New York 50A and B Award, Valuation and Deployment of the Net Award

Case resolution is plaintiffs' central focus, sometimes to the exclusion of resolving the matter to maximize plaintiffs' benefit. Often, this leads to a failure of funds to match needs created by the loss, the sell-off of parts or all of plaintiffs' annuities, failure of structured payments to keep pace with actual inflation, and serious deterioration of the value of the net Award.

Putting aside all of the razzle dazzle, there are only three things that count after liability is determined. They are

- The detailing and quantifying of past and future losses that make up plaintiffs' damage Awards.
- The valuation of that Award and incorporation of adjustments to arrive at net discounted awards by element of loss, together with any interest to be paid by the defendant.
- The resulting amounts of cash, or the sum of net discounted awards by element, past damages and lump sums, and how that cash is deployed for the benefit of plaintiffs.

Plaintiffs' attorneys need not be proficient in performing these tasks, but they should know the various components to gauge those who perform the tasks for them.

Development of the Award

The statutes are largely silent on how an Award is developed or the limitations associated with Award elements. In Med/Mal cases, Loss of Services and loss of Consortium are treated as lump sums (not discounted), and wrongful death Awards are the Net Award, not discounted. Awards for future Pain and Suffering are limited to 10 years under 50A and 50B, and 8 years under Amended 50A.

The Court has only addressed Award Development in a peripheral way by restricting recoveries to "pecuniary injuries", and limiting those recoveries to avoid unjust enrichment.

In practice, Awards are developed by factoring the initial cost for each element of loss for expected COLA, and multiplying the initial cost by the period over which payments will be paid (periodic payments) or, for discrete payments (lump sums) the number of events. The Award elements are then allocated between past and future damages.

Valuation of the Award

The Award elements are first converted to periodic (monthly) payments. Then the provisions of the statutes are applied

- To adjust the awards for any taxes,
- To allocate lump sums to the Award elements,
- To discount the remaining Award,
- To adjust for the discounted value of any Collateral Source offsets,
- To adjust for Plaintiffs' Litigation Expenses (Expenses and Disbursements), and
- To adjust for Plaintiffs' attorney fees.

Then interest is calculated and applied, as appropriate.

Taxes.

If taxes are to be applied as adjustments to lost or impaired earnings, they are to be applied either during the Award process or at the beginning of the Valuation process. When applicable, they are also applied as adjustments to past lost or impaired earnings. By statute, application of taxes are determined by the jury in Mad/Mal Wrongful Death cases and, after the verdict, by the Court and parties in other Med/Mal cases. The statutes are silent about application of taxes in 50B General Liability cases. This has been interpreted to mean that taxes are not applicable in these cases.

In the event that “unjust enrichment” is applicable to Awards for lost or impaired earnings under 50B, those taxes could be applied either in the process of developing the Award amount or as an adjustment in the valuation process.

Lump Sums

50A and 50B

The first $250,000 of future damages is to be paid in a lump sum, and allocated across the future loss elements based on the relationship of the element’s future loss to total future loss, before any discounting.

The value of each element is determined by dividing the amounts after application of lump sums by the period over which the payments are to be made to arrive at initial future monthly/annual payments. The stream of payments is then factored up by 4% for each year or part after the first year, and then discounted back to the date of the verdict (first payment is due on the date of the verdict, or -0- days).

Amended New York 50A

Under the amended 50A, Lump Sums are determined by

- Allocating the first $500,000 or 35% of future Pain and Suffering, whichever is larger, as a lump sum, and

- Allocating 35% of each other element of future economic or pecuniary loss, and discounting that amount to arrive at the element’s lump sum. The remaining 65% is the net future award.

The value of each element is determined by dividing the amounts after application of lump sums by the period over which the payments are to be made to arrive at initial future monthly/annual payments. Only the stream of payments for Pain and Suffering is factored up by 4% for each year or part after the first year. All streams are then discounted back to the date of the verdict (first payment is due on the date of the verdict or -0- days).

