or comparable event on which the claim is based or pertains to a material rule or statutory violation. Additionally, the violation must be affirmed and no longer appealable either administratively or through court review in order to be admissible in a civil action.

7) **STATUTE OF REPOSE**:
Doctors and hospitals are now granted a 10-year statute of repose. A plaintiff must file suit within 10 years of the incident otherwise the case is time barred. This effectively cuts the tail of an obstetrician or neonatologist in half.

8) **EMERGENCY CARE PROTECTIONS:**
Plaintiffs must show a demonstration of "willful and wanton" conduct in order to prove a negligence case against an emergency care physician. This measure provides significant protection for a physician who had no prior contact with or health history from the patient

The Insurance Commissioner was aware that in light of the low frequency and very high potential severity (average size) of medical malpractice claims in a state like Hawaii, the following paragraph was also included in the request to providers:

> While I recognize the difficulties involved in pricing legislative measures dealing with low-frequency and high potential severity lines of insurance such as medical malpractice, and that these difficulties are even greater for smaller states like Hawaii, it is important that legislative discussions be based upon the historical data and actuarial expertise that is available from providers of the coverage.

During the auto insurance reforms in the mid-1990's, data was obtained on almost 1 million policies issued by over a hundred insurance companies. The data on medical liability in Hawaii is extremely limited: only about a couple thousand doctors and three insurers. The Law of Large Numbers and other generally accepted actuarial procedures require a large amount of data in order to confidently predict the future. When a state does not have sufficiently large numbers, comparable data from other states may be used to calculate a reasonably reliable estimate of future effects.

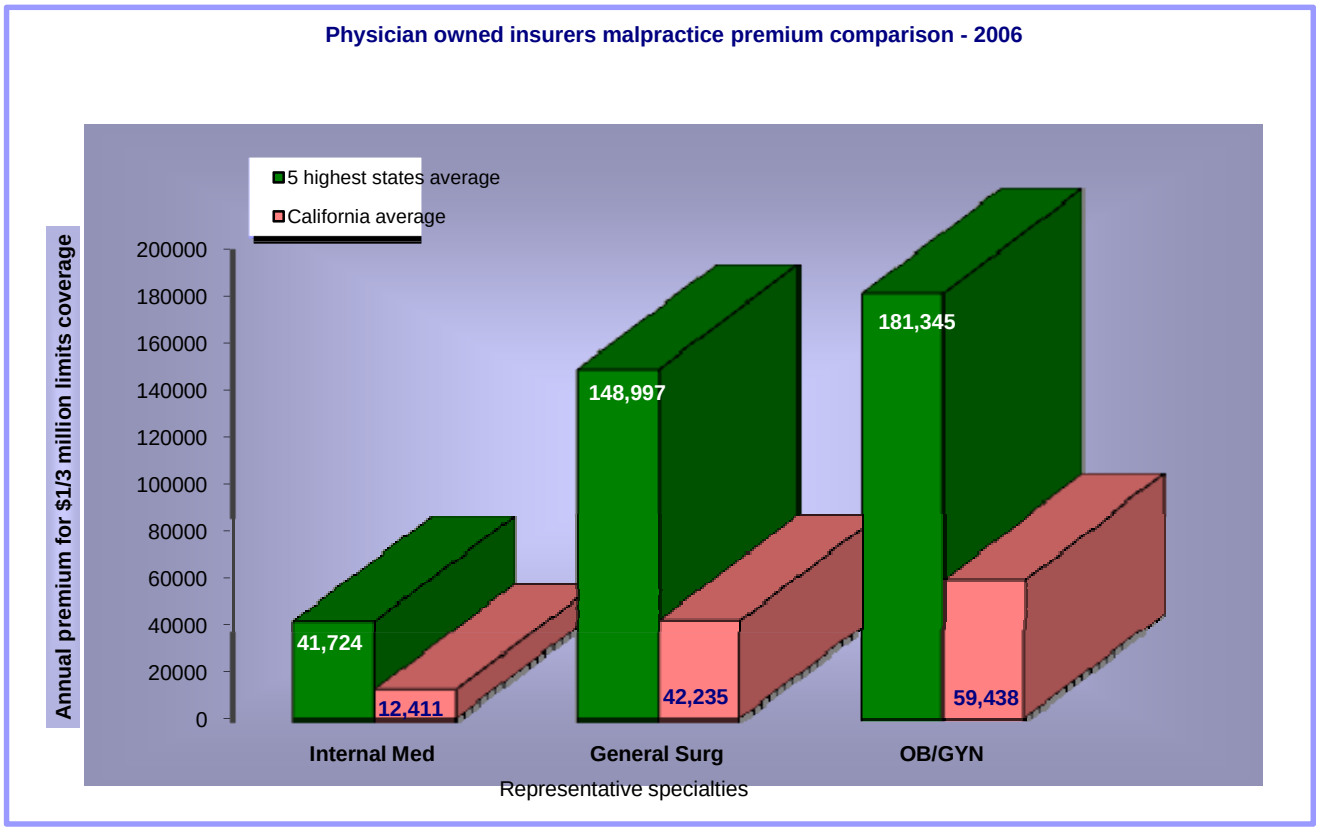
The Insurance Division was not able to obtain detailed actuarial analyses of the effects of the selected medical malpractice insurance reforms. Once again, this is not surprising since there simply is not enough Hawaii medical malpractice insurance experience at the higher levels of awards from which one can produce an actuarially appropriate rate determination based on Hawaii experience.

