Attorney Fee Based on Present Value

A Look at the DEU Calculations

First Case

One of our customers asked me to look at a present value/attorney fee commutation done by the Disability Evaluation Unit (DEU). Attached to an email were the award and the DEU calculation sheets. It didn't take long to find problems with the case.

Award Should Not Specify Rate of First Payment of Life Pension

One problem is the last sentence of paragraph 4 of the award. Paragraph 4 says:

> 4. The injury caused permanent disability of 97 percent equivalent to 689.25 weeks at $250 per week, in the total sum of $172,312.50 payable beginning November 16, 2006, with a life pension payable thereafter pursuant to the Labor Code. After deduction for attorney fees, permanent disability will be paid at the weekly rate of $205.51. The life pension shall be paid at the rate of $107.87 per week.

It is not clear that State Average Weekly Wage (SAWW) increases are to be applied in the future to the weekly rate of $107.87. Maybe the language "with a life pension payable thereafter pursuant to the Labor Code" takes care of that but I doubt it.

According to the DEU printouts, the $107.87 is the statutory life pension rate of $143.02 minus $35.15 per week for commuted attorney fee on the life pension.

Even if the language of "pursuant to the Labor Code" were interpreted as allowing for SAWW increases, the increases will undoubtedly be calculated incorrectly in the future. The percentage increase would only apply to 107.87 rather than 143.02 as it should.

Even if the language of "pursuant to the Labor Code" were interpreted as allowing for SAWW increases the award does not state when the increases start. Do the increases start January 1, 2004, or at the date of injury or when permanent and stationary (P&S) or at the time of the first life pension payment?

The language of awards is archaic. The award uses language from when life pensions were not subject to Cost of Living Adjustment (COLA). The award in this case isn't alone. Awards that I have seen specify an exact amount as the payment of the life pension and they shouldn't.

First, the amount of the first payment is unknown at the time of the issuance of the award and depends on the actual SAWWs between the issuance of the award and when the first payment is due.

Second, the language of the award also does not make it clear that the life pension rate increases for life. By only specifying an exact amount for the life pension an insurance company would be justified in not making COLA increases.

What’s a claims administer going to do with this in the year 2019 when the life pension kicks in? Who knows, but it probably won’t be favorable to the applicant. The applicant’s attorney should expect a telephone call about that time – if he or she is still around.

DEU Template E Should Not Be Used To Compute Present Value of Life Pension

Not just the award but even the DEU got it wrong in this case. To get the present value of the life pension the DEU used the template entitled, “E) COMMUTATION OF ALL REMAINING LIFE PENSION BEFORE COMMENCEMENT OF LIFE PENSION.” The rater correctly plugged in the starting weekly payment based on SAWW increases from January 1, 2004 to the date that the life pension payments start. The template gave out a present value. But that template does not consider any increases after the start of payments. That template only computes a present value for a fixed weekly life payment. The present value reported by the DEU was $41,000 too low. That makes a difference in attorney fee of $6,142.22. Big difference.

The award should not state the amount of the projected starting weekly payment rate of the life pension. That amount is unknown at the time of the award and depends on actual values of SAWW between the time of the award and when the life pension payments commence. The actual starting payment would be different from that specified in the award and would be interpreted as never increasing. When the award specifies an amount for the starting payment it can be interpreted as a fixed or constant amount that never increases. The award should just say something like this:

> Applicant is awarded a life pension in accordance with the labor code with payments commencing <total weeks of PD> weeks after <P&S date> at the weekly rate of $<rate based on DOI and earnings> per week with increases of the weekly rate for SAWW starting on January 1, 2004, and continuing for life with 15% deducted from each life pension payment for commuted attorney fee.

Second Case

A customer asked me to look at another case. In this case the DEU says it has done the calculations according to the Duncan case. The Duncan case said that the SAWW increases are to start on January 1, 2004.

The rating was 73%. This should be a typical case. Attorneys must run into this many times. When a rating is 70% or more the applicant is entitled to a life pension.[1] This makes a big difference in benefit for the applicant. The applicant gets two benefits: a permanent disability (PD) benefit paid at a higher rate but which terminates after a specified number of weeks; and a life pension benefit payable for life commencing after the permanent disability payments end.

