

Collateral Source Offsets

The Burbank Group

Collateral Source Offsets are obligation to make payments that will replace or indemnify, in whole or in part, past and payments related to elements of loss. Those loss elements include any earnings or other economic loss, or care, custodial care, rehabilitation or treatment costs sought to be recovered. The indemnification source may be from insurance (excluding life insurance), Social Security Survivor benefits, Workers Compensation or employee benefits.

The Court has imposed a requirement of direct correspondence between items of loss and the collateral reimbursement. "The Court must also find that the plaintiff is legally entitled to the continued receipt of such collateral source, pursuant to a contract or otherwise enforceable agreement, subject only to the continued payment of a premium and such other financial obligations as may be required by such agreement." To qualify as a Collateral Source offset, it must be reasonably certain of payment. That has been interpreted to mean that the only allowed material condition precedent to continued payment of the offset be the payment of any ongoing premium or maintenance cost. To be an offset, it cannot give rise to a statutory lien in favor of the person providing the payment.

While not fully specified in statute or case decision, the impact of a Collateral Source offset can be calculated, as follows;

- Reduce the offset periodic payment by any continuing premium payment
- Establish the period over which the offset will extend. (As an offset, the period should not be longer than that of the related element of loss and, in Med/Mal Wrongful Death, it would seem that it should not include any future periods as future loss is paid as a lump sum.)
- Apply a reasonably expected COLA or inflation to the net offset payment, and then discount the future stream of payments. (It would seem appropriate that the discount rate should be the same as that applicable to the loss element.)
- Allocate loss amounts and related net offset payments to past and future damages.
- Apply any maintenance during the two years preceding the event of loss to increase past damages or reduce the future offset value.

For any element of economic loss to which taxes are applicable, the loss should be adjusted by the sum of the offset payments before applying taxes. The net tax should then be deducted from the element of loss before adjustment. The effect is the reduction of taxes applicable to the economic loss.

Adjustments to Initial Payments

The genius of the statutory scheme under Article 50 is that, if followed, the overall net value for an element will agree with the total of the annual discounted values for that element. It works if both methods of calculation are employed, and if the element is not impacted by a Collateral Source offset. As set out in the statutes, an element's initial monthly payment is determined by

- Dividing the future Awards after lump sum deductions by the period over which payments are to be made to arrive at an initial monthly/annual payment.
- Reducing that initial payment by application of effective expense and fee rates. (Not some combined rate but first the expense to produce an interim amount then the fee against the interim amount.)
- Reducing that payment by the net, initial collateral source offset payment.

All discussion of Collateral Source offsets talk to determining and applying the discounted value. To be effective, loss element payments must be adjusted for related offset payments. If total offset payments are discounted and applied against the related element's annual discounted value, that total net value will be smaller than the overall net value for the element.

To bring the amounts to agreement, expense and fee rates should be applied to adjust initial offset payments. The net result is close agreement between total net discounted payments and the overall net value for the element. It also means that the net element payments against which offsets were applied will be larger. It also means that offsets should be incorporated into both the Award development and the Valuation.

The following schedules outline the various discrete steps for calculating and adjusting lost or impaired earnings payments and related Collateral Source offsets under 50A and 50B. (Attachment A. Incorporates the detail.)

	<u>Am. 50A</u>	<u>Orig. 50A</u>	<u>Orig. 50B</u>
Initial Gross Monthly Payment	\$4,424	\$6,389	\$6,389
Offset Impact of Taxes	\$40	\$57	
Total	\$4,464	\$6,446	\$6,389
Expense Allocation (2.00%)	(\$89)	(\$129)	(\$128)
Fee Allocation (12.5%)	(\$507)	(\$790)	(30.0%) (\$1,878)
Initial Net Monthly Payment	\$3,828	\$5,527	\$4,383
Gross Monthly Offset	(\$300)	(\$300)	(\$300)
Net Monthly Pay't less Gross Offset	\$3,528	\$5,227	\$4,083
Offset Exp. Adj.	\$6	\$6	\$6
Offset Fee Adj.	\$37	\$37	\$88
Net Initial Monthly Payment	\$3,560	\$5,270	\$4,177
Simple Addition of Rates Adj. (14.5%)	(\$15)	(\$15)	(32.0%) (\$37)

