

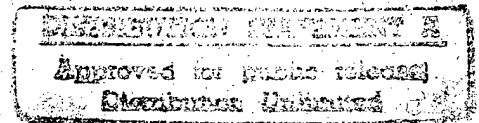
Research Brief

RAND

❖ *Institute for Civil Justice*

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How Big Is the Price Tag for Excess Auto Injury Claims?



Although the nationwide accident rate has been falling steadily, the cost of personal injury automobile insurance has grown at a breathtaking rate over the last two decades, leaving the average driver with a bill for basic coverage in 1990 that was two and a half times higher than the bill for the same coverage in 1980. Because every state requires some form of personal injury insurance, these stiff increases are burdensome for everyone, and especially so for low-income populations. The high costs of coverage also probably swell the ranks of those who drive without coverage.

Many believe that excess claims are a major contributor to rising insurance costs, but to date there has been no comprehensive evidence to support or refute this view. A recent Institute for Civil Justice study, *The Costs of Excess Medical Claims for Automobile Personal Injuries*, takes the first rigorous look at the pattern and cost of excess automobile medical claiming across the states. Authors Steve Carroll, Allan Abrahamse, and Mary Vaiana found that about one-third of the automobile injury medical costs submitted to insurers appear to be excess.

ACCESS TO GENERAL DAMAGES PROVIDES INCENTIVE TO EXCESS CLAIMING

In the study, the term *excess medical claiming* includes claims based on staged or nonexistent accidents, claims by people involved in real accidents for nonexistent injuries,

and buildup of claims for real injuries. To develop an estimate of how much excess claiming occurs nationwide—in contrast to individual instances of fraud identified in a sting operation—the researchers take an indirect approach.

First, they analyze the incentives to submit inflated or invented claims for various types of injuries provided by different insurance systems:

- Under the tort liability system—the set of legal rules governing compensation for automobile injuries in about three-quarters of the states—an injured individual may seek compensation for both the economic loss incurred as a result of that injury (e.g., medical costs) and for noneconomic losses or general damages—hurts such as “pain and suffering” not directly measured in dollars.
- In 1988, when the data used in this study were collected, eleven states had adopted dollar threshold no-fault insurance systems, under which an automobile accident victim is allowed to seek compensation for general damages only if his or her medical costs exceed a specified amount.
- Florida, Michigan, and New York had adopted verbal no-fault systems. In these states the law contains an explicit list of injuries—usually quite serious—for

*RAND research briefs summarize research that has been more fully documented elsewhere. This research brief describes work done in the Institute for Civil Justice and published as *The Costs of Excess Medical Claims for Automobile Personal Injuries*, by Stephen Carroll, Allan Abrahamse, and Mary Vaiana, RAND DB-139-ICJ, 25 pp., \$6.00, ISBN: 0-8330-1649-0, which is available from National Book Network (Telephone: 800-462-6420; FAX: 301-459-2118) or from RAND on the Internet (order@rand.org). RAND is a nonprofit institution that helps improve public policy through research and analysis; its publications do not necessarily reflect the opinions or policies of its research sponsors.*

which an accident victim is allowed to seek general damages.

The availability of general damages and the fact that they are usually calculated as some multiple of economic losses provide the incentive to submit claims for nonexistent injuries and to build medical costs.

CHARACTERISTICS OF INJURIES ALSO AFFECT ABILITY TO EXAGGERATE CLAIMS

The opportunity for exaggeration is also influenced by the nature of the injuries themselves. The researchers distinguish soft injuries, such as sprains and strains, from hard or objectively verifiable injuries, such as fractures and loss of limbs. Examining the incentives embedded in the insurance systems and the ease or difficulty of exaggerating injuries, they predicted what patterns of excess claiming for injuries might occur.

TESTING ANALYTIC PREDICTIONS

The authors draw on a large database of individual closed claims developed in previous ICJ research to test these analytical predictions. Their results support the predictions about the extent of excess claiming that will occur in certain insurance environments.

