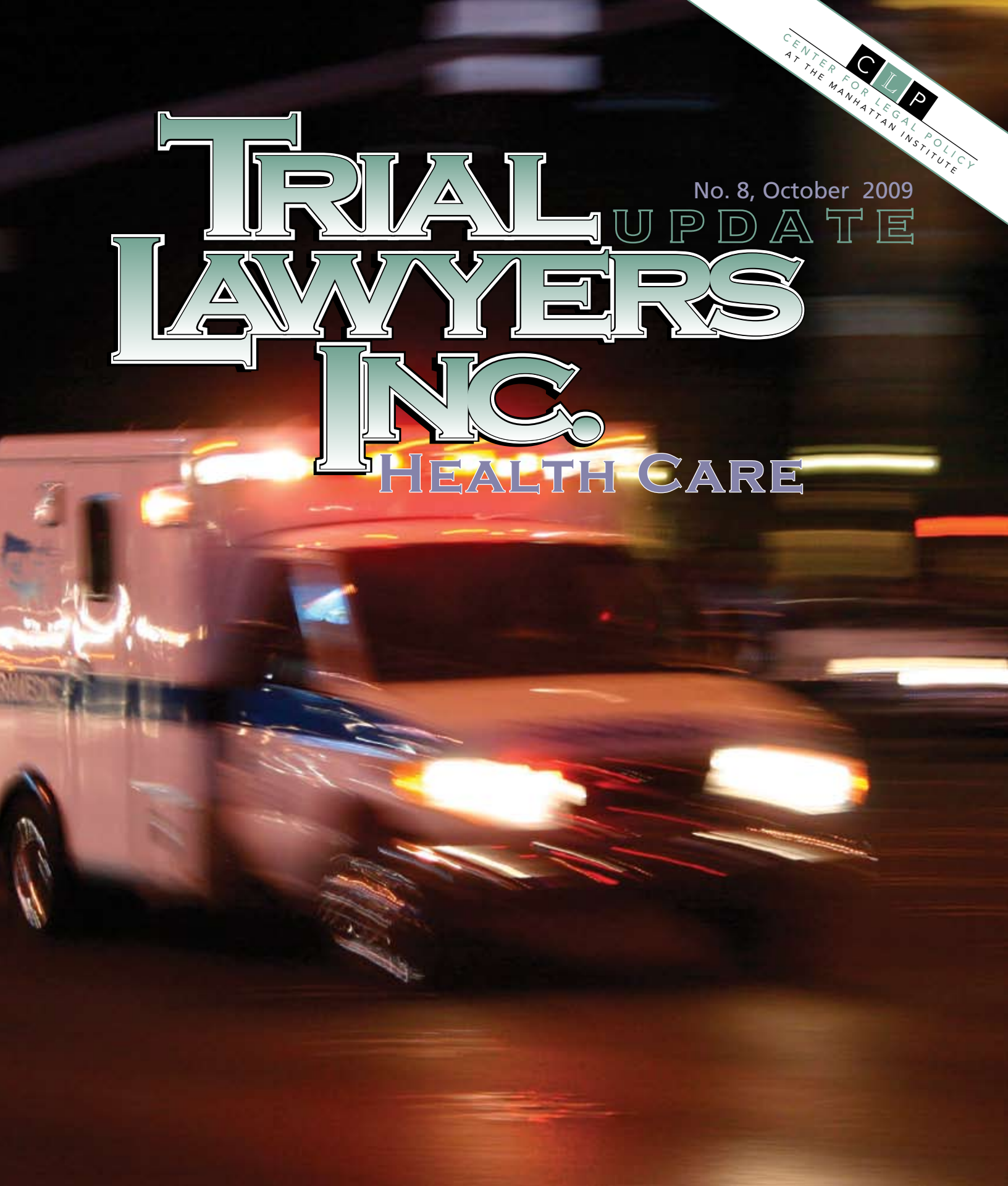


No. 8, October 2009

TRIAL LAWYERS INC.