While it may be difficult to quantify the rate level effects of medical malpractice reforms such as those enumerated in the request, it is reasonable to assume that the effect is greater than zero based on experience in other states. That is, regardless of the inability to determine how much a specific item of reform is worth in loss reductions, it is appropriate to base an estimate of those effects from other sources.

Laws capping non-economic damages have been enacted in a number of states. Milliman USA, Inc. provided an analysis of caps for the Pennsylvania legislature in 2003. Milliman looked at the effect of caps in states that had passed such laws and states without caps. In California, MICRA reduced costs, medical malpractice losses per physician to 52% of the countywide average. Other states with caps have also reduced costs: Colorado 69%, Indiana 86%, and Maryland 64% of countrywide averages.

Conversely, states without caps have higher than average malpractice costs: Pennsylvania 171%, Florida 136%, Illinois 144%, New Jersey 131%, New York 156% and Washington, D.C. 144% of countrywide averages. Milliman estimated a reduction of 18% medical malpractice premium rates if reforms were enacted in Pennsylvania in 2003. In a 2004 study, Milliman estimated a 15% reduction in rates in Wyoming if reforms were enacted.

Premiums are affected by numerous factors, but clearly lower costs will result in reduced premium rates. Again, the experience of California shows that premiums have been stabilized at a lower level than similar states without caps.



Source: Medical Liability Monitor, October 2006

Since the requested information was based on reforms similar to reforms that were recently enacted in the State of Texas, the Insurance Division researched the effects of the reforms in that state.

Reforms' Effect on Texas Medical Malpractice Market

A. How Medical Malpractice Companies Have Responded (i.e. rates)

1) Physician Rates Since September 2003

- Rate decreases
  - o The largest writer, Texas Medical Liability Trust, with $189,000,000 in written premium (2003) reduced their rates by 16.4% since September 01, 2003 (-12% on January 01, 2004 and another 5% on January 01, 2005).
  - o A small writer, Continental Casualty Company, with $800,000 in written premium (2003) reduced their rates by 11.5% on February 01, 2004.

- Proposed Rate Increases Eliminated / No Changes in Rates

- o Most companies fall into this category.
- o The Doctors Company had an indicated rate change prior to the consideration of HB 4 of about +20% but filed in October 2003 for no change. On May 01, 2004 they implemented an increase of +0.7%. Doctors Company writes $15,000,000 in physician premium (2003).

• Rate Increases Disapproved

- o The Texas Medical Liability Insurance Underwriting Association (JUA) filed for a 35.8% increase which was disapproved November 2003. The JUA has $58,000,000 in physician premium (2003).
- o The Medical Protective Company (Med Pro) filed for a 19% increase, which was disapproved April 20, 2004. Med Pro has $134,000,000 in physician premium (2003). Med Pro moved its physicians to its risk purchasing group July 1, 2004 and implemented a 10% increase. TDI staff brought an enforcement action against this carrier. From July 12 through July 14, 2004, a hearing was held before the State Office of Administrative Hearings (SOAH) on both the 10% increase and the disapproved 19% increase.

Based upon the Texas experience and similar experience in other reform states, an appropriate expectation following the passage of similar reforms in Hawaii, if a legislative package is approved and passed by the Hawaii Legislature, is that losses and the corresponding loss costs should decrease by an amount between 12 and 18%.

Understanding that the method used to arrive at the 12 -18% range is a "best available" approach, medical malpractice reform legislation containing a mandated reduction should also provide for insurers to provide actuarially appropriate analyses that indicate the mandated reduction will place the insurer in financial jeopardy.

An insurer may file for an exemption or waiver from the mandatory decreases by providing an actuarial analysis indicating that the mandatory decreases will place them in financial jeopardy. At a minimum, the actuarial analysis should include the following:

A) A detailed description of the techniques and data used in determining each estimate.
B) A comparison of the estimated cost savings with the actuarial excess limits rating calculations in your current rates.
C) A description of all assumptions made in your estimated cost savings.
D) Your actual Hawaii medical malpractice loss ratios for each of the past ten years
E) Your actual total company medical malpractice loss ratios for each of the past ten years

F) Year end loss and loss adjustment expense reserves for each of the past five years

G) An estimate of the effects upon insurance rates and premiums from each of the listed measures upon future loss and loss adjustment expense reserves

H) An analysis of the effects from each of the listed measures due to anticipated changes in claim frequency and claim severity separately.

CONCLUSION

Based on studies and comparable data on reforms in other states and the limited information in Hawaii, the typical medical liability reforms would result in estimated reductions of between 12 and 18% in medical malpractice premiums in Hawaii. Care should be taken to evaluate each insurer's financial condition and provide an exception from application of any automatic rate reduction that might force the insurer into insolvency.