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A Reply to Professors Wolkoff & Hanushek on The Economics of Structured Judgments Under CPLR Article 50-B

ANTHONY H. RICCARDI†

INTRODUCTION

In their article,¹ Wolkoff & Hanushek discuss the economics of measuring damages in personal injury matters in relation to New York's structured judgment statute, CPLR 50-B.² The analysis is principally focused on the stipulated methodology for estimating a verdict's present value. Using different verdict damages scenarios, the authors discuss several aspects of potential bias against an accurate measure of present value. Although the authors' analysis of the various scenarios is extensive, they present an argument to dismiss an important statutory refinement to the present value computation. Ironically, heeding the authors' logic may result in the overstatement of a verdict's present value and the claimant's attorney's fee.

In discussing CPLR 5045, "Effect of death of judgment creditor,"³ the authors explain that a bias is introduced. Based on their logic, it is the authors' contention that the present value computation is actuarially distorted by the stipulation of a life-contingent limit to future damages annuity payments on certain elements of loss.⁴ Unless this stipulation is technically dismissed⁵ and annuity payments for all future damages are assumed to continue for fixed and guaranteed periods, perhaps beyond the life of the claimant, the authors predict a deflation in negotiated settlements.⁶

It is here that the authors' logic results in unsupported conclusions, in two respects. First, there is no reason for a technical

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1. Michael J. Wolkoff & Eric A. Hanushek, *The Economics of Structured Judgments Under CPLR Article 50-B*, 43 BUFF. L. REV. 563 (1995).

2. N.Y. C.P.L.R. 5041-5049 (McKinney 1992).

3. *Id.* 5045.

4. Wolkoff & Hanushek, *supra* note 1, at 563.

5. A dismissal of life-contingent mortality considerations in only the annuity present value computations is labeled as a technical dismissal.

6. Wolkoff & Hanushek, *supra* note 1, at 575.

dismissal of a life-contingent limit to certain annuity payments; in fact, there is clear statutory and actuarial support for such a limit.⁷ Second, any actuarial bias to the present value computation will have no impact on the claimant's recovery, or the negotiation of such, since only the claimant's attorney's fee is related to the estimate of present value. A review and analysis of the statute will obviate these points.

I. STATUTORIAL BASIS

In personal injury and wrongful death matters, CPLR 5041, "Basis for determining judgment to be entered," presents the essence of the structured judgment statute, a financial scheme for the post-verdict determination of the judgment distributions.⁸ The financial scheme features a set of lump sums and (future damages) annuity contract payments, serving as the complete basis for the determination of the claimant's recovery distributions. As a separate matter, the claimant's attorney's fee distribution is to be determined, based on a present value estimate of the set of undistributed lump sums and annuity contract payments.⁹ It is here, beyond the lump sums,¹⁰ in the estimation of the present value of the annuity contract payments, where the statute reveals some important, but subtle, complexities, which are apparently overlooked by the authors.

CPLR 5041(e), regarding the selection of an interest rate for the estimation of the present value of the payments from the annuity contract, provides: "The present value of such contract shall be determined in accordance with generally accepted actuarial practices by applying the discount rate in effect at the time of the award"¹¹ The section continues with a reference to the selection of the proper period of time to employ in the present value computation: "The period of time over which such periodic payments shall be made and the period of time used to calculate the present value of the annuity contract shall be the period of years determined by the trier of fact in arriving at the itemized verdict"¹²

Given no other direction, a limited reading of the statute indicates no additional present value considerations beyond the

7. See N.Y. C.P.L.R. 5045.

8. *Id.* 5041.

9. *Id.* 5041(c).

10. There is no question regarding the present value of any lump sums, they are in present value, if paid at once.

11. N.Y. C.P.L.R. 5041(e).

12. *Id.*

selection of a discount rate, to be applied to the annuity payments over the specified periods of time. However, to further clarify the period of time for determining the defendant's contractual obligation for the annuity payments (installments), in the event of the claimant's (judgment creditor's) death, sections 5045(a) and (b) state:

