

Bracing for change

Medical professional liability (MPL) insurance costs at a crossroads

February 2011

At a glance

The effects of the healthcare reform law, changing market conditions, emerging societal trends and challenges to MPL tort reform all will influence future MPL insurance costs.

Inflationary pressures and other factors are likely to increase MPL insurance costs in the short-term.

There are strategies that will help to control MPL insurance costs.

Introduction

Medical professional liability insurance costs, which have remained stable in recent years, are likely to rise in the near future. This is the result of general inflationary pressures and challenges to tort reform, as well as societal changes—both demographic and legislative—that are likely to increase healthcare utilization. Careful consideration of the impact of these potential changes will better prepare healthcare providers, liability insurers, and medical professionals for changes in MPL insurance costs before they actually occur.

Medical professional liability insurance costs at a crossroads

Medical professional liability (MPL) insurance costs have exhibited a pattern of crisis or near crisis followed by relative calm since the 1970s. Over the last five years, costs have remained stable for healthcare providers¹ in most practice and geographical areas due to fewer and smaller claims being paid. However, many factors suggest that costs are likely to rise in the near future. In addition to general inflationary pressures, a number of factors, both internal and external to the healthcare system, are likely to contribute to a near-term increase in future costs, including:

- Successful challenges to MPL tort reform at the state level;
- Recent trends in MPL insurance costs; and
- Increased healthcare utilization resulting from impending societal and demographic changes, as well as healthcare reform.

Beyond the expected increase in healthcare utilization resulting from healthcare reform, other aspects of the new law are likely to impact MPL insurance costs. While the short- and long-term effects are difficult to predict, a brief review of key provisions is useful. In addition, careful consideration of the impact of potential changes affecting MPL costs will better prepare healthcare providers, liability insurers, and medical professionals for changes before they actually occur.

Medical professional liability insurance costs: Recent developments and trends

Challenges to state reforms

States have a strong influence on MPL insurance costs, since MPL insurance is primarily regulated at the state level. Common law and laws applicable to medical professional

Many of the state MPL tort reform laws passed over the last decade are being challenged, and seven states have already overturned previous caps on non-economic damages.

¹ An organization or individual who provides health services to consumers, including hospitals, physicians, nurses, allied health and other health professionals.

liability vary significantly from state to state, leading to large variations in costs. Various MPL tort reforms at the state level have helped control MPL insurance cost inflation in recent years and have led to lower insurance and self-insurance costs.

Approximately thirty states limit damages in MPL cases through statute, and approximately twenty of them specifically limit non-economic damages². However, many of the state tort reform laws passed over the last decade are being challenged, and seven states have already overturned previous caps on non-economic damages. The most recent challenges occurred last year in Georgia and Illinois, where the constitutionality of caps was at issue. The Georgia Supreme Court, ruling that the existence of the caps interferes with a jury's right to determine damages, struck down the state's caps on non-economic damages in March 2010. This ruling followed a similar decision by the Illinois Supreme Court in February 2010, which struck down that state's non-economic damages cap.

Insurance rate trends

A review of MPL insurance rate trends is relevant not only for healthcare payers and insurers, but also is useful as a proxy for trends in self-insurance costs, including amounts retained through captive insurance companies, since self-insurance programs rather than commercial coverage account for a significant portion of MPL costs. The commercial insurance industry continues to provide coverage for losses in excess of self-insurance retentions, and payers and providers should expect similar trends in their respective layers. The graph below illustrates the steady decline in the average price of commercial MPL insurance from 2006 to 2009.

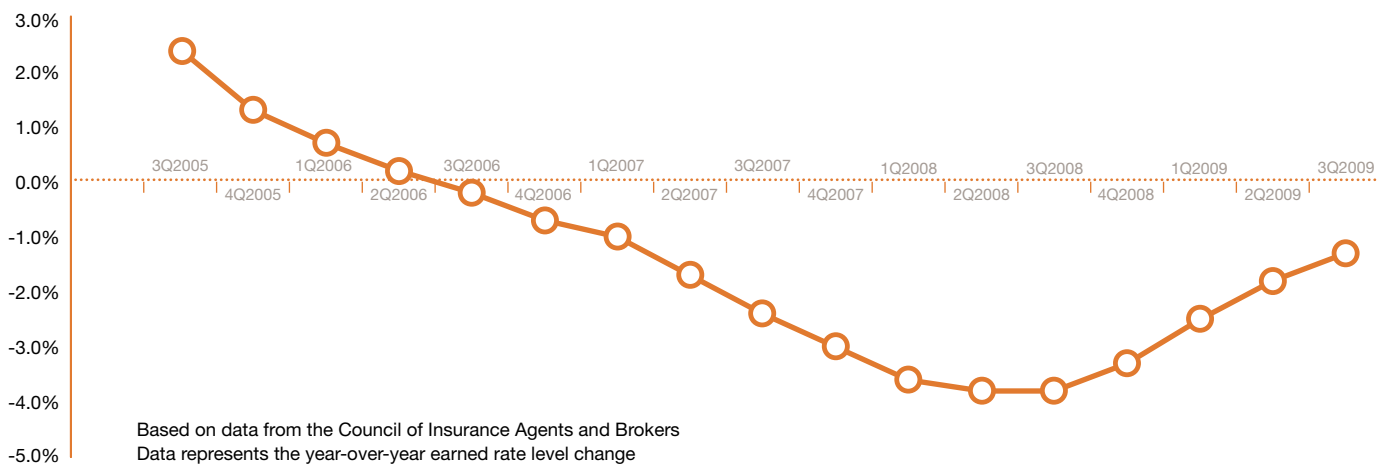
After record rate level increases in the early part of the decade, MPL insurance rates peaked in early 2006 and have continued to drop since that time. Successive years of rate decreases have reduced MPL premium rates to levels that are less profitable for insurers than they were in the early part of this decade, and current rates may prove to be unprofitable for some