UPDATE

HEALTH CARE



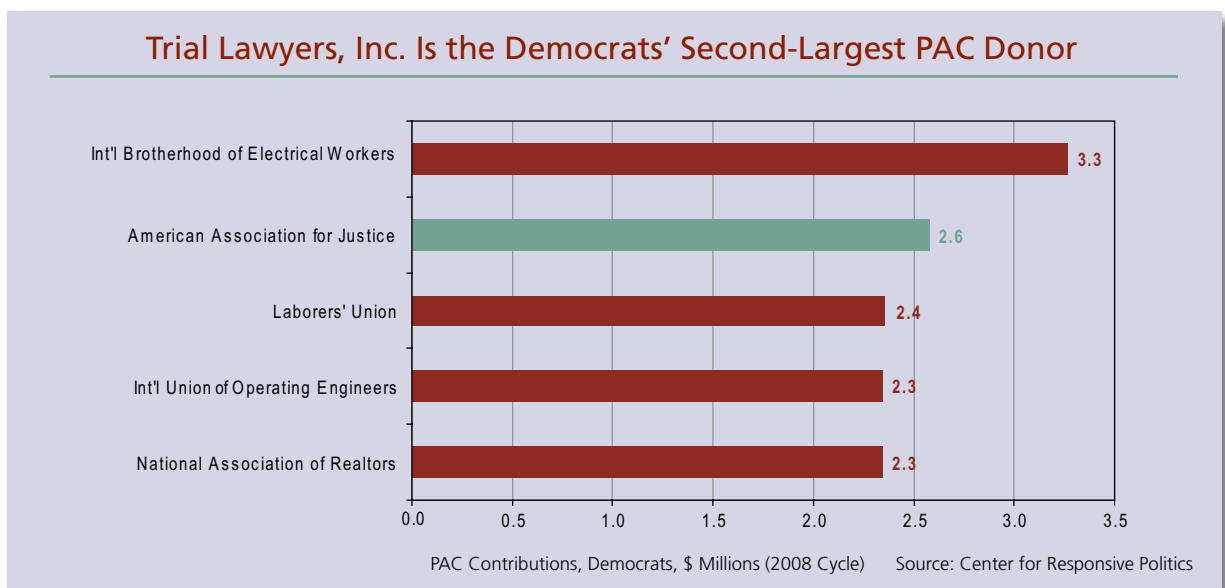
HEALTH HAZARD

Litigation Increases Medical Costs, but Lawyers Block Reform

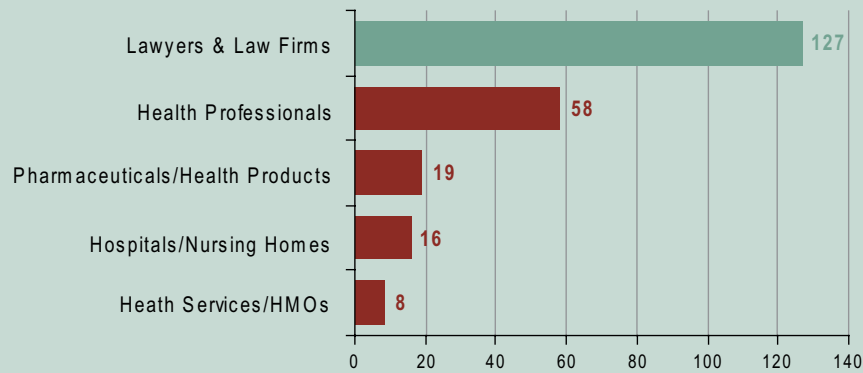
In his nationally televised speech before both houses of Congress on September 9, President Obama made news by acknowledging that medical-malpractice litigation “may be contributing to unnecessary costs” in the U.S. health-care system. The president’s comments were in keeping with popular opinion: 72 percent of Americans think that fear of lawsuits compromises doctor decisions, and fully 83 percent want any health-care reform to address medical-malpractice litigation.