[T]he liability for payment of any installments for medical, dental or other costs of health care or non-economic loss not yet due at the death of the judgment creditor terminates upon the death of the judgment creditor. . . The portion of any periodic payment allocable to loss of future earnings shall not be reduced or terminated by reason of the death of the judgment creditor, but shall be paid to persons to whom the judgment creditor owed a duty of support immediately prior to his death to the extent that such duty of support exists under applicable law at the time of the death of the judgment creditor. Such payments to such persons shall continue for the remainder of the period as originally found by the jury or until such duty of support ceases to exist, whichever occurs first. In such cases, the court which rendered the original judgment may, upon petition of any party in interest, modify the judgment to award and apportion the future payments of such unpaid future damages in accordance with this subdivision which apportioned amounts shall be payable in the future as provided for in this article. In the event that the judgment creditor does not owe a duty of support to any person at the time of the death of the judgment creditor or such duty ceases to exist, the remaining payments shall be considered part of the estate of the judgment creditor.¹³

Therefore, the statute indicates that the defendant is obligated to pay the full verdict-stipulated period of future annuity payments for the earnings-related damages. In the present value computation, such payments are to be considered period-guaranteed, and, thus, not subject to an actuarial adjustment for mortality. However, the obligation for annuity payments, as derived from non-earnings damages, is limited to the stipulated period or the life of the claimant, whichever is less.¹⁴ The apparent logic being that an annuity payment stream for a distinct category of future damages, realized only during the claimant's life, should cease at the death of the claimant.¹⁵

13. *Id.*

14. *Id.* 5045.

15. In the authors' terms, these elements of future loss are non-compensation damages and, here, such losses are referred to as non-earnings damages. However, regardless of how these elements are labeled, the statutory nomenclature identifies them as a distinct category of future damages, realized only during the claimant's life.

Since the non-earnings annuity payments may end at the claimant's death, they are to be considered as life-contingent payments and are (absolutely) limited by the verdict periods. Thus, given certain information regarding the claimant, including gender and age, the present value of a first year's annuity payment is to be actuarially adjusted by the claimant's mortality in the first year, with a similar adjustment for the second year and the third year, and so on, resulting in an aggregate measure of the annuity's mortality-adjusted present value. Although actuaries and economists are routinely called upon to perform mortality adjustments of this nature, the authors (in a footnote) state that it is impossible to make such adjustments.¹⁶ It is this logic which leads the authors to a technical dismissal of such adjustments, resulting in an overestimation of the present value measure. A case illustration will serve to demonstrate the impact of this technical faux pas.

II. CASE ILLUSTRATION¹⁷

Consider the case of a 60 year old, female claimant,¹⁸ who receives a verdict damage award of \$1,857,620, as itemized in Table 1.0. As a first step, the total past damages, \$257,120, and a portion of the future damages, \$250,000, are earmarked as undistributed lump sum payments and, as such, included in Table 3.0. In algorithmic terms relating to the statute, Table 2.0 shows the treatment of the remaining future damages, providing a complete basis for the annuity payment and present value estimates in Table 2.1. A consideration of the claimant's mortality enters into the analysis in Table 2.1, where two, alternative annuity present value estimates are presented, unadjusted and adjusted. These estimates are directly carried into the Table 3.0 aggregate present values, resulting in an unadjusted total of \$1,545,964, compared to an adjusted total of \$1,444,968. The aggregate present value difference between the adjusted and unadjusted totals results in a potential distortion of \$101,196. The data in Tables 4.0 and 4.1 allow an itemized comparison of the

16. Wolkoff & Hanushek, *supra* note 1, at 575 n.32. There are standard actuarial reference sources routinely relied upon by economists, including the survivor tabulations in the U.S. Life Tables, published by the Social Security Administration. See FELICITE C. BELL, U.S. DEP'T OF HEALTH AND HUMAN SERVICES, LIFE TABLES FOR THE UNITED STATES SOCIAL SECURITY AREA, 1900-2080 (1992).

17. The methodology used here is consistent with *Rohring v. City of Niagara Falls*, 638 N.E.2d 62 (N.Y. 1994).

18. The claimant is assumed to have a standard mortality rating for a female at age 60.

adjusted and unadjusted judgment distributions in relation to the present value estimates.

