

Medical Malpractice

IN THIS ISSUES UPDATE

THE TOPIC

RECENT DEVELOPMENTS

BACKGROUND">BACKGROUND

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THE TOPIC

2012

Medical malpractice insurance covers doctors and other professionals in the medical field for liability claims arising from their treatment of patients.

The cost of medical malpractice insurance began to rise in the early 2000s after a period of essentially flat prices. Rate increases were precipitated in part by the growing size of claims, particularly in urban areas. Among the other factors driving up prices was a reduced supply of available coverage as several major insurers exited the medical malpractice business because of the difficulty of making a profit.

The number of claims (frequency) filed has dropped over the last few years and the cost of claims (severity) has moderated. However, underwriting results are being hurt by declining premiums and low investment yields.

RECENT DEVELOPMENTS

- **Tort Reform:** Many states have considered tort reform over the past few years. In Georgia

physicians are considering two options: whether to push for a reinstatement of the \$350,000 cap on noneconomic damages, which was deemed unconstitutional by the state's Supreme Court in 2010 in that it nullified the jury's ability to award appropriate damages, or whether to dismantle the current liability system in favor of a no-fault model being promoted by Patients for Fair Compensation, based on the workers compensation system. Under this plan, claims would be evaluated by an independent review panel. Its supporters say the no-fault system would significantly reduce costs, eliminating physicians' use of defensive medicine in an effort to protect themselves from claims of negligence. This new approach was first advocated in Florida.

- In Missouri the state's Supreme Court ruled in August 2012 that caps on noneconomic damages in medical malpractice cases were unconstitutional, overturning a 2005 law enacted to help stem rising costs and premiums. The court voted 4 to 3 that the cap violated a claimant's right to a decision by a jury. In 2010 caps on awards were found unconstitutional by high courts in two states, Georgia and Illinois. In Illinois the constitutionality of limits on jury awards has come before the state's high court on two other occasions, most recently in 1997.
- **Costs to the Public:** According to a 2011 report by Towers Watson, since 1975, when medical malpractice insurance data were first separated out from other types of liability, medical malpractice cost increases have outpaced other tort areas, rising at an average of 10.0 percent a year, compared with 7.5 percent for all other tort costs. However, growth in medical malpractice costs since 2005 have averaged less than 0.5 percent annually. Regardless of whether a case is won or lost, going to court is expensive.
- **Claims:** A study reported in the New England Journal of Medicine (August 2011) found that 7.4 percent of all physicians could expect a medical malpractice claim to be filed against them in any given year but only 1.6 percent of physicians would be subject to a claim that would lead to a payment. This translated into 78 percent of all claims resulting in no payment to the claimant. The researchers studied claims received by one major medical malpractice insurer from 1991 through 2005 with a nationwide client base.
- The Ohio Department of Insurance publishes an annual Medical Professional Liability Closed Claim report. During the six years it has been reporting such data, total annual claims have steadily decreased from about 5,000 in 2005 to around 3,000 in each of the last three reports. Most claims, about 75 percent, are closed without a payment to the claimant, although most closed claims generated expenses for investigation and defense, an average of \$29,424 per claim.
- According to the National Association of Insurance Commissioners and SNL Financial Data, in 2010, the latest year of complete data, insurance company defense and cost containment expenses for medical malpractice were 61.4 percent of losses incurred, up from 57.2 percent in 2009. In other words, in addition to the \$2.9 billion insurers paid out in actual compensation, they spent another \$1.8 billion in expenses to settle claims.
- **Risk Management:** A new approach to patient safety, if adopted nationwide, could reduce

claims. Under a program developed by the University of Michigan Health System (UMHS) over the past decade, which was recently adopted by seven Massachusetts hospitals, the average monthly rate of new claims dropped from 7.03 to 4.52 claims per 100,000 patient visits and the average monthly rate of lawsuits has dropped from 2.13 to 0.75 per 100,000 patient visits. The essence of the new approach “seeks to elevate patient safety to the foreground and relegate claims considerations to the background,” the UMHS says in its recently published manual for other hospitals.

- **Market Conditions:** Data from SNL Financial show that the medical malpractice liability insurance business was profitable in 2011, with a combined ratio of 87.9 percent, a one percent improvement from 2010. The combined ratio represents the percentage of each premium dollar spent on claims and related expenses. In 2008 the combined ratio was 79.2, the best year in the current underwriting cycle. Premiums fell by 2.7 percent in 2011, dropping to \$8.85 billion from \$9.1 billion in 2010 and \$9.2 billion in 2009.
- Many hospitals obtain liability insurance through the alternative market, including risk retention groups (RRG), see report on Captives. In Vermont, which is home to 32 percent of RRGs nationwide as of July 2012, healthcare is the dominant industry, making up 62 percent of the total, according to the Risk Retention Reporter.

BACKGROUND

Brief History: The insurance industry tends to be cyclical. The medical malpractice insurance segment experienced a period of crisis in the early 1970s, when several private insurers left the market because of rising claims and inadequate rates. The exodus of capacity resulted in an availability crisis. Over the next 15 years, various attempts were made to ease the explosion in claims costs—tort reform, increased diagnostic testing, improved peer review and increased communication between doctors and patients. These efforts appear to have had a positive impact. The number of claims dropped. However, the size of claims—the dollar amount—continued to grow and is still growing.

