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Early Offer Reform In Personal Injury Cases — A Proposed Fix To The Personal Injury Litigation System

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Commentary

Early Offer Reform In Personal Injury Cases — A Proposed Fix To The Personal Injury Litigation System

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[Editor's Note: Michael G. Ornstil has been a full-time mediator with JAMS in San Francisco since 1994 and can be reached at mornstil@jamsadr.com. He successfully mediates a wide variety of disputes including matters involving personal injury and wrongful death, products liability, property damage, medical malpractice, insurance coverage, employment, and toxic torts. Copyright 2009 by Michael G. Ornstil.]

An interesting study was recently published discussing the potential advantages of adopting a system whereby liability insurance carriers are afforded the opportunity to make "early offers" in personal injury cases. This early offer system encourages liability insurers to issue prompt payment of medical expenses and wage loss to parties injured on a no-fault basis, with the injured party having to give up recovery of non-economic damages in exchange. The study, entitled "The Cost and Other Advantages of an Early Offers Reform for Personal Injury Claims Against Business, Including for Product Liability," appears in Volume 2008, Number 2 of the Columbia Business Law Review, and was written by Jeffrey O'Connell and Patricia Born. Mr. O'Connell is a law professor at the University of Virginia, and Ms. Born is an associate professor in the Department of Finance, Real Estate and Insurance at California State University, Northridge. This article shall discuss the general framework of the early offer reform system, an analysis of the findings of the study, and provide a mediator's perspective on early offer reform.

The Problem – At the outset of their study the authors note that "[m]any observers have concluded that the personal injury liability litigation system (including for product liability) needs improvement."[1] The authors further note that the "current system of tort liability for personal injury is often seen as unworkable and in need of fundamental reform."[2] The problem noted with our current tort litigation system is that such cases are "extremely complicated" as they require proof of liability, economic damages and non-economic damages.[3] Citing the complexities in proving fault and damages, the authors note that the current system is fraught with "frustrating uncertainties."[4] There are oftentimes long delays between the filing of the suit and its ultimate resolution either by settlement or trial, and the transactional costs involved in litigating these cases are "formidable" for both plaintiffs and defendants.[5] With respect to these transactional costs, the study notes that an earlier study found that only 37.5 cents of every dollar of liability premiums is paid to claimants and that of the 37.5 cents, only 14 cents is attributable to the actual economic losses sustained by the plaintiffs.[6]

The Proposed Solution – The proposed solution to improve the current personal injury litigation system is the adaptation of "early offer reform" or and "early offer statute." The proposed reform has two primary objectives: (1) to provide speedy payment of a plaintiff's economic losses, and (2) to reduce all parties' transactional costs. A third objective of the reform is to remove or at least minimize the uncertainty inherent in prosecuting or defending a complex injury case. Rather than having a judge, arbitrator or jury decide what, if anything, should be awarded, early offer reform offers a guaranteed and certain end result.

The early offer system, as generally constituted, would have the following component parts:

The reform plan would apply to personal injury cases in which insurance coverage is afforded the defendant(s);

Within 180 days after a claim is filed (presumably by way of the filing of a lawsuit), a defendant would have the option to offer the plaintiff periodic payment of the plaintiff's net economic losses (medical expenses, rehabilitation costs, lost wages/income) as such losses are incurred;

A defendant, as noted above, would not be required to make an early offer, but would have the option to do so if it considered doing so advantageous;

A plaintiff's economic losses are defined as net economic losses, i.e., losses incurred net of any collateral source payments such as worker's compensation payments;

The offer must also include payment of a 10% attorney fee to plaintiff's counsel. The 10% fee would be calculated based on the value of the early offer;

If the plaintiff accepts the defendant's early offer, the case would be settled. If the defendant elects not to make an early offer, the plaintiff can pursue his/her lawsuit seeking all recoverable damages, both economic and non-economic;

In the event an early offer is made and a defendant rejects it and pursues litigation, plaintiff's burden of proof is increased. To prevail on his/her claims, the plaintiff would have to establish that the defendant engaged in "gross negligence" rather than simple negligence, and the plaintiff would also have to prove such misconduct beyond a reasonable doubt or by clear and convincing evidence, rather than by a preponderance of the evidence; and

There is no prescribed time period within which a plaintiff must decide whether to accept or reject a defendant's early offer. Plaintiff may conduct discovery, for example, to aid in the decision as to whether or not to accept such an offer.