[1] Labor Code Section 4659(a)

The total payout of a 73% permanent disability with a date of injury in 2004 is 473.25 weeks multiplied by $250 per week for a total payout of $118,312.50.

Present Value of the Permanent Disability Benefit

Commutation is the process where the entire attorney fee is paid to the attorney in a lump sum at the time of the award. If the attorney fee were not commuted each payment would be reduced by the attorney fee and paid to the attorney. The applicant and attorney would each get a biweekly check. This is not desirable for the attorney. The attorney would rather have the entire fee paid immediately rather than a small amount paid over a period of time.

Essentially the attorney is cashing out an annuity. The cash-out value is less than the total payout. From the insurance company's point of view it is like paying off a loan early. The payoff is less than the total payout.

When the attorney fee on PD is commuted the fee is based on the present value of the PD benefit not the total pay-out. In this case the present value of PD is less than $118,312.50 if payments remain to be made.

The way the DEU commutes the attorney fee on the permanent disability part is the same way the Med-Legal calculator does it. The present value of the permanent disability is calculated and 15% of that is the attorney fee. The present value where payments have begun is the amount that should have been paid plus the present value of future PD payments. There is no discount on amounts that should have been paid because the present value is the actual value. The future payments are discounted by 3%.

It does not matter what has been advanced or has been underpaid or overpaid. Only what should have been paid. The attorney fee is being computed and not the amount of a check for the applicant.

The attorney fee gets reduced by the commutation. The attorney fee is not 15% of the total payout. In this case the attorney fee is not 15% of $118,312.50 or $17,746.88. The attorney fee is 15% of the amount that should have been paid plus 15% of the present value of the remainder.

For example, if it were 64.71 weeks from the date of permanent and stationary (P&S) until the date of commutation[2] (DOC). The amount that should have been paid is $16,178.57. The attorney fee on that amount is $2,426.79.

As an aside, the date of commutation (DOC) may be, and usually is, different from the date that the calculations are made. The calculations can be made well before the award is issued but be calculated as of the date of the expected award.

In this case there is 408.54 weeks of future payments still to be paid. The present value of that is $91,124.80. The attorney fee on that amount is $13,668.72. The attorney fee on the amount that

[2] This is the date used in the calculation. It may not be the same as the date when the calculations were performed.

should have been paid is $2,426.79. The total attorney fee is $2,426.79 + $13,668.72 = $16,095.51. This is less than the fee on the total payout given above as $17,178.57. In this way the attorney pays for the commutation and not the client. The attorney is getting the benefit of the commutation and the client is getting no benefit from the commutation of attorney fee

This method of calculating the attorney fee on the permanent disability benefit using the present value isn't usually done for ratings below 70%. Usually there is not a significant difference between the payout and the present value.

Total Fee on Permanent Disability is Deducted from Future Permanent Disability Payments

When the amount that should have been paid to the applicant has been paid with no amount withheld for attorney fee there is no fund in which to pay the attorney fee on the amount-due portion. In this case the $2,426.79. This amount will also have to be commuted from the remaining payments.

Where nothing has been paid for attorney fee and the amount that should have been paid for PD by the time of the date of commutation has been or will be paid to the applicant, the entire amount of attorney fee on PD of $16,095.51 needs to be deducted from the remaining PD payments. It can be deducted by taking an equal amount from each payment or "off the far end".

Off the Far End

The off-the-far-end method is where payments continue at the normal weekly rate ($250) with no deduction but then stop when there is $16,095.51 plus interest[3] yet to be paid.

The disadvantage of the off-the-far-end when the rating is 70% or more is that there is a gap between when PD payments stop and the start of the life pension. The client would get no payments during this period. Unless the client really understood this was going to happen and was prepared for it, the attorney should expect an unpleasant telephone call or worse.

There are no surprises where a deduction for the commuted attorney fee taken from each of the remaining PD payments.

There is not such a problem with the off-the-far-end method when the rating is below 70% -- as long as the client agrees to this method.

I agree with the DEU's calculations regarding the commutation of attorney fee from the **permanent disability** benefit. It's the life pension part that I don't agree with.