Notwithstanding the president’s remarks and popular opinion, Congress has been laboring to *expand* medical liability against nursing homes, medical-device makers, and military doctors—changes that would be expected to drive up, not

down, health-care costs. The reason is simple: with massive campaign contributions and lobbying clout, the organized plaintiffs’ bar—whom the Manhattan Institute has dubbed “Trial Lawyers, Inc.”—has bought Congressional leaders’ support. In the last election cycle, the trial lawyers’ political action committee gave over \$2.5 million to Congressional Democrats, making the plaintiffs’ bar the second largest donor after the electrical workers’ union (see graph below). Overall, lawyers and law firms gave almost \$234 million to federal campaigns in 2008, including almost \$127 million to Congressional candidates—more than any other industry group and significantly more than all health-care-related contributions combined (see graph on opposite page).



The Lawsuit Industry Gives More to Congressional Campaigns than the Entire Health Care Sector



Donations to Congressional Campaigns, \$ Millions (2008 Cycle) Source: Center for Responsive Politics

In a moment of candor, former Democratic National Committee chairman Howard Dean admitted as much at an August 26 town hall meeting when he remarked, “The reason why tort reform is not in the bill is because the people who wrote it did not want to take on the trial lawyers.” Himself a medical doctor, Dean is well aware how America’s lawsuit-friendly culture skews medical decision-making and inflates costs. The tort system’s impact on health care stretches well beyond the “defensive medicine” that President Obama noted in his speech. Regardless of the merits or demerits of various portions of the health-care reform bills in Congress, the bills’ failure to address out-of-control litigation is a glaring omission that will limit any reform’s ultimate effectiveness.

THE COSTS OF MALPRACTICE LITIGATION

In noting that malpractice lawsuits “*may* be contributing to unnecessary costs” [emphasis added] in the health care system, the president was needlessly cautious. Thoughtful analysts of varying political stripes understand that litigation matters in explaining America’s high cost of health care. The respected left-leaning health economist Uwe Reinhardt, for instance, singles out “our uniquely American tort laws” as one of four “prominent” reasons for “excess” health spending.



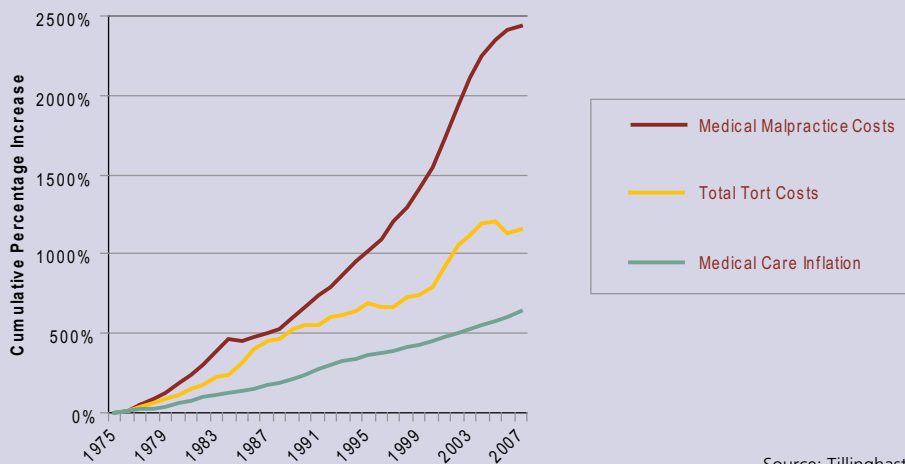
Howard Dean

AP Photo/Charles Dharapak

Trial lawyer lobby groups—the American Association for Justice and its assorted allies like Public Citizen and the Center for Justice and Democracy—regularly argue that litigation is an insignificant contributor to health care cost escalation because it only accounts for a tiny fraction of health costs. In making this argument, such organizations play the “denominator game”: the tiny fraction they point to takes the total \$2.2 trillion in U.S. health expenditures as its denominator and an absurdly narrow definition of health-care litigation as its numerator.