Aggressive campaigns to reform state laws governing medical liability lawsuits began in the 1970s. Every state except West Virginia passed reforms. New Hampshire’s entire reform act was subsequently struck down as unconstitutional by its Supreme Court, but Indiana’s, which was the most comprehensive in the nation when it went into effect in 1975, has been found constitutional in all challenges and has helped to keep physicians’ premiums down in that state. California’s Medical Injury Compensation Reform Act (MICRA), also enacted in 1975, which caps noneconomic damages and modifies the collateral source rule, is also considered a model law, in terms of curbing the size of claims to keep premium hikes in check, see below.

Responding to the problem of availability, physicians formed doctor-owned malpractice insurance companies to provide coverage. These companies now write about half of all the medical malpractice insurance in the nation. Since these new companies had not experienced any losses, they could initially charge much lower rates. Later they suffered the fate of their private insurer predecessors, having to pay claims of increasing frequency and size as the

patients of the doctors insured filed malpractice claims. This, in turn, necessitated charging higher insurance rates.

The incidence (frequency) of claims has fluctuated. In the 1980s, the number of medical malpractice claims filed appeared to increase. Reasons for the increase are not entirely clear, but several contributing factors have been suggested. In addition to the fact that people became more litigious than in the past, the crisis of the 1970s, which was extensively reported by the media, may have made people more aware of the possibility of suing for damages. Other factors were the loss of an intimate relationship between families and their doctors and the use of medical experts to testify in malpractice cases. Physicians have also accused lawyers of being excessively eager to bring malpractice suits because of the high fees the lawyers can collect when their clients win.

More recently, the number of claims filed has been decreasing. Just as it is unclear why claims increased, there are only theories about why they have been decreasing, among them that attorneys are taking fewer cases because doctors and hospitals usually win when a case goes to trial and taking a case through the courts is expensive. Some say attitudes of juries have changed, and yet others say that there is a measure of cyclicity to claims filing as costs rise and there is a reaction. Some industry observers are predicting an end to the decrease in the 2010s.

Prevalence of Medical Malpractice: A study (generally known as the Harvard study) commissioned by New York State in 1986, and released in 1990, showed that actual malpractice is relatively rare. Of the New York hospital cases examined, the incidence of adverse events, or injuries resulting from medical "interventions" or treatment, was 3.7 percent. The percentage of adverse events due to what the physician team characterized as "negligence" (not necessarily a legal definition) was 1 percent. However, only one in eight who suffered from an adverse event due to negligence filed a medical malpractice claim, and only one in 15 received compensation. Most adverse events resulted in only minimal and transient disability and most of the patients' medical care expenses were paid for by health insurance. This helps to explain why only a small percentage of patients who are injured as a result of negligence file medical malpractice claims. However, a significant portion (22 percent) of patients who did not file medical malpractice claims suffered moderate or greater incapacity. In a second phase of the study, researchers confirmed that some of the tort claims filed provided little or no evidence of medical malpractice or even an adverse event, suggesting that the tort system is "very error-prone," at least in its initial stages.

Effects of Tort Reform: Between February 1986 and May 1987 the General Accountability Office issued five reports on medical malpractice. The third, published in December 1986, "Medical Malpractice: Six State Case Studies Show Claims and Insurance Costs Still Rise Despite Reforms," singled out the reforms enacted in California in 1975 as among the most effective in moderating increases in the cost of malpractice insurance and the size of awards.

A 2004 study conducted by the RAND Corp.'s Institute of Civil Justice in Santa Monica, California, confirmed the success of California's tort reform initiative. It found that the 1975

California Medical Injury Compensation Reform Act (MICRA) reduced the damages that doctors and their insurers are ordered to pay in medical malpractice lawsuits by 30 percent. MICRA limits jury awards for pain and suffering to \$250,000 and also limits attorney fees. The study, which reviewed 257 plaintiff verdicts, also showed that compensation to injured patients declined by 15 percent while the fees for plaintiffs' attorneys fell by 60 percent. Caps on noneconomic damages were imposed in 45 percent of trials that ended in a victory for plaintiffs. Those with the highest percentage loss as a result of caps on noneconomic awards were often those with injuries that caused relatively little economic loss but a significantly lower quality of life, according to the study. A major effect of the law was to make plaintiffs' lawyers accept more of the cost of the litigation. The law, which was enacted when California was facing an insurance crisis, has been considered as a model for medical malpractice reform in other states.

In 2003, Texas voters approved Proposition 12, which gave the legislature the power to adopt a \$250,000 cap on most medical malpractice noneconomic damage awards. Since the passage of reforms, more doctors have moved to the state, including rural areas, thus improving access to medical care, and competition among medical malpractice insurers has increased as the number of medical malpractice insurance companies doing business in the state has grown. According to the state's medical association, all major physician liability insurers cut their rates once the caps were in place, most by double digits. By January 2010 the number of claims and lawsuits in most Texas counties had been cut in half and roughly half of the state's doctors were paying lower liability premiums than they were in 2001.

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[Back to top](#)