Life Pension

Keep in mind that the life pension does not start until all of the permanent disability payments have been paid. For a date of injury in 2004 the number of weeks of PD is 473.25 for a 73% rating. So, the

[3] DEU template B is used to compute number of weeks off the far end.

applicant would be paid PD at the rate of $250 per week for 473.25 weeks for a total of $118,312.50. The applicant would receive the PD payments until the year 2019 then the permanent disability payments would stop[4]. At that point in time the applicant would begin receiving life pension payments.

For the PD part, the Med-Legal calculator comes out with the same values as the DEU.

The present value of the permanent disability benefit does not consider COLA increases, the U.S. Life Tables and the probability of not living to collect the payments and I agree it should not. The tables in the Labor Code for PD are still good. It's the life pension that always is the problem. The tables are not good for determining the present value of a life pension where there is a COLA.

The Actual Starting Rate for Life Pension is Unknown

The exact life pension weekly payment rate is unknown at the time of the award and is not known until the time of the first payment is made. This is because the actual SAWW increases will not be known until them. An assumed starting life pension rate is needed to compute the present value of the life pension. The present value of the life pension is needed in order to calculate the attorney fee on the life pension.

I agree with the method used by the DEU to calculate the estimated starting life pension payment rate.

The way this is done is to compute the life pension rate based on the weekly earnings within the maximum allowed (which depends on the date of injury) and the rating. The formula is in the labor code.[5]

5) Estimated Future LP Rate Calculator

Annual rate increase:	4.60%
Initial rate:	$62.59
First year:	2011

Year	Rate	
1	62.59	2011
2	65.47	2012
3	68.48	2013
4	71.63	2014
5	74.93	2015
6	78.37	2016
7	81.98	2017
8	85.75	2018
9	89.69	2019
10	93.82	2020
11	98.13	2021
12	102.65	2022
13	107.37	2023
14	112.31	2024

Computing the Assumed Starting Life Pension Rate

That assumed starting rate is increased yearly by the actual SAWW increases for the already reported SAWW numbers[6]. For the years that there are no reported numbers, the assumed increase of 4.6 is used. The assumed starting rate is the rate in the year that the life pension payments start. In this case the life pension payments would start in the year 2019. The assumed starting rate would be $89.69.

This is what it looks like in the DEU calculations:

This assumed starting life pension rate is needed to calculate the present value of the life pension and the amount of the attorney fee. But it should not be used to calculate the actual starting deduction for the commuted attorney fee.

[4] If attorney fee wasn't taken off the far end.
[5] Labor Code Section 4659
[6] Before 2011

The DEU spreadsheets give the weekly deduction for commuted attorney fee on the life pension as $21.28. The rater got this by using Example G of the DEU spreadsheets[7]. The life pension starting payment was given as $86.69[8]. This would be 25% of the starting payment.

The calculation is correct but using this method is not what the applicant would want if given an informed choice.

Uniform Reduction (UR) or Uniform Increasing Reduction (UIR)

With the Uniform Reduction method a constant, fixed amount is deducted from each life pension payment. The amount deducted does not change.

With the Uniform Increasing Reduction method the life pension payment is increased yearly depending on the percentage of the actual increase in SAWW for the previous year. The percentage attorney fee as specified in the award is then deducted.

In this case the DEU used template G to compute the amount to be deducted for the Uniform Reduction method. The UR method results in a constant amount being deducted from each payment.

Just to clarify. The deductions using either method do not ever stop. The deductions do not stop after the accumulated total is equal to the attorney fee. The attorney fee never gets "paid off". As long as the applicant lives there is a deduction from the payments for the commutation of the attorney fee.

There is no off-the-far-end method for a life pension. The date for the far end is unknown. The far end is the date of death of the beneficiary. That is unknown. The insurance company would not be able to determine the date when payments should stop. Waiting until the beneficiary dies to determine the stop-payment date would be too late.

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[7] http://www.dir.ca.gov/dwc/commtemps.zip Example G is not in the 2011NexisLexis Labor Code.

[8] Should have been 89.69. Rater made typo in transferring the numbers.