The key offset points are

	<u>Am. 50A</u>	<u>Orig. 50A</u>	<u>Orig. 50B</u>
Initial Net Monthly Payment	\$3,828	\$5,527	\$4,383
Net Monthly Offset	(\$257)	(\$257)	(\$206)
Net Initial Monthly Payment	\$3,560	\$5,270	\$4,177
Net Monthly w/o Offset Adj.	\$3,528	\$5,227	\$4,083
Net Increase in Monthly Payment	\$32	\$43	\$106

There are two other incidental issues related to Collateral Source offset.

- Amended 50A provides that the first payment of the future Award be the date of the verdict unless otherwise provided in the verdict. In insertion of a future date would seem to create an additional condition related to any payment of an offset.
- Collateral Source Offsets are not presented to the jury for assessment, but are determined by the Court and the parties after the verdict is returned.

Attachment A.

Lost or Impaired Earnings - discount 3.50%									
	<u>Tot. Award</u>	<u>Taxes</u>	<u>Net</u>	<u>Lump Sum</u>	<u>Net Total</u>	<u>30 Years Payments</u>	<u>After Expense</u>	<u>After Fee</u>	<u>Single Applic</u>
		30.00%				360	2.00%	12.50%	14.50%
Amend. 50A	\$3,500,000	\$1,050,000	\$2,450,000	\$525,277	\$1,592,500	\$4,424	\$4,335	\$3,793	\$3,782
Off Pay'ts	(\$75,000)	(\$22,500)							
	\$3,500,000	\$1,027,500	\$2,472,500	\$529,851	\$1,607,125	\$4,464	\$4,375	\$3,828	\$3,817
Mo. Offset						(\$300)	(\$294)	(\$257)	(\$257)
Net Monthly						\$4,164	\$4,081	\$3,571	\$3,560
Low		\$3,482							
High		\$3,571							
Range	2.55%	\$89							
	<u>Tot. Award</u>	<u>Taxes</u>	<u>Net</u>	<u>Lump Sum</u>	<u>Net Total</u>	<u>30 Years Payments</u>	<u>After Expense</u>	<u>After Fee</u>	<u>Single Applic</u>
		30.00%				360	2.00%	12.50%	14.50%
Orig. 50A	\$3,500,000	\$1,050,000	\$2,450,000	\$150,000	\$2,300,000	\$6,389	\$6,261	\$5,478	\$5,463
Off Pay'ts	(\$75,000)	(\$22,500)							
	\$3,500,000	\$1,027,500	\$2,472,500	\$152,000	\$2,320,500	\$6,446	\$6,317	\$5,527	\$5,511
Mo. Offset						(\$300)	(\$294)	(\$257)	(\$257)
Net Monthly						\$6,146	\$6,023	\$5,270	\$5,255
Low		\$5,163							
High		\$5,270							
Range	2.08%	\$108							
	<u>Tot. Award</u>	<u>Taxes</u>	<u>Net</u>	<u>Lump Sum</u>	<u>Net Total</u>	<u>30 Years Payments</u>	<u>After Expense</u>	<u>After Fee</u>	<u>Single Applic</u>
		30.00%				360	2.00%	30.00%	32.00%
50B	\$3,500,000	\$1,050,000	\$2,450,000	\$150,000	\$2,300,000	\$6,389	\$6,261	\$4,383	\$4,344
	\$3,500,000	\$1,050,000	\$2,450,000	\$150,000	\$2,300,000	\$6,389	\$6,261	\$4,383	\$4,344
Mo. Offset						(\$300)	(\$294)	(\$206)	(\$204)
Net Monthly						\$6,089	\$5,967	\$4,177	\$4,140
Low		\$4,044							