Wage loss vs earning capacity: Defining the differences

The difference can be confusing, but it is essential to explain this basic concept – wage loss vs earning capacity – to the mediator or jury

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"Earning capacity" is a term often used by the courts to describe what is compensable to a person with a disability. Different states use different language to describe future loss. Some states refer to "the power to labor and earn money," while other states will refer to "reduction of potential to work and earn money." In some instances, the focus is on an individual's "ability" to work and earn. The intent of the law is that if the tort feasor is liable for the injury, he or she must pay damages to a person with a disability that will compensate for potential future losses. (Gamboa, Anthony M Jr., et al. "A Vocational Economic Rationale." Estimating Earning Capacity: A Journal of Debate and Discussion 2, no. 2 (2009): 97-123.)

An important distinction must be made between the terms "wage loss" and "loss of earning capacity." Wage loss is a retrospective, while loss of earning capacity is prospective. For example, imagine a plaintiff earning $50,000 per year who is injured in 2007 and out of work for one year. The plaintiff has a claim of $50,000 for a past loss of wages. However, if the plaintiff has a permanent impairment that limits his or her ability to work, there is probably a loss of future earning capacity.

It should be noted that it is not possible to forecast the actual future wages of an individual either with or without a disability. Defense attorneys often attempt to capitalize on the lack of distinction between the terms "wage loss" and "loss of future earning capacity" by attempting to conflate the two terms in the minds of the jury, and then arguing that because no one can accurately forecast an individual's future wages it is too speculative to award damages. However, there is a sound methodological basis for calculating an individual's earning capacity using principles from economics.

> This is the first in a series of five articles on the determination of damages from loss of future earning capacity in cases of partial disability.
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> The focus of the first article is on *earning capacity*; the second will focus on the disparity in *earnings* and *worklife expectancy* existing for persons who meet the definition of disability; the third revisits and updates information from the article "What the Infant or Child Could Have Been" (Gamboa, Anthony Jr., Ph.D. *Trial*. September 1986.); the fourth focuses on defining earning capacity loss for a partially disabled worker who has *returned to work* earning more money than was earned prior to the injury in question; and the final article focuses on present value of future earnings.
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Human capital defined

While the concept of earning capacity has not been clearly defined by the courts, economists have defined a term synonymous with earning capacity. They call it "human capital." "Capital" is anything that produces wealth.

Human capital is defined as the acquisition of knowledge, skill, and understanding as a result of education, training, and experience that allows an individual to sell his or her services in the marketplace in exchange for money.

While economists do an excellent job of defining human capital, they typically ignore the precursors to human capital: **general learning ability** and **physical ability**. (Gamboa, *ibid.)* If an individual's level of cognition is reduced his physical capabilities are diminished, by definition the individual's level of human capital has decreased. For comparison, imagine a $1 million investment that produces a five-percent return, or $50,000 per year. If the $1 million is cut in half, the return on investment reduced by $25,000 per year.

Similarly, when human beings experience a diminution of their human capital, it is likely and probable that future cash flows will be decreased. The theory makes intuitive sense, and data reported by the U.S. Census Bureau specific to earnings and worklife expectancy support the theory.

What is compensable

It is imperative that jurors understand what is compensable so that they can award adequate damages. It is incumbent on the plaintiff's attorney to help

the jury to understand that loss of earning capacity is what drives the significant economic effect that disability has on an individual with a disability.

Thus, it is essential to differentiate for the jury the difference between wage loss and earning capacity loss. Absent a clear differentiation between wage loss and earning capacity loss, jurors are likely to ask, "How can anyone possibly predict the future lost wages that will incur for the plaintiff?" Before deliberations begin at least one juror must understand the distinction and point out to others that loss of earning capacity and not wage loss is the issue.

If loss of earning capacity or diminution of human capital were not the legal issue, it would be impossible for anyone who has never been employed to recover for the future earnings loss that would likely occur. Similarly, workers who return to work with a disability could not recover for their probable future reduced earnings, which result from decreased levels of productivity in combination with a reduced worklife expectancy.

Earning capacity diminution through the lifespan

Employment levels form the building blocks of a worklife expectancy. The reduction in worklife expectancy existing for workers with a disability is largely a function of the fact that they tend to exit the workforce earlier than their non-disabled counterparts. In addition, when unemployed, persons with a disability take longer to find employment than persons without a disability. In an expanding economy, workers with a disability are the last hired, and in a contracting economy they are the first to be laid off. (Yelin, Edward. "The Labor Market and Persons with and without Disabilities: Analysis of the 1993 through 1995 Current Population Surveys." Conference on Employment and Return to Work for People with Disabilities. Office of Disability, Social Security Administration and National Institute on Disability and Rehabilitation Research, 1996.) (Gibson, David S. Daubert, Disability, and Worklife Expectancy. Louisville, KY: Vocational Econometrics, 2001.)

Moreover, physical impairments and cognitive impairments rarely improve with the passing of time; in fact, those with physical or cognitive impairments tend to deteriorate. In comparing employment data for workers with a disability and workers without a disability, the disparity is significantly greater during the 50s than it is during the 20s. The aging process reduces the probability of employment during the 40s and 50s. The interaction effect between aging and disability produces a more precipitous decline for individuals with a disability. These factors account for a significant portion of the diminution of earning capacity as a result of disability.

When the focus is on earning capacity or human capital, it is understandable how a jury can award money to an employed person with a permanent disability. This is true even when the individual is earning more subsequent to the injury than prior to the injury.

No presumption of permanence

Factors existing at the time of trial such as the plaintiff's current earnings or employment status are not necessarily an indicator of what will occur over a lifespan. For example, imagine a plaintiff who is a 35-year-old unemployed male with a permanent disability associated with a back injury and subsequent back fusion. If he is capable of performing sedentary or light work, it is not reasonable to presume that he will remain unemployed for the rest of his life. His employment status at the time of trial is transitory. Although such a plaintiff likely retains the ability to work and earn money, it is probable that he has suffered a reduction in his future earning capacity.

Jurors at the time of trial are asked not to look at the moment for guidance in determining lifetime earning capacity capability. Rather, they should be provided with information specific to what typically occurs for individuals most like the plaintiff. Factors that need to be considered include average earnings and worklife expectancy levels for persons with and without a disability specific to age, gender, level of educational attainment, and disability status (severe or non-severe).

Conclusion

The foundation for future economic loss is built from the premise of assessing future earning capacity. Without a strong understanding of the concept of earning capacity, jurors are denied the opportunity to help right a wrong.

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