Do Not Use DEU Template G

G) COMMUTATION OF A PORTION OF DEFERRED LIFE PENSION BY UNIFORM REDUCTION OF LIFE PENSION

Date of birth:	11/23/53	Total weeks PD:	473.25
DOI:	02/29/04	Life pension rate:	$86.69
PD start:	01/15/10	Gender:	FEMALE
DOC:	04/12/11	Amount to commute:	$11,219.70

1	**Determine exact age in years as of date of commutation (DOC).**	
1a	# of days from DOB through DOC	20959
1b	Divide by average number of days per year)	365.24
1c	Exact age on DOC	57.384
2	**Determine number of years between DOC and LP commencement.**	
2a	Total weeks of PD	473.25
2b	Multiply by 7 days per week x	7
2c	Total days of PD	3312.8
2d	Subtract #days from PD commencement through DOC inclusive -	453.0
2e	Number of days from DOC to LP commencement	2859.8
2f	Divide by average number of days per year)	365.24
2g	Period in years from DOC to LP commencement (i.e. deferral period)	7.830
3	**Determine PV of life pension for exact age and deferral period.***	
3a	Enter PV for age 57 and deferral period 7	567.09
3b	Enter PV for age 58 and deferral period 7 -	547.68
3c	Difference of 3a and 3b	19.41
3d	Multiply by fractional portion of 1c x	0.384
3e	Interpolation adjustment for age	7.45
3f	Enter PV for age 57 and deferral period 7	567.09
3g	PV for age 57 and deferral period 8 -	528.13
3h	Difference of 3f and 3g	38.96
3i	Multiply by fractional portion of deferral period (from 2g) x	0.830
3j	Interpolation adjustment for deferral period	32.34
3k	PV for age below 1c and deferral period below 2g (3a from above)	567.09
3l	Subtract sum of 3e and 3j -	39.79
3m	PV for exact age and deferral period on DOC	527.30

* Take values from Table 2 - Present Value of Life Pension for a Male, or Table 3 - Present Value of Life Pension for a Female, as dictated by gender.

4	**Calculate amount of reduction in LP rate necessary to produce lump sum.**	
4a	Amount to be commuted	$11,219.70
4b	Divide by 3m)	527.30
4c	Amount of weekly reduction in LP	$21.28
5	**Calculate LP rate after commutation.**	
5a	LP rate before commutation	$86.69
5b	Subtract weekly reduction in LP (4c from above) -	21.28
5c	LP rate after commutation	$65.41

Here is the DEU template G:

Using the Uniform Increasing Reduction (UIR) method the projected starting deduction would only have been $13.00. The UIR method bases the reduction on the percentage of attorney fee awarded.

Using the UR method of template G the constant deduction is $21.28.

At these rates the amount deducted using the constant deduction (UR) method would be more in the beginning years than the percentage deduction method. In this example the accumulated total amount deducted using the percentage method would not catch up to the constant deduction method until the year 2038. The applicant would be 84 years old.

It appears that this is the default method used by the DEU in Los Angeles or it is the only way the raters have been trained. There is no authority for using this method. It's a leftover from when there were no SAWW increases. I do not agree that this method should be used.

The DEU should just not calculate the starting deduction. The DEU shouldn't use the Example G calculator. The wording of the award can take care of what should be deducted. Using the Example G spreadsheet should be a red flag to the applicant's attorney.

Latest Life Tables

In this case the DEU calculated the present value of the life pension to be $74,798. Had the latest the 2004 life table been used the value would be $81,636.42. That's a difference of $6,838.42. The attorney fee would have been $1,025.76 higher.

Law Firm's Income

Besides the two cases discussed above I have looked at many other cases. All of them had something that I did not agree with. I have seen a case where mistakes were made by the DEU that made a difference in attorney's fee of $30,000.00. Considering that a law firm may have many cases where the rating is above 70% a law firm may be losing a significant amount of income in a year by not paying attention to present value calculations.

Some Thoughts

A General Proposition

As a general proposition I think the applicant should not be penalized when the attorney's fee is commuted. The commutation should be only between the insurance company and the attorney.

The non-increasing method of deduction penalizes the applicant in two ways.

First, a greater percentage is deducted in the beginning than would have been had there been no commutation of fee.

With no commutation of fee, 15% would be deducted from each payment. As the payment rate increases the deduction increases uniformly. The percentage of deduction remains the same. This is how the payment would be made had there been no commutation.

I agree with the calculation of the **projected** starting life pension payment but I do not agree that this will be the actual starting payment. The award should not specify a rate for the first payment.

The amount of the attorney fee on the life pension is based on the calculated present value of the life pension. The exact value of the deduction would depend on the actual SAWW increases over future years. When the award is issued it is not known what the life pension payment rate will be when the payments finally commence.