Figure 1 illustrates their findings. It shows the number of soft injury claims per hard injury claim in every state. The horizontal black line indicates the average value for Michigan and New York, which is used as a baseline in the study. (Certain features of Florida's verbal no-fault system precluded its inclusion in the baseline.)

Claims for nonexistent soft injuries in the verbal threshold no-fault states should be rare because this insurance system provides no access to general damages unless the injury is one of those explicitly specified by the law. In addition, the economic barriers to an accident victim's access to medical care in these states are as low as, or lower than, in any other. Michigan and New York offer first-party auto insurance with no deductible or coinsurance, very high benefit levels, and prohibitions on rate increases based on claiming. Thus, more than in other insurance environments, accident victims are likely to claim whatever medical care they need. Assuming that hard claims are almost always valid, the ratio of soft to hard claims in Michigan and New York suggests the relative frequency of these injuries in automobile accidents.

Soft injury claimants will obtain general damages in dollar no-fault states if the medical claim can be pushed over the threshold; thus the possibility of general damages offers an incentive to claim nonexistent soft injuries in these states. The eleven dollar no-fault states in Figure 1 are scattered, and ten have ratios above the baseline. But all cluster toward the lower end of the distribution.

Because general damages can be obtained for even a small medical claim in the tort states, the study predicted that comparatively more claims for nonexistent soft injuries would occur in these states. The result: Only one of the 36 tort states falls below the baseline. And the 35 tort states that have comparatively high ratios of soft to hard injury claims tend to cluster toward the high end of the distribution. All of the highest 18 states in Figure 1 are tort states.

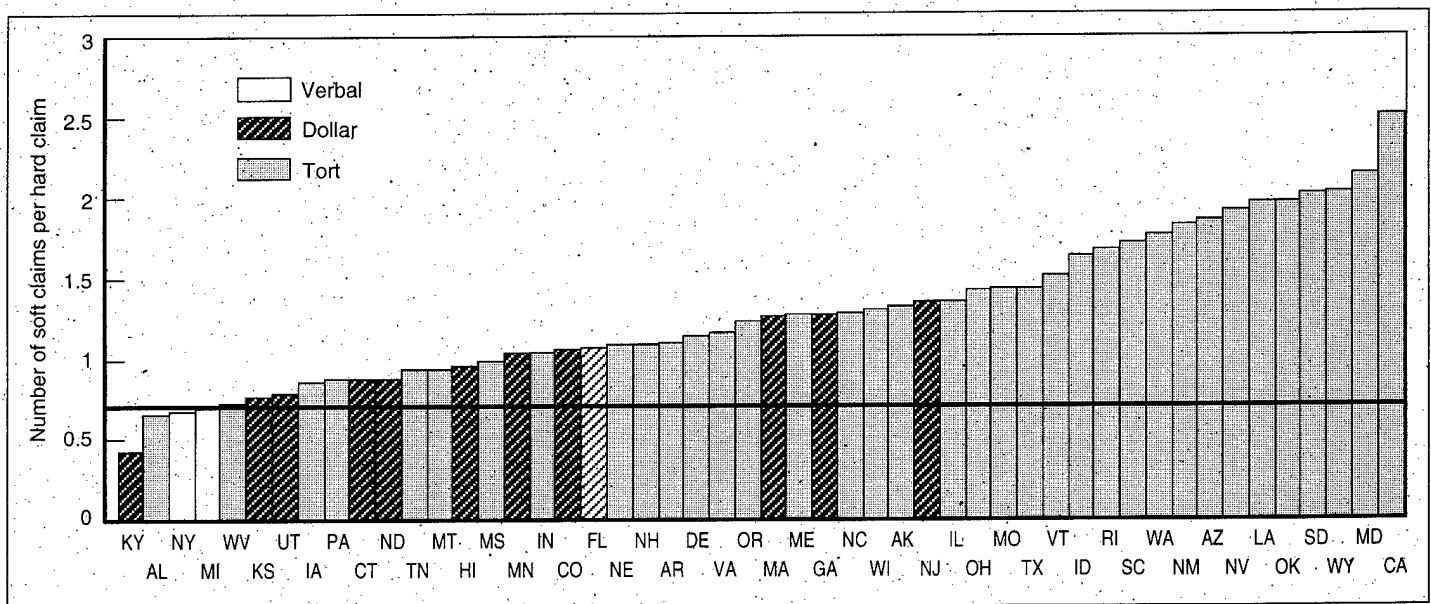


Figure 1—Claims Above Michigan/New York Baseline Suggest Extent of Claims for Nonexistent Soft Injuries

