RALLYING FOR REFORM

Lawmakers Pressed on Malpractice

A year after West Virginia "fixed" its tort system to make malpractice insurance more affordable and available, medical professionals elsewhere in the Fifth District are having insurance problems, especially certain specialties like obstetrics and trauma care. While the American Medical Association says the situation has reached a crisis level only in North Carolina and West Virginia, lawmakers throughout the region are being lobbied hard to follow the Mountain State's lead.

CHARLES GERENA/FRB OF RICHMOND

Physicians lobbied outside of the Virginia State Capitol in February for changes to the state's medical malpractice rules.

In March 2003, the West Virginia Medical Professional Liability Reform Act changed several aspects of the state's tort law. The bill's provisions included a $250,000 limit on "pain and suffering" damages and a $500,000 overall cap on damages paid by trauma centers.

Since then, the West Virginia Hospital Association has noted an improvement in recruitment efforts at the state's hospitals. Still, the state has only one major private provider of malpractice insurance — Medical Assurance of West Virginia — and its parent company stopped providing it reinsurance last December. Another firm, NCRIC Inc., announced in January that it wouldn't renew its malpractice policies in West Virginia as they expire.

Other parts of the Fifth District don't have such a limited market for malpractice insurance. But some have experienced significant increases in premiums, and that has doctors worried about the future. In the last 12 months, physicians converged on statehouses in Virginia, Maryland, North Carolina, and South Carolina to rally for changes in tort law.

Two proposed reforms could help reduce the number of frivolous lawsuits, which doctors and insurers say have pushed up malpractice costs. One proposal would require plaintiffs to pay for defendants' legal bills if they lose. Roy Cordato, vice president for research at the John Locke Foundation in Raleigh, N.C., believes this would bring balance to a system where the potential payoff from a suit is much higher than the expense of filing a case. "The lawyer doesn't look at the legitimacy of the complaint," explains Cordato. "What he looks at is the probability of getting a settlement." And the odds are in the plaintiffs' favor because defendants often settle out of court to avoid a big jury award.

Another reform proposal would subject malpractice lawsuits to arbitration or a review panel of medical experts before trial. G. Robert Thompson, an economist at Clemson University, believes the latter would help discourage frivolous lawsuits.

But other tort reforms are more problematic. For instance, caps on jury awards haven't been proven to affect the price of malpractice insurance, and Thompson suspects that caps may encourage incompetent doctors to migrate to a state because they know their liability is limited.

Another imperfect solution, which is being considered in West Virginia, is to start a patient injury compensation fund. South Carolina created such a fund in 1977 that pays for any part of a malpractice judgment or settlement over $200,000. Virginia created a more specialized fund in 1987 that pays for lifelong medical care for infants that suffer brain injuries at birth. But both programs are underfunded and they have no upper limit on payouts. They also don't charge deductibles, co-payments, or any other form of cost sharing that would shift some of the risk burden onto doctors. Consequently, physicians have no incentive to avoid lawsuits, creating a moral hazard problem according to Thompson.

Cutting back on the number of lawsuits and the size of jury awards alone does not make malpractice insurance more available or affordable, since certain market forces are also driving the current premium increases. Still, there is relatively broad support for tort reform among economists, who see it as a good first step toward fixing a very difficult problem.

—CHARLES GERENA

BAD CONNECTION

Southwest Virginia Loses Call Center

Internet travel agency Travelocity.com has announced plans to close its call center in Clintwood, Va., by the end of 2004, putting roughly 250 people out of work. Clintwood is in Dickenson County, in the state's southwest corner, an area that has suffered economic hardship in recent decades. Dickenson's population has fallen from a peak of 23,000 in 1950 to 17,600 in 2000. As of December 2003, the county's unemployment rate stood at 11 percent.