Second, using the constant deduction method involves the applicant in the process. It is as if the applicant had obtained a loan from the insurance company and now must make a fixed payment on the loan. If the SAWWs do not increase greater than 4.6% then the loan payback will cost the applicant more than a 15% attorney fee. The applicant has to bear the burden of varying SAWWs.

Estimate of Future SAWW Increases

The DEU originally estimated the SAWW increases[9] at 4.7% based on the average over the past 50 years. Their latest estimate has been reduced to 4.6%. I have not seen the numbers and don't know if negative numbers were excluded in computing the average or considered zero increase. The code section states that only increases are to be used. The applicant's life pension payment would never get reduced due to a negative SAWW. I don't think that was taken into consideration when determining the average but it may not make much difference.

[9] http://www.oui.doleta.gov/unemploy/content/data.asp

The estimated 4.6% can be subject to challenge[10]. I have not heard of a successful challenge or of an attorney having to prove up the number. Maybe the witness to prove that is a rater. Also, there might be a presumption that a rater is correct.

Do Not Use Labor Code Tables for Life Pension

The tables in the back of the Labor Code have not been updated to take into consideration increases in payments due to increases in SAWW. For a date of injury on or after 1/1/2003[11] life pension payments are entitled to be increased yearly by the percentage increase in SAWW.

The tables in the back of the Labor Code should not be used to calculate the present value of a life pension for cases where the applicant is entitled to SAWW increases. Attorneys should either use the DEU or Med-Legal for the calculation of present value.

Latest Life Tables

Even if the DEU did take into consideration SAWW increases from January 1, 2004, and continuing after the commencement of the life pension payments, the calculation of the present value is low. The calculations do not take into consideration the latest life tables.

The tables in the back of the labor code are based upon U.S. Life Tables for the years 1989-91[12]. The tables are more than 20 years old! The tables were supposed to be updated at least every 10 years. I wonder if they will ever be updated.

The only reason I do not agree with the present value calculations by the DEU is probably because more current tables are not used. When the user of the Med-Legal program choses to use the same tables as the DEU then Med-Legal's calculator come out with answers that are very close to the DEU answers. Med-Legal's calculations are more accurate.

When Should the Increases Start?

There should not be much quarrel with the increases starting on 1/1/2004 for life pension increases. That's what the code says in plain language. The Loya[13] case said to the contrary that the increases should only start when the payments actually commence, i.e. the first payment is made. The opinion based this on the language of the code that says, "… when entitled to receive a life pension…" The WCAB panel reasoned that if the applicant died before the first payment the applicant "would have never been actually entitled to receive any life pension". The logic doesn't make any sense. The fact is that the beneficiary was entitled to receive the life pension until he or she died whether the payments have commenced or not.

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[10] *Michael Lewis vs. Rex Moore Electrical Contractors* ADJ4118785
[11] LC 4659(c)
[12] It says that at the top of tables.
[13] *Ramon Loya v Arrowhead Brass Products* (2008) Cal. Wrk. Comp. P.D. Lexis 87 (a life pension case)

Had the payment commenced before the applicant died would the applicant's estate have to pay back the insurance company because the applicant was never entitled to the life pension?

If a person purchases a retirement life pension from an insurance company that person is to receive a life pension commencing after a date fixed for retirement. The beneficiary is **entitled** to life pension payments after issuance of the policy even though benefit payments do not commence until a future date. The insurance company cannot cancel the policy before commencement of payments because future payments have no value.

Using the Loya opinion's logic the attorney fee on the life pension cannot be commuted because the applicant is not entitled to anything; so there can be no fee on something of no value.

Yes, if the applicant dies before the first payment is due the applicant is no longer entitled to the life pension. But the real issue is how much is the first payment if the applicant lives to collect it? Is that first payment entitled to COLA increases from January 1, 2004? I think so. The applicant is now collecting the benefit.

Other cases have held that the SAWW increases should start on January 1 after the date of injury[14] or after the date of P&S[15].

COLA for Maximum Earnings and for Payment

COLA increases apply to the payments for both life pension and permanent total disability (PTD) but with different starting dates of injury. COLA increases apply to the **limits** of earnings for permanent total disability but not for life pension. Here is a table of the effective dates.