To begin with, such groups typically use as a numerator medical-malpractice losses as reported by insurance com-

Medical Malpractice Tort Costs Have Risen Far Faster than All Other Tort Costs and Medical Care Inflation



Source: Tillinghast-Towers Perrin

panies—numbers that ignore legal defense costs as well as the fact that most major health systems in the U.S. cover at least a portion of their medical malpractice losses without insurance. More comprehensive estimates by the insurance consulting firm Tillinghast Towers-Perrin place the total direct cost of medical-malpractice litigation at \$30.4 billion annually—an expense that has grown almost twice as fast as overall tort litigation and over four times as fast as health-care inflation since 1975 (see graph).

This direct cost represents only a portion of the cost imposed by medical-malpractice lawsuits. “Defensive medicine”—“the application of tests and procedures mainly as a defense against possible malpractice litigation, rather than as a clinical imperative”—is widespread. In a 2005 survey published in the *Journal of the American Medical Association*, 93 percent of doctors said they had practiced defensive medicine and 92 percent said they had made unnecessary referrals or ordered unnecessary tests or procedures. The cost of defensive medicine likely exceeds the total cost of malpractice liability itself because doctors themselves bear the cost of any potential litigation (even if their insurance companies cover their losses, doctors must endure the time, stress, and reputational effects of dealing with the lawsuit), while they bear little cost for imposing extra tests and procedures (since

patients with low-deductible health insurance are not price-sensitive, in part because the expenses are borne by their insurance companies).

Putting an estimate on the cost of defensive medicine is difficult. Many studies have extrapolated from a 1996 study by Stanford economists Daniel Kessler and Mark McClellan which found that tort reforms lowered costs by 5 to 9 percent without worsening health outcomes. Based on this study, PriceWaterhouseCoopers estimated that 10 percent of all health care spending is consumed by medical-malpractice-liability-related defensive medicine and insurance costs—a total sum of \$210 billion, or almost one-third the difference between the cost of U.S. health care and that in other developed nations.

Other academic studies using different methodologies have found more modest cost savings from state-enacted tort reforms, on the order of 2 percent of total health costs. Even this level of savings is not as small as it might at first appear. As explained below, medical-malpractice lawsuits are only a part of the total body of litigation affecting the health system and do not include other major classes of costly lawsuits, including suits against drug and medical-device manufacturers, nursing homes, and health

maintenance organizations. Expenditures on hospital and physician services constitute only 52 percent of all U.S. health expenditures, so a 2 percent cost saving from traditional tort reforms on medical-malpractice liability represents 4 percent of the portion of health spending relevant to such reforms.

In addition, the proper denominator for assessing the relative import of defensive medicine is not health spending *per se* but rather *excess* health spending. If U.S. health expenditures were reduced by one-third, the percentage of the American economy devoted to health care would be roughly on par with that of Canada, Germany, and France. Viewed thus, defensive medicine caused by medical-malpractice lawsuits that could be offset by traditional tort reforms, using conservative academic estimates, constitutes fully 12 percent of the relevant gap in spending between the United States and these comparable countries.

It is also worth emphasizing that academic estimates of defensive medicine do not fully capture the actual costs of defensive medicine *per se*; rather, they merely measure the impact of traditional tort-reform measures—damage caps, the allocation of liability among defendants, and insurance policy offsets—in bringing defensive-medicine costs down. Such reforms lower medical-malpractice litigation costs and deter speculative lawsuits, but they fail to correct fully the American tort system's problems in assessing causation and medical negligence. Such problems are substantial: Harvard researchers examining thousands of patient records have determined that the vast majority of medical-malpractice suits did not involve actual medical injury—and that most cases in which there was actual injury involved no doctor error. More systemic legal reforms that go beyond the traditional panoply of state solutions—such as loser-pays systems or specialized health courts—might be expected to reduce costs more than the traditional tort reforms measured by academic researchers.