Comparing the distributions in Tables 4.0 and 4.1, the sole impact of the present value mortality adjustment is shown in item B, the attorney's fee. The Table 4.0, lump sum, attorney fee distribution is \$515,321, as compared to \$481,589 in Table 4.1, a difference—an overestimate—of \$33,732. However, the claimant's net recovery, in terms of her lump sum (item A) and annuity contract distributions (item D), is unaffected. This outcome should not be a surprise, since only the attorney's fee is based on the Table 3.0 total present value estimates. In effect, the claimant has nothing to lose, and is economically indifferent, by allowing a settlement negotiation to focus on the Table 4.1 adjusted distributions; a direct contradiction to the authors' contention that lower present value estimates will unilaterally result in deflated negotiated settlements.¹⁹

To extend this analysis one step further and fully illustrate the impact of the authors' logic, a final point should be made in regard to an additional consequence of a complete dismissal of life-contingent annuity payments. Going beyond the technical dismissal, a complete dismissal would replace the life-contingent annuity payments with their period-guaranteed cousins and, thus, affect the defendant's (statutory) obligation to purchase an annuity contract. All other things being equal, the purchase of an annuity contract which stipulates only period-guaranteed payments will be more expensive than would the purchase of a contract which includes life-contingent payments. Referring to the pertinent annuity contract data shown in item D of Tables 4.0 and 4.1, the contract premium²⁰ for the annuities, as shown, is \$545,680 and, alternatively, \$583,972 if all the annuity payments are period-guaranteed. The difference in the annuity contract premiums, \$38,112, is the extra expense to guarantee that the annuity payments to either the claimant or her survivors (including her estate) will continue for the full, future damages periods. However, since the defendant is not obligated to offer an annuity contract with such blanket guarantees, this extra expense is only illustrative and, as a practical matter, irrelevant in contemplating a settlement offer.

19. See Wolkoff & Hanushek, *supra* note 1, at 565. It is assumed that the primary focus of any settlement negotiation is the claimant's recovery.

20. The annuity contract premiums are believed to be representative of the competitive quotes available in mid-August 1996. Interview with Christopher E. Larned, President of Settlement Services, Inc., in New York, NY.

CONCLUSION

The work of the authors has helped to highlight many of the complexities of New York's structured judgment statute. In that spirit, this comment highlights an important technical adjustment to the authors' present value analyses: the consideration of life-contingent annuity payments for certain elements of future damages. The sole impact of this refinement is upon the present value estimate, as the basis for the claimant attorney's contingency fee. Although the full impact on the authors' conclusions is unclear, their analyses of various verdict present values are generally affected (downward) by this refinement.²¹ The most significant impact is on verdicts with large amounts of non-earnings-related future damages, paid to an elderly claimant, over a long period of time. Verdicts with future damages which are only earnings-related would not be affected.

21. Depending on the assumptions the Court includes in its verdict, the negative impact of a present value mortality adjustment may be mitigated. That is, trial testimony may present the future damages in a form that is not limited by the claimant's life expectancy, effectively projecting the future damages to the actuarial limit of life, normally considered to be age 100. In the illustration presented here, the verdict periods of the future damages for medical expenses would be increased to 40 years from the claimant's 23-year life expectancy period. By virtue of the added years, the total, verdict future damages would be substantially greater and, therefore, mitigate the impact of the mortality adjustments.

TABLE 1.0
ITEMIZED VERDICT DAMAGES

<u>PAST DAMAGES:</u>			
<u>ELEMENT OF DAMAGES</u>		<u>VERDICT AMOUNT</u>	
Lost Earnings		\$ 33,120	Attorney's Fee Ratio <u>1/3</u>
Medical Expenses		64,000	Claimant's Recovery Ratio <u>2/3</u>
Pain and Suffering		160,000	
Total Past Damages		\$257,120	Litigation Expenses \$ <u>9,120</u>
<u>FUTURE DAMAGES:</u>			
<u>ELEMENT OF DAMAGES</u>		<u>VERDICT AMOUNT</u>	<u>PERIOD (YRS)</u>
Lost Earnings		\$ 150,500	<u>5.0</u>
Medical Expenses		950,000	<u>23.0</u>
Pain and Suffering		500,000	<u>23.0</u>
Total Future Damages		\$1,600,500	
TOTAL VERDICT DAMAGES		\$1,857,620	

TABLE 2.0
 FUTURE DAMAGES
 PROPORTIONATE LUMP SUMS AND REMAINDER AMOUNTS AND PERIODS

<u>ELEMENT OF FUTURE DAMAGES (YRS)</u>	<u>PRO. LUMP SUM²²</u>	<u>REMAINDER AMOUNT²³</u>	<u>PERIOD²⁴</u>
Lost Earnings	\$ 23,500 (9.40%)	\$127,000	5.0
Medical Expenses	148,400 (59.36%)	801,600	23.0
Pain and Suffering	78,100 (31.24%)	421,900	10.0
TOTAL	\$250,000 (100.00%)		

²² The proportionate lump sums are the Table 1.0 future damages, verdict amounts expressed as a percentage of total future damages and multiplied by \$250,000.