The early offer reform proposal acknowledges that some flexibility shall be required to account for unusual circumstances. For example, the proposed reform would permit plaintiff's counsel to petition the court for additional fees beyond the 10% standard attorney fee if counsel believes that under the particular circumstances of the case, an award of 10% would be unfair. In addition, the proposed reform acknowledges that there will be claims where the plaintiff's physical injuries are severe but his or her economic damages are modest and the non-economic damages are very significant. Examples cited are cases involving the death of a child or a death of an aged adult. In both instances despite the horrific nature of the injury, i.e., death, there would be relatively insignificant economic damages because the loss of earnings component would be minimal, but the non-economic losses to the surviving heirs could be of very significant value. Other instances where such dynamics exist are cases involving amputation, brain injuries and spinal cord injuries. The proposed reform would allow for minimum payments, in the range of $100,000 to $500,000, to account for the potential discrepancy between economic and non-economic damages in severe injury and death cases. Thus, even though the economic damages in these serious cases may be relatively modest, the plaintiff would receive a guaranteed payment in the $100,000 to $500,000 range.

Study's Findings Regarding Effects of Early Offer Reform – To evaluate the potential implications of early offers, the authors examined 39,553 "general business liability" claims for personal injury settled or tried to verdict in Texas courts between 1998 and 2004, where the settlement or verdict was greater than $10,000.[7] The study excluded cases involving claims of medical malpractice and auto accident cases. The authors were able to obtain this information as Texas requires that insurers report to the Texas State Department of Insurance on all claims involving personal injury where a payment of at least $10,000 is made. Insurers are required to report the reserve amount, both initial and final, it set in each case, the amount paid by way of settlement or award, and whether any other insurers contributed to satisfying the settlement or award.

Utilizing the above data, the authors were able to quantify the savings, both in terms of amounts paid to plaintiffs and litigation expenses incurred, of the early offer system versus the traditional litigation system.

In addition, the authors were able to quantify the amount of time saved in terms of overall resolution of claims.

It should be noted that the results of the analysis are extremely complex and are contained in 20 tables.[8] These tables break down the results based upon types of damages sought, the nature of the claim, and other relevant factors. It would be impractical to detail all of the authors' findings, but the authors were able to draw several general conclusions which are representative of the study's detailed findings.

The study focused on the insurer's perspective in evaluating whether early offer reform would result in lowered payouts to claimants. The study found that out of 39,553 Texas tort claims, an early offer would result in a lowered payout in 29,915 cases when comparing the insurer's initial reserve amount with the amount of the early offer payout.[9] When comparing the early offer with the final reserve amount, which the study noted was generally considerably greater than the initial claim reserve, the study found that the insurer would pay less in 38,826 of the 39,553 cases.[10]

In terms of amounts insurers would save by making early offers, the study noted that the savings would be substantial. For example, the study noted that in cases where no minimum guaranteed payment is made (discussed in Section B, above), the average savings would range from $128,911 to $256,854, depending on whether the settlement payment was measured against the initial or final reserve amount.[11] These savings are primarily the by-product of eliminating payment of non-economic damages to plaintiffs. The study noted that in cases involving death or severe injury where a minimum guaranteed payment component ($100,000/$250,000) were added to the early offer, the number of cases where an early offer would be economically advantageous to insurers would be significantly reduced. The study noted, however, that in the cases where an early offer would be advantageous, the cost savings in such cases would be hundreds of thousands of dollars even with guaranteed minimum component.[12]