COLA on	Disability Benefit	DOI o/a	Increases Commence	Labor Code
	Permanent Partial (PD<70)	No COLA	NA	
Earning Limits	Life Pension (PD ≥ 70)	NA	NA	
	Permanent Total (PD 100%)	1/1/05	1/1/07	4453(a)(10)
Payments	Life Pension (PD ≥ 70)	1/1/03	1/1/04	4659(c)
	Permanent Total (PD 100%)			

It makes sense to have the rate of payment the same for all injured employees injured in the same year with the same income and rating. An injured employee who was temporarily totally disabled (TTD) for three years should be entitled to the same rate as he or she would if only on TTD for a short time.

For permanent total disability the payment rate is set as the same as temporary total disability.[16]

The Duncan case dealt with the issue as to when increases are to start except in Duncan the applicant was permanently totally disabled. The added complication with Duncan is that another code section

[14] *Allied Waste Industries, Inc. v. Rojas* C064914, ADJ608971 (not published)
[15] *Mari Monti-Alexander vs. Pleasant Valley State Prison* FRE 0223543
[16] Labor Code Section 4659(b)

increases the maximum allowable earnings based on increases in SAWW. The life pension does not have any statutory provision for setting the initial rate that allows for increases based on SAWW. For a date of injury on or after January 1, 2006, the maximum allowable earnings are not increased for the life pension.

With increasing the maximum allowable earnings for TTD and the rate of payment for PTD, it is argued that this is double dipping. Getting two increases based on SAWW increases. But the two increases are entirely different. One increases the maximum allowable earnings for setting the starting payment while the other increases the future payments for COLA.

A totally disabled beneficiary with earnings below the maximum allowable for TTD would only get the weekly payment rate increases.

The calculation of the rate of TTD and therefore, the rate of PTD is a one-time calculation based on the date of injury. That code section does not keep giving the injured employee increases for setting the initial TTD rate. The increases of the payment rate are on-going yearly increases.

The increases for the maximum TTD rate have in the past been increased by exact amounts and not based on SAWW. Only commencing in 2007 did the code tie the increases to the SAWW.

About Computing Present Value

It is not computed by multiplying the weekly rate by life expectancy in weeks. This is not even done if there were no SAWW increases or interest discounts.

The present value of future payments is computed as the sum of the probability of the beneficiary living to collect each payment multiplied by the payment amount. The probability changes for each payment based on the person's gender and age on the date the payment is made. The probability is based on actual data compiled by the Center for Disease Control and published as the U.S. Life Tables. This is the way actuaries compute present value.

An added complexity is that the payment rate changes each year. On January 1 of each year the payment is increased by the percentage increase in SAWW[17].

Payments are made for a two week period. It gets even more complicated if a payment covers a period in the prior year and a period in the next year. Payments that straddle the end and beginning of a year need to be taken into account to get an accurate value.

Also, each payment must be discounted for interest. This is the reverse of the loan situation. When you are loaned money you have to pay back more than you borrow. It depends on the loan interest rate. The present value is the amount loaned when the loan is taken out.

[17] State Average Weekly Wage

In the present value situation the payments are known but the “loan” amount must be calculated. There are standard financial formulas for this.

The discount interest rate used by the DEU is 3%. This is based on Regulation 10169.1. The regulation says to use 3% for a commutation. This interest rate has not been seriously challenged although attempts have been made. Just a heads up - using a higher interest rate will result in a lower present value.

What Now?

The DEU and the workers compensation administrative judges are getting closer to getting this stuff right but they still have a ways to go. Many attorneys don’t understand this stuff and should ask for help. This area is ripe for malpractice. What now---

Ask that the:

1. Award includes language that the life pension is paid pursuant to the Labor Code.
2. Award **not** specify an amount for the starting life pension payment.
3. Award includes language that SAWW increases commence on January 1, 2004, and continue for life.
4. Award specifies that the attorney fee on the life pension be commuted.
5. Award has language that the uniform increasing deduction method be used for the commuted attorney fee and that the deduction is uniform at the percentage of attorney fee.
6. DEU calculate the present value of the life pension using an up-to-date life table.
7. DEU not use Example G template to compute the deduction.
8. DEU calculations and the award are reviewed by someone who understands this stuff.