²³ The remainder amounts are the difference between the Table 1.0 future damages and the proportionate lump sums.

²⁴ Any pain and suffering remainder amount is limited to an annuity payment period of ten years and all other periods are as shown in Table 1.0.

TABLE 2.1
 FUTURE DAMAGES
 UNDISTRIBUTED ANNUITY
 ANNUAL PAYMENTS, PERIODS AND PRESENT VALUES

ELEMENT OF DAMAGES	UNDISTRIBUTED ANNUITY		PRESENT VALUE ²⁵	
	ANNUAL PAYMENT ²⁶	PERIOD (YRS)	UNADJUSTED	ADJUSTED
Lost Earnings	(P*1) \$25,400.00	5.0	\$118,781.46	\$118,781.46
Medical Expenses	(P*2) 34,852.17	23.0	\$565,454.51	\$481,783.06
Pain and Suffering	(P*3) 42,190.00	10.0	\$363,728.11	\$346,203.43
		TOTALS	\$1,047,964.08	\$946,767.95

²⁵ The present value computations are shown in Appendix 1.

²⁶ The undistributed annuity annual payments are first year figures, equal to the Table 2.0, remainder amounts divided by the respective periods.

TABLE 3.0
PRESENT VALUE BY DAMAGE COMPONENT

<u>DAMAGE COMPONENT</u>	<u>AMOUNT</u>	<u>PRESENT VALUE</u>	
		<u>UNADJUSTED</u>	<u>ADJUSTED</u>
Past Damages ²⁷	\$257,120		
Future Damages - Lump Sum ²⁸	250,000	\$498,000	\$ 498,000
Litigation Expenses ²⁹	(9,120)	1,047,964	\$ 946,768
Net, Undistributed Lump Sums ³⁰			
Future Damages - Annuities ³¹		\$1,545,964	\$1,444,768
TOTAL³²			

²⁷ See Table 1.0, past damages, total.

²⁸ See Table 2.0, future damages, lump sum, total.

²⁹ See Table 1.0, litigation expenses.

³⁰ The figure shown here is the complete basis for the computation of the claimant's lump sum distribution.

³¹ See Table 2.1, annuity, present value, total.

³² The total shown here is the net, present value of the Table 1.0, total verdict damages and the complete basis for the computation of the attorney's fee distribution.

TABLE 4.0
STRUCTURED JUDGMENT DISTRIBUTIONS
UNADJUSTED BASIS

<u>ITEM</u>	<u>DISTRIBUTION TYPE</u>	<u>DISTRIBUTION AMOUNT</u>	<u>DISTRIBUTE</u>
A	Lump Sum Payment ³³	\$332,000	Claimant
B	Lump Sum Payment ³⁴	\$515,321	Attorney @ Fee
C	Lump Sum Payment ³⁵	\$ 9,120	Attorney @ Lit. Exp.
D	Annuity Contract ³⁶		
	•1	\$1,411.11	Claimant
	•2	Mode G @ 5.0 years	Claimant
	•3	Mode L @ 23.0 years	Claimant
		\$2,343.89	Mode L @ 10.0 years

MODE

G - A continuous series of monthly payments, increased at four percent on each anniversary date for a Table 2.1, guaranteed period.
L - A continuous series of monthly payments, increased at four percent on each anniversary date for a Table 2.1, life contingent period.

33 The claimant's lump sum distribution is the Table 3.0, unadjusted, net lump sums, present value multiplied by the claimant's recovery ratio.
34 The attorney's fee distribution is the Table 3.0, unadjusted, total, present value multiplied by the attorney's fee ratio.
35 See Table 1.0, litigation expenses.
36 The Table 2.1, undistributed annuity annual payments multiplied by the claimant's recovery ratio yields the claimant's first year, annuity contract payments. Dividing the first year payments by twelve yields the claimant's monthly annuity payments, shown here.