Discount Rates

Discount rates are set by reference to the 10-year Treasury Bond rate in effect on the date of the verdict. The subject of which discount rate to use was first addressed in Amended 50A. Since this is the first and only guidance, it is usual that it be applied to all 50A and 50B cases.

First, there are only 10-year Treasury Notes. The only rate in effect is the stated auction rate. Unfortunately, there are some forty issues in the market at any time, and all have somewhat different stated rates.

There are two other ‘rates’ related to 10-year Treasuries. The first is the yield at auction, or how much a willing buyer will pay for a 10-year Note of a given amount with a stated rate. This varies from the stated rate depending upon the demand for instruments.

Then there are the periodic yields generated from trades in the market for any given trading day, week, month or year. They are the average of the price paid in a set of purchases during the period. A number of insurers and courts seem to have adopted the yield on the date of the verdict as the rate in effect. The daily yield is never in effect. It is an historical average. It also does not meet the seeming dual purposes of stability and predictability. Only some average of auction rates or auction yields would seem to do that.

The discount rate is determined by use of the 10-year rate for all elements with a future period of 20 years or less, and a weighted average of the 10-year rate for the first 20 years, and 2 percentage points above the 10-year rate for years beyond 20 years.

Discounted Value

The value of each element is determined by dividing the amounts after application of lump sums by the period over which the payments are to be made and increased by any inflation factor dictated by the statute. The stream of future payments is then discounted back to the date of the verdict (-0- days) to arrive at the element's discounted value. That value is then reduced by the discounted value of related Collateral Source offsets, and allocation of plaintiffs' litigation expenses and allocation of attorney fees.

> [The statutes are silent about whether the allocations should be applied against element future damages prior to or after reduction for Collateral Source offsets. If applied after reduction there will be a significant disparity between the overall net value and the sum of net annual discounted values. If applied before Collateral Source offset (reduce the value of the Collateral Source by an allocation of litigation expenses and fees), the sum closely matches the overall net.]

The selection of discount rate more heavily impacts longer term future loss elements. In a somewhat typical future Award with 1/3 of the Award in the 10-year bucket, 1/3 in the 20-year bucket and 1/3 in the 30-year bucket, a change of 25 basis points (1/4%) in Treasury rate will produce an approximate 2.5% change in the total discounted Award including past damages and lump sums. Daily yields have most recently fluctuated wildly within a 50 basis point range (3.50%-4.00%). Over a longer 2-year period, the fluctuation has been 125 basis points.

Collateral Source offset is a future payment stream that is a substitute for some portion of future loss. It like in kind to a contractual obligation whose payment is certain, and which does not result in a statutory lien in favor of the provider of the payment. The only material condition on the continuation of the payment is the payment of any continuing maintenance payments (e.g. annual premiums). The offset cannot go beyond the period of the element's future loss. The Collateral Source is the sum of the future payments factored by any appropriate COLA rate, and reduced by any continuing maintenance. Collateral Source offsets can be spread across both past and future damages, and maintenance for the two years prior to the incident giving rise to the loss is applied to reduce the impact of the Collateral Source offset.

Plaintiffs' litigation expenses are divided by the sum of past damages, lump sums and the discounted value of future loss elements to arrive at a percentage, and that is applied against each to arrive at net values prior to application of attorney fees.

Attorney fees are determined by applying the sliding scale as set by statute (NY50A and Amended NY50A) to past damages, lump sums and the value of future damages after allocation of plaintiffs' litigation expenses to arrive at an overall average that is applied against the same past damages, lump sums, and the value of future damages (all net of litigation expenses) to arrive at a net Award. Attorney fees are determined by applying the negotiated rate (NY50B) against the past damages, lump sums, and the value of future damages (all net of litigation expenses) to arrive at a net Award.

Initial Monthly/Annual Payments are determined by dividing an element's undiscounted future damages net of lump sums by the element's future payment period. The initial payment for each element is then reduced by Collateral Source offset initial payments, and allocation of plaintiffs' litigation expenses and attorney fees.