The study uses the extent to which the ratio of soft claims to hard claims in each state exceeds the corresponding ratio for Michigan and New York as the measure of the degree to which claims are being submitted for nonexistent soft injuries in that state.

The study goes on to analyze the amount of medical costs claimed on either soft or hard claims, using methods similar to those described above to estimate the degree to which accident victims are building costs on real injury claims to leverage larger insurance settlements.

Figure 2 provides an example of the analysis. It shows the distributions of medical costs for soft injury claims in Hawaii, a dollar threshold state, and New York. Dollar threshold states provide strong incentives to build costs on soft injury claims because pushing the claim over the threshold allows access to general damages. The vertical line in the figure shows Hawaii's threshold. The average cost of a soft injury claim in each state is adjusted for interstate differences in medical costs and treatment patterns. The horizontal axis in the figure is a logarithmic scale so that equal intervals show equal percentage differences.

The distribution of medical costs in New York rises quickly, peaks, and then drops off sharply to the right. The large majority of soft injury claims are for relatively small medical costs. New York has very few soft injury claims for medical costs that exceed Hawaii's threshold.

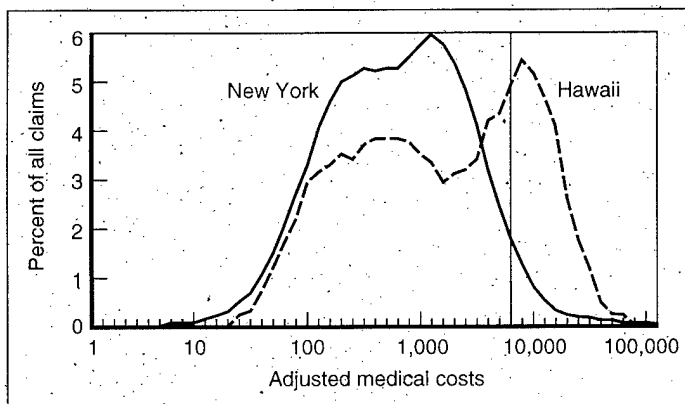


Figure 2—Hawaii's Distribution of Medical Costs for Soft Injury Claims Peaks Just Past Dollar Threshold

Hawaii's distribution also rises sharply, then flattens out. It begins to decline at a relatively low level of medical costs, then turns up again and rises sharply through the threshold. The Hawaii distribution peaks above the threshold, and finally falls off.

A substantial fraction of Hawaii's soft injury claims are for medical costs above the threshold. Compared with New York, the distribution of adjusted medical costs in Hawaii is shifted substantially to the right, as one would predict given the incentives built into the state's insurance system.

THE PRICE TAG FOR EXCESS CLAIMING

The researchers use their empirical analysis of the extent of excess claiming to estimate that between 34 and 40 percent of the automobile injury medical costs submitted to insurers appear to be excess. In 1994, these questionable medical claims would have added roughly \$13 to \$16 billion to the nation's total automobile insurance bill, or about \$100, on average, per policy. These excess claims also stimulated \$4 billion in excess health care consumption.

POLICY DIRECTION

There are no easy solutions to the problem of excess claiming, but the study suggests one possible policy direction: Break the connection between medical costs and general damages. Ways to accomplish this include

- Modifying our insurance systems. (Verbal no-fault systems appear to eliminate the incentives that drive excess claiming for soft injuries, while dollar no-fault systems appear to exacerbate them.)
- Establishing a schedule for general damages based on the nature of the injury, as in disability policies.
- Changing the rule governing admissibility of medical cost information in courts. Modifying this rule could reduce the incentive to inflate that figure.



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