TABLE 4.1
STRUCTURED JUDGMENT DISTRIBUTIONS
ADJUSTED BASIS

<u>ITEM</u>	<u>DISTRIBUTION TYPE</u>	<u>DISTRIBUTION AMOUNT</u>	<u>DISTRIBUTE</u>
A	Lump Sum Payment ³⁷	\$332,000 Paid at once	Claimant
B	Lump Sum Payment ³⁸	\$481,589 Paid at once	Attorney @ Fee
C	Lump Sum Payment ³⁹	\$ 9,120 Paid at once	Attorney @ Lit. Exp.
D	Annuity Contract ⁴⁰		
	•1	\$1,411.11 Mode G @ 5.0 years	Claimant
	•2	\$1,936.23 Mode L @ 23.0 years	Claimant
	•3	\$2,343.89 Mode L @ 10.0 years	Claimant

MODE

G - A continuous series of monthly payments, increased at four percent on each anniversary date for a Table 2.1, guaranteed period.
L - A continuous series of monthly payments, increased at four percent on each anniversary date for a Table 2.1, life contingent period.

³⁷ The claimant's lump sum distribution is the Table 3.0, adjusted, net lump sums, present value multiplied by the claimant's recovery ratio.

³⁸ The attorney's fee distribution is the Table 3.0, adjusted, total, present value multiplied by the attorney's fee ratio.

³⁹ See Table 1.0, litigation expenses.

⁴⁰ The Table 2.1, undistributed annuity annual payments multiplied by the claimant's recovery ratio yields the claimant's first year, annuity contract payments. Dividing the first year payments by twelve yields the claimant's monthly annuity payments, shown here.

APPENDIX 1
Undistributed Annuity
Present Value Computations
i = 7.6 %

Element of Damage: Pain and Suffering.

PERIOD (YEARS)	ANNUAL PAYMENT	DISCOUNT FACTOR	UNADJUSTED PRESENT VALUE	AGE	SURVIVORS	SURVIVAL RATE	MORTALITY ADJUSTED PRES. VAL.
1	\$42,190.00	1.000000	\$42,190.00	60	89,317	1.000000	\$42,190.00
2	\$43,877.60	0.929368	\$40,778.44	61	88,479	0.990618	\$40,395.84
3	\$45,632.70	0.863725	\$39,414.10	62	87,571	0.980452	\$38,643.62
4	\$47,458.01	0.802718	\$38,095.42	63	86,594	0.969513	\$36,934.01
5	\$49,356.33	0.746021	\$36,820.85	64	85,548	0.957802	\$35,267.08
6	\$51,330.59	0.693328	\$35,588.92	65	84,434	0.945330	\$33,643.26
7	\$53,383.81	0.644357	\$34,398.22	66	83,249	0.932062	\$32,061.28
8	\$55,519.16	0.598845	\$33,247.35	67	81,986	0.917922	\$30,518.46
9	\$57,739.93	0.556547	\$32,134.98	68	80,637	0.902818	\$29,012.04
10	\$60,049.53	0.517237	\$31,059.83	69	79,189	0.886606	\$27,537.84
TOTALS	\$506,537.66		\$363,728.11				\$346,203.43

APPENDIX 1
Undistributed Annuity
Present Value Computations
 $i = 7.6\%$

Element of Damage: Medical Expenses.