Application of Interest

Interest is applied against the Net Total Award. The Net Total Award includes Past Damages, Lump Sums and the discounted value of future damages adjusted for Collateral Source offsets. Interest is applied

- **From the determination of liability to Verdict**.
  The date of death is the date of liability in Wrongful Death Actions. Case decisions provide that the Net Total Award excluding past damages be discounted back to the date of death. Past Damages are discounted back to the date of the individual items of loss or to some average past date. Interest is applied against that discounted amount.

In all other cases, liability is determined in the verdict and usually at the same time that damage Awards are returned (no interest to verdict). Occasionally, liability is determined at a point in time earlier than return of the Award. In those bifurcated cases, the Net Total Award is discounted to the earlier date then interest is applied. Interest is applied against that discounted amount.

- **From verdict to judgment**
  Interest is cumulative and the interest from verdict to judgment is applied against the Net Total Award or further discounted Net Total Award, plus any pre-verdict interest.

- **From judgment to payment**
  Interest is cumulative and the interest from judgment to payment is applied against the Net Total Award or further discounted Net Total Award plus any pre-verdict interest and pre-judgment interest.

Statutory interest is set at 9%, but it is not clear whether the statutory rate applies to the pre-verdict and pre-judgment periods as the interest is to be calculated by the Clerk of the Court. Accumulated interest is allocated between and added to plaintiffs' Net Award and Attorneys' fees.

Cash. This is the most important unused word in the entire statutory scheme. Cash is the amount that the defendant or its insurer is expected to pay out in the verdict or settlement. That cash includes

- Past damages for each element of loss
- Lump sum portions of future damages
- Plaintiff litigation expenses (expenses and disbursements)
- Attorney fees
- Net discounted future damages awards
- Interest.

Except for fees and expenses, this is Plaintiffs' money (a portion of the interest is allocable to attorney fees).

Liability carriers seem to believe that it is their right and obligation to determine the vehicles to be used for the payment of future damage streams and the providers of such vehicles.

Deployment of the Cash. The statutes provide that

> "The defendants and their insurance carriers shall be required to offer and to guarantee the purchase and payment of an annuity contract to make annual payments in equal monthly installments of the remaining streams of payments specified .... after deductions and adjustments..."

Taken literally, the offer and guarantee applies to a single annuity contract for all payments. In practice, different contracts cover different elements of loss. This provision imposes no obligation for the plaintiff to accept the offer, and there are no provisions which make the offer and guarantee all or nothing. As a result, the plaintiffs or their guardians should be free to pick and choose among the elements to structure, items to convert to cash, and how to deploy the resulting proceeds. The parties should be free, even after a verdict, to settle on reasonable terms.

> "Settlements. Nothing in this article shall be construed to limit the right of the plaintiff, defendant or defendants and any insurer to settle ... claims as they consider appropriate and in their complete discretion."

The Court of Appeals has recognized that the valuation and payment schemes are not meant to match those payments with the expected needs. Yet the entire damages scheme is designed to compensate for the current and expected losses encountered by the plaintiff. The only way that these needs can be met is by giving the plaintiff and counsel greater freedom in selecting deployment vehicles.

Discounting the Award and applying annuities were first employed to reduce the actual cash that the liability carrier was required to pay out, and to pay out funds to match the future needs as they occurred. If certain conditions were met, those payments were treated as the payment of the loss over time, and any gain was not subject to taxes. If the plaintiff were to take the cash and invest it, he/she would be compelled to pay taxes on the gain.

It has been a long held belief that this tax exemption made the annuities the better choice over other taxable vehicles. In a number of cases that is true, but only if the discount rate is high enough and, more importantly, the payment period is long enough. The benefit from an annuity can be determined by totaling the stream of payments, dividing them by the cost (net element Award), and subtracting 1. The result is the gain that is not subject to taxes.