The study found that significant time would be saved in terms of payment to claimants by adoption of early offer reform. The authors assumed that offers will be made and accepted in 180 days of the filing of suit. With that assumption, the study found that the early offer proposal could expedite payment to claimant by approximately two and a half years.[13]

The study also examined the potential savings in litigation costs. The model and assumptions used by the authors to calculate cost savings is complicated and the best that was offered were estimates of expected savings. The study concluded that by accepting an early offer, claimants would enjoy litigation savings of 0.23 of what the total settlement or award would have been in the absence of the acceptance of an early offer.[14] For insurers, the study concluded that they would enjoy litigation cost savings of 23/33 of the reserve for legal expenses or actual legal expenses.[15]

A Mediator's Perspective on Early Offer Reform – Early offer reform offers the prospect for three significant benefits to litigants: (1) timely payment of economic damages without enduring protracted litigation; (2) significant savings in litigation expenses, including attorney fees; and (3) avoiding the uncertainties attendant to a judge, jury or arbitrator deciding the matter. Not coincidentally, saving time and money and avoiding the risks of trial are the primary reasons litigants utilize the mediation process. Thus, from a mediator's perspective, early offer reform has promising features.

Unfortunately, while early offer reform offers benefits to litigants, it is anticipated that there will be great resistance to implementing such a program. The major stumbling block is the provision whereby the burden of proof and the level of misconduct needed to be proved increases if the plaintiff fails to accept an early offer. As noted above, a key component of early offer reform is the provision that if a claimant does not accept an insurer's early offer, the claimant at trial would have to establish that the defendant engaged in gross negligence and the claimant's burden of proof would be increased from a preponderance of the evidence to beyond a reasonable doubt. The plaintiffs' bar is undoubtedly going to have strong objection to having plaintiffs "penalized" for not accepting an offer of economic damages only. The plaintiffs' bar might perceive that insurers would use early offer reform to gain strategic advantage over plaintiffs. For example, in a serious injury case where plaintiff suffers not only significant economic losses but significant non-economic losses, and where liability is clear, it makes

sense that the insurer would always make an early offer of economic damages. Why wouldn't it? If plaintiff accepted the offer, the insurer benefits by avoiding the inevitable award of substantial non-economic damages. Of course, if liability is clear and there is a reasonably good chance that plaintiff would receive a substantial non-economic damage award, it would be fairly rare for a plaintiff to accept such an "early offer" of only non-economic damages. Why would he or she? A guaranteed early payment of just economic damages, coupled with a reduced attorney's fee of 10%, is probably not a significant enough enticement for a plaintiff to give up the near certainty of recovery of non-economic damages. The insurer, however, would not be crushed by the rejection of its early offer as it has gained the strategic advantage of plaintiff now being required to prove gross rather than simple negligence, and having to establish such misconduct beyond a reasonable doubt.

To entice plaintiffs to consider an early offer in cases of serious injury and significant non-economic damages, the proposed reform allows for the payment of a fixed sum ($100,000 to $500,000) in excess of economic damages. This additional payment would likely entice some plaintiffs to accept an early offer, but would not totally alleviate the problem described above.