Some of the work done in Clintwood will be sent to a facility in India. Similar outsourcing recently has occurred at call centers operated by other companies in the Fifth District. (See Charles Gerena's article, "On Hold: Fifth District Call Centers Are Shedding Workers Due to Technological Improvements and Globalization," from the Winter 2004 issue of *Region Focus*.)

Travelocity originally planned to employ up to 500 people at the Clintwood facility, which opened its doors in mid-2001. But sluggish business for the travel industry following the terrorist attacks of Sept. 11, 2001, reduced the demand for workers.

The Virginia Coalfield Economic Development Authority and the Dickenson County Industrial Development Authority courted Travelocity, with the county taking out a $250,000 loan to improve the company's call-center facility. (For more on economic development incentives see Karl Rhodes' article, "The Baiting Game," on pp. 20-23 of this issue.) —AARON STEELMAN

ELECTRIC DEBATE

Is Deregulation Working?

It seemed like a great idea. And it may turn out to be a great idea yet. But, so far, efforts to deregulate the electric industry have fallen short of their original promise.

"I've been somewhat disappointed at the way deregulation has unfolded," says Jack Reasor, president and chief executive officer of Old Dominion Electric Cooperative, headquartered in Glen Allen, Va. Before joining Old Dominion, Reasor was chairman of the Senate Subcommittee on Electric Utility Restructuring in the Virginia General Assembly. "I question whether it [deregulation] can work in the electric utility industry," he says candidly.

A lot of people share Reasor's doubts these days, particularly in California, where the restructuring of electric markets began in earnest in the late 1990s. A firm belief that competition would lower the state's high electric rates led to fundamental changes in state laws and regulations affecting the ownership of generating plants and the way wholesale electricity markets functioned. California's efforts to deregulate its industry were among the earliest and most comprehensive in the nation.

Unfortunately, California's deregulation plan failed miserably. By June 2000, the state was experiencing soaring wholesale prices for electricity, and by 2001 there were rolling blackouts and a big-time crisis. While other factors, such as a time-consuming process for licensing new generating plants and unusually hot, dry weather, contributed to the problems, the California restructuring plan was clearly flawed.

California's experience with deregulation was sobering for those developing restructuring plans in other states. The Enron scandal and issues with manipulation of wholesale markets raised further questions about the feasibility of deregulation

Even in states that managed to avoid California's calamities, there was growing suspicion that deregulation helped only a select group of consumers. "Whether deregulation has been a success or not depends on whom you talk to," says Robert Burns, a senior research specialist with the National Regulatory Research Institute in Columbus, Ohio. "Large commercial and industrial customers have benefited, but there hasn't been much benefit at all for residential customers."

Legislators in several Fifth District states have acted in recent months to either slow down electric deregulation or better protect consumers from potentially higher electric rates in a more deregulated environment. Legislation passed in the 2004 session of the Virginia General Assembly calls for an extension of electric rate caps until Dec. 31, 2010, unless ended sooner by a finding that a competitive market for generation exists. (Rate caps are a common feature of deregulation plans and offer consumers some protection against volatile price swings during the transition to more competitive markets.)

Among the legislative proposals in Maryland to protect customers from rate shock is Senate Bill 739, which restricts residential rate increases to no more than 10 percent in any one year.

Despite the setbacks in California and elsewhere, the debate over restructuring will continue. Competitive markets have great allure, and economists certainly prefer them where possible.

And amid the setbacks, there have been some overlooked success stories in deregulation, which hold promise for future restructuring efforts. William Hecht, chairman of PPL Corporation, an electric utility headquartered in Allentown, Pa., says Pennsylvania "got it right." The state's restructuring effort gives each electric customer the option of choosing an electricity supplier. He credits a system that allows new electric-generating capacity to be built "in response to economic price signals, not through the old central planning approach," as a key to Pennsylvania's success. Restructuring efforts in Texas and Ohio have also garnered praise.

There is even talk about giving deregulation another shot in California. New governor Arnold Schwarzenegger is an advocate but, not surprisingly, strong opposition exists. —ROBERT LACY