C-SECTIONS AND CEREBRAL PALSY

John Edwards



AP Photo/Elise Amendola

One of the best examples of the costs of defensive medicine—and the litigation system's failure to improve health outcomes—is the increased use of Cesarean sections in the United States. While the five-fold rise in the number of C-section deliveries over the last thirty years stems from various factors, including mothers' choices, it is partly attributable to the liability imposed on doctors and hospitals who deliver babies born with birth defects, particularly cerebral palsy. Such liability can be massive: former Senator and presidential candidate John Edwards earned millions through such cases, including a jury verdict of \$6.5 million (reduced to \$2.75 million on appeal) and a settlement of a reported \$5 million; and some New York verdicts have topped \$100 million for a single case.

Although such lawsuits are highly lucrative for trial lawyers, they have not improved health outcomes. The cases are based on the theory that oxygen deprivation in delivery has caused an infant's cerebral palsy. Though such cases are not unknown, they are virtually impossible for a medical expert, let alone a lay jury, to assess with any confidence in an individual case: a January 2003 report issued by the American

College of Obstetricians and Gynecologists and American Academy of Pediatrics found that "that use of nonreassuring fetal heart rate patterns to predict subsequent cerebral palsy had a 99% false-positive rate." Little wonder, then, that a study in the March 2003 *American Journal of Obstetrics & Gynecology* found that notwithstanding the dramatic increase in C-section rates, the "rate of cerebral palsy has not decreased."

THE COSTS OF OTHER HEALTH-RELATED LITIGATION

Apart from lawsuits alleging malpractice on the part of doctors and hospitals, Trial Lawyers, Inc. profits handsomely from other forms of health-care-related litigation. The importance of other such litigation is evidenced by looking at attorney advertising for major litigation (excluding automobile accidents and slip-and-fall-cases). In 2004, medical-malpractice-lawsuit ads constituted 7 percent of all such spending (though such advertising has reportedly increased markedly in recent years), while ads seeking plaintiffs alleging nursing-home abuse represented 16 percent and ads seeking plaintiffs alleging injury from prescription pharmaceuticals represented fully 46 percent of all attorney advertising dollars.

The total cost of pharmaceutical litigation is harder to estimate than medical-malpractice liability, since large pharmaceutical companies self-insure against losses. The \$4.85 billion settlement that Merck reached with some 50,000 former Vioxx users in 2008 is illustrative of pharmaceutical litigation's cost. And Merck should not expect that the settlement will end its troubles; when Wyeth set aside \$13 billion to settle claims from former users of its diet drug cocktail Fen-Phen, it soon found costs were ballooning, up to a now-estimated \$21 billion.

Vioxx and Fen-Phen may be two of the costliest examples of pharmaceutical litigation, but they are hardly alone. On its website, the trial-lawyer lobbying group the American Association for Justice (formerly the Association of Trial Lawyers of America) lists thirty-three different drugs and medical devices as "litigation groups" through which plaintiffs' lawyers are "able to share accumulated information and experience, regarding a specific type of case."

Certainly, some of the products involved in litigation—including Vioxx and Fen-Phen—are harmful. But litigation in this area overlaps with extensive regulation by the federal Food and Drug Administration, and FDA-regulated companies often lack the discretion to modify product designs or labeling. Thus, tort lawsuits can do little more than increase

BENDECTIN AND BIRTH DEFECTS



In some cases, medical products targeted by the trial bar simply cease to exist—even when safe—because mounting legal bills make them too expensive to produce. The morning-sickness drug Bendectin was being used by 25 percent of expectant mothers in 1980, when trial lawyers generated a national panic over the unfounded claim that the drug was associated with birth defects. By 1983, when the drug's annual legal bills totaled 90 percent of its sales, the product was pulled from the market, and the incidence of hospitalization for morning sickness in the United States has doubled. Bendectin is still unavailable to American women, despite being safely sold elsewhere around the world and despite more than thirty published studies that have failed to establish any link between the drug and birth defects.

company costs, which are then, of course, passed along to consumers in the form of higher prices. For example, in the 1980s, as trial lawyers sued the manufacturers of vaccines that sometimes injure infants, overall vaccine prices doubled, while the most targeted vaccines—polio and diphtheria-pertussis-tetanus—saw prices rise 600 percent and 4,000 percent, respectively.