- Any payment streams that last 15 years or less provide very small gains, and do not perform as well as investment in AAA taxable bonds, even when taxes are applied against the bond income.
- Any payment streams that last more than 15 years but less than 20 provide marginally better gains than investment in AAA taxable bonds, when taxes are applied against the bond income.
- As payment streams that last beyond 20 years, provide substantially better results than investment in AAA taxable bonds, when taxes are applied against the bond income.

If some of the future payments are for medical services or custodial care, they would normally be tax deductible when they exceed 7% of Gross Income. When that is factored in, the advantage of the trust extends well beyond 20 years. (The single disadvantage is that annuities guarantee payments, and trusts do not.)

The individual payment streams are set by statute, and are independent of the discount rate. The cost (net element discounted future damages award) is impacted by the discount rate chosen, but mostly in longer payment periods.

As a practical matter, the substantial throw off of uncommitted cash that often occurs independent of any cash out of shorter term elements of future loss, might warrant some level of protection similar to that offered by a trust. When shorter term future loss elements are added, the amount can be very significant. That resulting pool can be deployed to produce taxable income. The advantages would be

- Matching Payments to prospective needs of plaintiffs.
- Adjusting future payments for expected inflation.
- Adjusting those payments to meet unanticipated needs, and with only minor penalties.
- Adjusting the investments to keep pace with increasing inflation.
- Protecting the principal from dissipation to some extent.
- Providing for the future needs of heirs or dependents.

Verdict and Settlement Negotiation

In the post-verdict negotiations, the primary foci are

- Alterations to the Award through Taxes and Collateral Source offsets.
- Application of discount rates to future damages and Collateral Source offsets.
- Calculation of interest associated with the Award.
- Deployment of the proceeds.

In settlement negotiations, add alterations to Award element.

Conclusion

We believe that there are a series of steps to take to achieve timely resolution of an Award, a full and fair Award and deployment that both matches the plaintiffs' needs and protects principal. It is critical that plaintiff have confidence in those providing Award, Valuation and Deployment services and in protecting the attorney work product.

A. Develop the Award early in the process, and update it on a regular basis.
   1. Apply Collateral Sources and adjustments, as appropriate
   2. Apply taxes to lost or impaired earnings, when appropriate
   3. Allocate elements of loss, taxes and Collateral Source offsets between past and future damages
   4. Specify whether the Action is Wrongful Death, and determine an average date applicable to Past Damages.

B. Value the Award early in the process, and update it on a regular basis.
   1. Use the Award, if available
   2. Develop the valuation, Apply taxes and Collateral Source offsets, as appropriate.
   3. Apply the appropriate discount rates.

C. After a verdict, apply interest and any 2nd level discounting to the valuation, as appropriate.

D. If liability or level of liability are not significant questions, propose a settlement that incorporates
   1. Full Award and Valuation
   2. A reconciliation of Gross Award to Net Valuation
   3. Detailed Monthly and Annual payments by element
   4. Detailed discounted value by element by year.
   5. A listing of future loss items to be reduced to cash

E. Evaluate the deployment of future damages and shift to cash, as appropriate.
   1. Compare the cost with each element's Stream of payments
   2. Select which elements that remain as annuities
   3. Project the trust sums including the elements of future loss, some or all of the lump sum amounts and past Pain and Suffering.
      - Apply a broker fee or load
      - Select future bond rates to apply
      - Apply any trust administration expenses and any tax preparation costs
      - Apply a Tax to the trust gains
      - Choose which elements and amounts are to be paid through the trust
      - If any elements are tax deductible medical expenses, determine whether and how much they will reduce the tax burden
      - Choose how and when to distribute any remainder

Submitting a complete detailed Settlement offer before trial puts resolution in play. The other party is placed in the position of having to make a good faith, timely response. If plaintiff waits for settlement or suggests amenability to settlement, moves nothing that would not help otherwise.

The timing of any pre-trial settlement offer will vary from case to case. The timing of post-verdict offers is tied to issues of post verdict motions and ancillary matters. Submitting a complete detailed offer after trial again places the other party in the position of having to make a good faith, more timely response.