A second potential problem with early offer reform is that in many cases it might be an enormous challenge to both sides to determine the nature and extent of a plaintiff's economic damages. Economic damages, by and large, come in two varieties: (1) medical expenses both past and future, and (2) loss of income both past and future. In many cases the plaintiff's injuries have not resolved or stabilized within 180 days of the filing of a suit. In cases where plaintiff's medical status remains uncertain at the 180-day mark, it would be an enormous challenge for both sides to evaluate the future medical expenses plaintiff will likely incur, and what loss of earnings may result from plaintiff's prolonged recovery or residual disability. Oftentimes, the nature and extent of a plaintiff's future medical care and loss of earnings is the subject of expert analysis. In many injury cases, within the first 180 days of filing suit neither side is likely to have sufficient information to allow for physicians, economists, etc. to properly evaluate future needs and losses. Thus, early offer reform would require a fair amount of speculation or educated guesswork by both sides. Plaintiffs, in particular, might be reluctant to accept an offer of economic damages when there is significant uncertainty as to whether or not their injuries will fully resolve, when their medical situation will stabilize, and what losses of income might result from their medical situation. This is a second reason why plaintiffs may understandably be unwilling to accept an early offer. Yet if they fail to accept the offer for these valid reasons, they still face the prospect of having to establish a higher level of misconduct and a more stringent burden of proof.

A third potential stumbling block for early offer reform to work is that many personal injury cases involve more than one defendant and more than one insurer. Oftentimes defendants and insurers have very different views on liability exposure, damages, verdict potential, and cost to defend the suit. It is anticipated that in cases involving multiple defendants and insurers, it will be no easy task to get the insurers to act in unison and jointly offer an early settlement. Insurer's differences over relative shares of liability, coverage or damages might paralyze them such that an early offer cannot be made. The authors suggest that if such a problem arises, the insurers can make an early offer and if accepted, they can work out their differences at a subsequent arbitration. While this is true and is a practical proposal, it has been my experience that insurers want certainty and like to close files. The prospect of paying a percentage of an early offer to plaintiff and then later arbitrating with other insurers whether some money should be refunded to an insurer or additional sums are owed by an insurer, will not be very appealing to many insurance carriers. They have not achieved the certainty they seek and have not closed their file by virtue of their early offer to plaintiff.

With this said, there are certainly some cases where early offer reform makes sense and can be a useful tool. The cases that jump to mind are cases where there are both significant liability issues and there is the potential for recovery of great non-economic damages. In such cases, plaintiffs, due to liability questions, face the prospect of getting nothing. In these cases it may make sense for plaintiffs to give up the chance to receive non-economic damages to avoid the risk of a defense verdict. Likewise, because of the risk of a high non-economic damage award, insurers in these cases may be motivated to offer plaintiffs their

economic damages and give up the opportunity of defensing the case.

A second category of cases where early offer reform looks promising is cases where (1) liability is clear, (2) the potential for an award of significant non-economic damage is remote, and (3) all parties agree that plaintiff has not suffered significant non-economic damages. In these cases it makes perfect sense for insurers to offer plaintiffs their economic damages and it makes sense for plaintiffs to accept the offer. Neither side is giving up much, and both sides are benefiting by resolving the case quickly and efficiently with minimal litigation fees and costs.

Conclusion – Personal injury litigation can be expensive and protracted for both plaintiffs and insurers, and of course there is the uncertainty that exists any time a case is adjudicated by a judge or jury. The study examining early offer reform published in the Columbia Business Law Review demonstrates quantitatively that money and time can be saved in these cases by adaptation of a system whereby insurers are encouraged to make early offers of economic damages, and plaintiffs are encouraged to accept such offers.

There are categories of cases where early offer reform makes sense. There are, however, categories of cases where early offer reform will be ineffective and will penalize plaintiffs form making a reasonable decision to reject such an offer. Furthermore, because early offer reform incorporates proof of a heightened standard of misconduct by defendants and a more stringent burden of proof by plaintiffs if an early offer is rejected, it is expected that early offer reform will not receive overwhelming support from the plaintiffs' bar.

Endnotes

1. At page 425.
2. At Page 432.
3. At page 425.
4. At page 432.
5. At page 425.
6. At page 433.
7. At pages 426, 447.
8. At pages 468-503.
9. At pages 458 and 472.
10. At pages 458 and 472.
11. At pages 458 and 472.
12. At pages 458-459.
13. At pages 459-460, 482-487.
14. At page 460.
15. At page 460. ■

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