TRIAL LAWYERS, INC. TAKES WASHINGTON

In spite of clear evidence that litigation contributes to the high cost of health care in the United States, Congress is refusing to consider any serious efforts to reform the legal system. Instead, Congressional leaders are pushing legislation that threatens to *increase* litigation and *drive up* health-care costs, albeit to the substantial benefit of Trial Lawyers, Inc.:

- **Nursing homes.** The cost of long-term care for the elderly continues to escalate, fueled significantly by lawsuits: between 1992 and 2003, the litigation costs per bed at such facilities swelled by 700 percent. One way in which nursing homes have tried to lower such costs is by including arbitration agreements in contracts, so that disputes over care quality can be resolved without having to incur litigation costs. In reaction, leaders in Congress have introduced the Fairness in Nursing Home Arbitration Act of 2009 (H.R. 1237, S. 512) that would invalidate all such contracts—and increase the costs of caring for the elderly.
- **Medical devices.** In a 2008 decision, *Riegel v. Medtronic*, the U.S. Supreme Court determined, in an 8-1 decision, that certain state tort lawsuits against the manufacturers of FDA-approved medical devices were expressly preempted by the plain language of the 1976 Amendments to the Food, Drug, and Cosmetics Act. In response, Congressional leaders have introduced the Medical Device Safety Act of 2009 (H.R. 1346, S. 540), which would not only repeal the express statutory preemption clause but apply *retroactively* to all pending litigation that was filed before the law's enactment.
- **Military medicine.** In seeking to overturn Supreme Court decisions that place reasonable curbs on litigation, Congress is not limiting itself to recent holdings. The Carmelo Rodriguez Military Medical Accountability Act of 2009 (H.R. 1478, S. 1347) would reverse a 1950 Supreme Court precedent, *Feres v. United States*, 340 U.S. 135, which interprets the Federal Torts Claims Act to prevent active members of the military from

suing the government for medical malpractice related to their service on active duty. Veterans are undoubtedly a sympathetic group deserving of special treatment, and it certainly may be the case that military personnel are entitled to greater benefits for injuries or death. Veterans' injury benefits could be increased, however, without exposing the government to greater costs through liability—though such an approach would of course not help to enrich Trial Lawyers, Inc.

Another striking demonstration of trial lawyers' clout in Congress emerged this summer when House leaders were marking up health-care reform itself in committee. In what Manhattan Institute scholar Walter Olson called "one of the more audacious and far-reaching trial lawyer power grabs seen on Capitol Hill in a while," trial-lawyer ally Lloyd Doggett (D-TX) tried to insert language into the bill that would allow trial lawyers to sue defendants in Medicare-related disputes on behalf of the government—"notwithstanding the objections of the United States." Fortunately, committee Republicans were able to remove the language after strong objections.

A KEY PIECE OF THE PUZZLE

The U.S. health-care system is badly in need of reform. Views on the proper approach to reforming the medical system vary, but any reform intended to reduce the escalation of health-care costs should rein in litigation abuse. The president's announced intention to spend \$25 million on grants for state pilot programs is a worthwhile gesture, but little more than window dressing: the grants would constitute less than 0.003 percent of the reform bills' massive cost, and just over 0.001 percent of annual health expenditures.

Any serious health-care reform should instead take major steps to reform litigation in the health-care sector, including pharmaceutical and medical-device as well as medical-malpractice liability. Lawsuit abuse is hardly the sole factor underlying American health-care cost escalation, but it is a key piece of the puzzle.



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