insurers. This decrease in premium rates is partially attributable to state caps on non-economic damages and other state MPL tort reforms, which affect both claim frequency (the number of claims per physician or hospital bed) and claim severity (the average cost per claim), although claim severity has continued to increase as a result of general inflationary pressures. However, if claim frequency has bottomed out, commercial insurance rates and self-insurance costs are likely to rise, and the increase likely will accelerate beyond normal inflationary and market trends if state tort reforms continue to be repealed.

Increased healthcare utilization—baby boomers and healthcare reform

Many baby boomers are beginning to reach retirement age, and record numbers of individuals are beginning to access healthcare through Medicare. While most of these individuals may have been covered previously under employer-sponsored healthcare plans, many individuals who did not have health insurance coverage

Commercial medical malpractice insurance rate level change



² <http://www.ncsl.org/default.aspx?tabid=18516>

An aging population and expansion of insurance coverage are likely to increase healthcare utilization.

are gaining it through Medicare. Because the baby boomers' demand for healthcare services will increase as they age, healthcare utilization is expected to increase. Additionally, the Patient Protection and Affordability Care Act and the Healthcare and Education Reconciliation Act of 2010 ("healthcare reform law") is expected to increase healthcare utilization through the expansion of Medicaid eligibility and requirements for healthcare insurance coverage for all Americans, including those with pre-existing conditions. In some markets, increased demand for services could overburden the current supply of physicians and hospitals. Such an overburdened system could lead to more medical errors and misdiagnoses. Without a commensurate increase in healthcare professionals, increased utilization of the healthcare system could also contribute to delays in diagnoses—one of the seven most common reasons that family physicians are sued, according to a 2003 study by the American Academy of Family Practitioners (AAFP)³. In an overburdened healthcare system, patients could experience longer wait times to see primary care physicians, which in turn could delay diagnosis, lead to poor patient outcomes, and eventually increase the number of MPL lawsuits. The potential consequences of an overburdened healthcare system will vary from market to market, depending on demographics and healthcare resources.

Other aspects of healthcare reform

While the merits and direct consequences of the healthcare reform law have been the subject of extensive discussion and debate, many of the indirect effects—including the potential impact on MPL insurance costs—have yet to receive significant attention. The law includes few provisions that directly affect MPL insurance costs; however, several components of the law could have an indirect impact, including:

- The establishment of the Patient-Centered Outcomes Research Institute (PCORI), designed to increase the availability of unbiased, quality research;
- Federal funding for state tort reform alternatives; and
- Cost control pressures spurring more providers to consolidate.

It is uncertain how or if future congressional action will impact the healthcare reform law. Additionally, many states have filed lawsuits challenging the constitutionality of the healthcare law, and it is uncertain how these lawsuits will be resolved. Regardless, healthcare providers, liability insurers and medical professionals should think about the issues now so that they are prepared for changes when they occur.

³ <http://www.aafp.org/fpm/2003/0300/p29.html>

Establishment of the Patient-Centered Outcomes Research Institute (PCORI)

Section 6301 of the healthcare reform law establishes a private, non-profit entity, PCORI, to improve availability of unbiased, quality research (see below). Debate over the merits of PCORI includes discussion of the potential positive effects on healthcare and MPL costs versus the costs of operating PCORI. Over time, PCORI is expected to provide doctors with better research on appropriate drug therapy and treatment procedures, which could result in better patient care, quicker positive outcomes and, ultimately, a lower incidence of MPL lawsuits⁴.

The impact of PCORI on liability costs is yet to be determined. For example, PCORI research could provide doctors with clearer guidelines on

the outcomes of various treatments, giving them a defensible position in the event of a lawsuit, although the healthcare reform law does not provide a safe harbor to physicians who rely on PCORI guidance.

On the other hand, some doctors could face increased risk of liability, if PCORI research suggests that an alternative treatment is preferable to the treatment selected by the doctor. Further, some critics in the medical community suggest that PCORI could be a potential threat to doctors' choice regarding treatment procedures⁵. If doctors limit treatments based on PCORI research, an increased incidence of medical errors (or omissions of treatment) could occur, thereby resulting in an increase in MPL lawsuits.