PERIOD (YEARS)	ANNUAL PAYMENT	DISCOUNT FACTOR	UNADJUSTED PRESENT VALUE	AGE	SURVIVORS	SURVIVAL RATE	MORTALITY ADJUSTED PRES. VAL.
1	\$34,852.17	1.000000	\$34,852.17	60	89,317	1.000000	\$34,852.17
2	\$36,246.26	0.929368	\$33,686.11	61	88,479	0.990618	\$33,370.06
3	\$37,696.11	0.863725	\$32,559.07	62	87,571	0.980452	\$31,922.59
4	\$39,203.95	0.802718	\$31,469.73	63	86,594	0.969513	\$30,510.32
5	\$40,772.11	0.746021	\$30,416.84	64	85,548	0.957802	\$29,133.31
6	\$42,402.99	0.693328	\$29,399.18	65	84,434	0.945330	\$27,791.91
7	\$44,099.11	0.644357	\$28,415.56	66	83,249	0.932062	\$26,485.07
8	\$45,863.08	0.598845	\$27,464.85	67	81,986	0.917922	\$25,210.58
9	\$47,697.60	0.556547	\$26,545.96	68	80,637	0.902818	\$23,966.17
10	\$49,605.51	0.517237	\$25,657.80	69	79,189	0.886606	\$22,748.36
11	\$51,589.73	0.480704	\$24,799.36	70	77,633	0.869185	\$21,555.23
12	\$53,653.31	0.446750	\$23,969.64	71	75,963	0.850488	\$20,385.88
13	\$55,799.45	0.415196	\$23,167.69	72	74,175	0.830469	\$19,240.04
14	\$58,031.42	0.385870	\$22,392.56	73	72,268	0.809118	\$18,118.22

APPENDIX 1
Undistributed Annuity
Present Value Computations
i = 7.6 %

Element of Damage: Medical Expenses

PERIOD (YEARS)	ANNUAL PAYMENT	DISCOUNT FACTOR	UNADJUSTED PRESENT VALUE	AGE	SURVIVORS	SURVIVAL RATE	MORTALITY ADJUSTED PRES. VAL.
15	\$60,352.68	0.358615	\$21,643.36	74	70,240	0.7866412	\$17,020.61
16	\$62,766.79	0.333285	\$20,919.24	75	68,088	0.762318	\$15,947.12
17	\$65,277.46	0.309745	\$20,219.34	76	65,810	0.736814	\$14,897.89
18	\$67,888.56	0.287867	\$19,542.85	77	63,400	0.709831	\$13,872.13
19	\$70,604.10	0.267534	\$18,889.00	78	60,852	0.681304	\$12,869.15
20	\$73,428.27	0.248638	\$18,257.03	79	58,160	0.651164	\$11,888.32
21	\$76,365.40	0.231076	\$17,646.20	80	55,320	0.619367	\$10,929.47
22	\$79,420.01	0.214755	\$17,055.81	81	52,326	0.585846	\$9,992.07
23	\$82,596.81	0.199586	\$16,485.17	82	49,176	0.550578	\$9,076.37
TOTALS	\$1,276,212.88		\$565,454.51				\$481,783.06

APPENDIX 1
Undistributed Annuity
Present Value Computations
i = 7.6 %

Element of Damage: Lost Earnings

PERIOD (YEARS)	ANNUAL PAYMENT ⁴¹	DISCOUNT FACTOR ⁴²	UNADJUSTED PRESENT VALUE ⁴³	AGE	SURVIVORS ⁴⁴	SURVIVAL RATE ⁴⁵	MORTALITY ADJUSTED PRES. VAL. ⁴⁶
1	\$25,400.00	1.000000	\$25,400.00	60	89,317	1.000000	\$25,400.00
2	\$26,416.00	0.929368	\$24,550.19	61	88,479	1.000000	\$24,550.19
3	\$27,472.64	0.863725	\$23,728.80	62	87,571	1.000000	\$23,728.80
4	\$28,571.55	0.802718	\$22,934.90	63	86,594	1.000000	\$22,934.90
5	\$29,714.41	0.746021	\$22,167.56	64	85,548	1.000000	\$22,167.56
TOTALS	\$137,574.59		\$118,781.46				\$118,781.46

41. For the specified element of damages, the first year undistributed annuity payment is as shown in table 2.1 and increased by four percent, annually.

42. The discount factors are related to the interest rate, as presented in the *New York Pattern Jury Instructions - Civil*, Volume 1, Second Edition, issued 1993.

43. The unadjusted present values are the multiplication products of the annual payments and discount factors.

44. Given the claimant's age and gender, the survivors are the number of individuals alive, from a birth base of 100,000, as found in the *U.S. Life Tables and the New York Pattern Jury Instructions - Civil*, Volume 1, Second Edition, issued 1993.

45. For an element of non-earnings related damages, the survival rate is equal to a given year's survivors divided by the first year's survivors; for all other elements the survival rate is one for the entire annuity period.

46. The mortality adjusted present values are the multiplication products of the unadjusted present values and survival rates.