PCORI was established by the healthcare reform law as a non-profit corporation, not “an agency or establishment of the US government”, which will perform research under the following guidelines:

- Establish a standing Methodology Committee to develop and periodically update scientifically based methodological standards;
- Ensure peer review to assess scientific integrity and adherence to methodological standards adopted;
- Provide public comment periods prior to adoption of national priorities, agendas and standards; and
- Make research findings publicly available within 90 days of completion.

⁴ <http://www.md-writer.com/blog/?tag=patient-centered-outcomes-research-institute>

⁵ <http://www.issa.int/News-Events/News2/United-States-adopts-historic-health-care-reform>

“Demonstration projects” explore cost containment alternatives to the current MPL tort litigation system.

Funding for state tort reform alternatives

Perhaps the most direct effect of the healthcare reform law on MPL relates to \$50 million in federal grants to states for “demonstration projects” that explore cost containment alternatives to the current MPL tort litigation system. A posting on the Wall Street Journal health blog speculated that these projects might include the following types of programs⁶:

- **Health Courts:** Establishing a special court with judges who specialize in medical liability cases and rely on neutral experts, preset timelines and compensation schedules designed to produce a more efficient and predictable system.
- **Early Offers:** Increasing the efficiency of the system by allowing defendants the option to pay economic damages and lawyer’s costs within 180 days of a claim with the hope of avoiding lengthy litigation, thereby reducing cost.
- **Apology Programs:** Creating pilot programs where doctors are trained and encouraged to apologize for or admit errors, thereby reducing the risk of future litigation. While conventional legal wisdom suggests that physicians who apologize for medical errors are essentially admitting guilt and therefore are more likely to be subject to future litigation, some new research suggests that the opposite is true.

The University of Michigan Health System reported in a 2008 New York Times article that MPL lawsuits dropped from 262 in August 2001 to 83 in August 2007 following an experiment with a full disclosure apology program⁷.

- **Medical Review Panels:** Establishing a nonbinding panel of medical experts who review lawsuits before they go to trial to prevent non-meritorious cases from being pursued.

In addition to the pilot programs above, another potential tool to mitigate MPL costs—viewed as more radical by some—could be to enact a no-fault system similar to workers’ compensation insurance or some states’ automobile liability systems. Under a no-fault system, the insurance company providing coverage to a physician or hospital would indemnify any patient whose surgery or treatment resulted in an adverse outcome, regardless of fault. Such a system could reduce the cost of lengthy legal battles and more quickly compensate injured patients. A no-fault system might also remove or lessen the incentive for doctors to practice defensive medicine, thereby contributing to a reduction in overall healthcare system costs.

While these pilot programs are currently several years away from widespread implementation, they could prove to have a beneficial impact on MPL insurance costs and overall healthcare costs.

6 http://blogs.wsj.com/health/2010/06/11/what-might-medical-malpractice-test-projects-look-like/?utm_source=feedburner&utm_medium=feed&utm_campaign=Feed%3A+wsj%2Fhealth%2Ffeed+%28WSJ.com%3A+Health+Blog%29

7 http://www.nytimes.com/2008/05/18/us/18apology.html?_r=1

The healthcare reform law increases pressures on healthcare providers to control costs, providing even more incentive to consolidate.

Cost control pressures spurring more providers to consolidate

Healthcare providers have had strong incentives in recent years to control costs, making it more difficult for individual and small group physician practices and community-based hospitals to continue operating independently. Since early 2010, numerous community-based hospitals have begun aligning with regional or national healthcare systems, and an increasing number of physicians are aligning with hospitals or gaining employment directly through the hospitals or healthcare systems. The healthcare reform law increases pressures on healthcare providers to control costs, providing even more incentive to consolidate. We expect these trends to continue for both hospitals and physicians.

A consolidated healthcare system may be more inclined to retain risk than a smaller system or individual physician, self-insuring a larger portion of its risk or increasing its deductible. Consequently, liability insurers are likely to see a continued reduction in first dollar coverage, with a shift toward lower premium, excess layer coverage. Liability insurers will need to revise underwriting guidelines to ensure that they collect adequate premiums from those healthcare providers that continue to purchase first dollar coverage.

PwC recommendations

MPL tort reform challenges, changing market conditions, anticipated increased healthcare utilization and healthcare reform all contribute to the complex environment facing healthcare providers and liability insurers. PwC recommends that healthcare providers be proactive in addressing the changes by:

- Planning for likely MPL insurance cost increases over the next few years.
- Seeking opportunities to partner with other healthcare providers to self-insure larger portions of risk.
- Reviewing current risk management programs and practices to determine if the impact of healthcare reform legislation or other cost drivers warrant a change in the overall focus of those programs.
- Developing a strategy to remain vigilant on emerging issues in MPL, including the effects of the healthcare reform law, relevant state regulatory changes, emerging societal trends and challenges to MPL tort reform.

MPL insurance companies should plan for a reduction in their primary, or first dollar, insurance coverage and revisit underwriting, ratemaking and business strategies to ensure the collection of adequate premium for the remaining coverage written.

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***To have a deeper conversation
about potential changes in MPL
insurance costs, please contact:***

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