January 1986

Hafer v. Anaconda: "Lost Earning Capacity" Refines "Permanent Partial Disability"

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HAFER V. ANACONDA: "LOST EARNING CAPACITY" REFINES "PERMANENT PARTIAL DISABILITY"

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I. INTRODUCTION

Hafer v. Anaconda Aluminum Co. signals a new era in workers' compensation law. In a well-reasoned decision, the Montana Supreme Court defined a test for injured workers seeking permanent partial disability under the theory of lost earning capacity. Protecting the worker against economic loss, the decision in Hafer elevates earning capacity over medical impairment as the prime determinant of permanent partial disability. The decision clarifies the factors which once clouded the disability issue. Hafer accurately evaluates the worker's position in the open labor market.

II. BACKGROUND

On June 17, 1977, Kerry K. Hafer fractured his elbow in an industrial accident in the course of his employment with the Anaconda Aluminum Company (Anaconda). At that time, Hafer's base pay was approximately $7.00 per hour as an ironworker. In treating the injury, a surgeon implanted a silastic prosthesis in Hafer's elbow. The manufacturer of the device disclaimed its effectiveness for workers who engaged in strenuous physical activity. Hafer's surgeon evaluated Hafer as suffering a permanent partial impairment of 20% of his left upper arm at the shoulder. Hafer could neither work with his former efficiency, nor completely straighten and rotate his arm, yet Anaconda retained Hafer as an ironworker and increased his base pay to approximately $10.00 per hour.


2. Id. at ___, 684 P.2d at 1118.
4. Id.
5. Id. at 111, 643 P.2d at 1195.
6. Id. at 106, 643 P.2d at 1193.
7. Mont. Code Ann. § 39-71-703(1) (1983) states, "Weekly compensation benefits for injury producing partial disability shall be 66.7% of the actual diminution in the worker's earning capacity measured in dollars, subject to a maximum weekly compensation of one-half the state's average wage."
partial disability. Two years after the accident, Hafer petitioned for a hearing in the Workers' Compensation Court. Hafer had been working for Anaconda for three years by the time of the hearing. He was 24 years old and did not have a high school degree, although he had earned an associate of applied science degree in welding. Hafer's previous job experience consisted primarily of physical labor.  8

At the hearing, an employee relations manager for Anaconda testified that if Hafer could no longer perform the duties of an ironworker, then Anaconda would attempt to employ him in a clerical position. Anaconda entry level clerical workers only earned about $6.00 per hour. A placement expert from the Montana State Job Service also testified regarding Hafer's employment. The expert considered Hafer's job experience and inability to perform strenuous physical labor. He testified that Hafer lacked the capacity to perform 90% of the available jobs in Flathead County and could expect to earn less than $700.00 per month.  9

The workers' compensation hearing examiner found that Hafer suffered an impaired ability to compete in the open labor market. Although Hafer's actual earnings remained undiminished, the injury had diminished his earning capacity by 40%. Therefore, if Hafer had to find another job, it would probably pay only 60% of what he could have earned before the injury. The hearing examiner calculated a partial disability factor of 30%, which is the median of the physical impairment rating of 20% and the earning capacity diminution of 40%.  10

The Workers' Compensation Court, Judge William Hunt presiding, adopted the hearing examiner's findings and conclusions.  11 Both Hafer and Anaconda agreed that Hafer suffered a "whole arm injury," meriting benefits for the maximum of 280 weeks. The court entered a judgment on behalf of Hafer and found he was entitled to a partial disability award of $81.00 per week, multiplied by 30% of 280 weeks.  12 Hafer appealed, on the grounds that the factor of 30% should not limit his recovery.  13

The Montana Supreme Court vacated and remanded the case to the Workers' Compensation Court of Judge Timothy Reardon. Judge Reardon ruled that the 40% wage contour between an iron-

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9. Id.
10. Id. at 107, 643 P.2d at 1193.
11. Id. at 108, 643 P.2d at 1194.
12. Id.
13. Hafer, --- Mont. at ---, 684 P.2d at 1115.
worker and a clerk might not remain constant and found that Hafer’s 40% diminished earning capacity was not synonymous with a 40% partial disability.\textsuperscript{14} He stated that diminished earning capacity is only one element to consider in determining the extent of Hafer’s disability. Like Judge Hunt before him, Judge Reardon concluded that Hafer was only 30% permanently partially disabled as a result of his industrial accident.\textsuperscript{15} Hafer appealed this decision to the Montana Supreme Court.\textsuperscript{16}

On appeal, Hafer contended that Judge Reardon’s decision was inconsistent because it found a 40% earnings capacity impairment, yet used a 30% disability factor to compute Hafer’s benefits. Hafer asserted that factors other than earning capacity impairment apply only when the court cannot make an independent impairment determination. Hafer concluded that his award should be based solely on reduced earning capacity and not on physical impairment percentage.\textsuperscript{17}

\section*{III. HOLDINGS}

In a unanimous decision, the Montana Supreme Court vacated and remanded the lower court’s decision.\textsuperscript{18} The court stated, “[T]he purpose of workers’ compensation is to protect the worker against economic loss. Therefore any disability rating which does not achieve this goal must be set aside and a figure representing potential economic loss must be substituted.”\textsuperscript{19} The court also held, “[F]actors other than earning capacity impairment are only relevant when the Workers’ Compensation Court is unable to make independent determination of the degree to which the claimant’s income earning ability has been impaired.”\textsuperscript{20}

Thus, the \textit{Hafer} court outlined the proper test to determine the degree of permanent partial disability: If the Workers’ Compensation Court found that an injury reduced the claimant’s earning capacity by 40%, then 40% should be the figure used in computing the claimant’s permanent partial disability.\textsuperscript{21}

\begin{itemize}
\item \textsuperscript{14} \textit{Id.} at ___, 684 P.2d at 1118.
\item \textsuperscript{15} \textit{Id.}
\item \textsuperscript{16} \textit{Id.} at ___, 684 P.2d at 1114.
\item \textsuperscript{17} \textit{Id.} at ___, 684 P.2d at 1115.
\item \textsuperscript{18} \textit{Id.} at ___, 684 P.2d at 1118.
\item \textsuperscript{19} \textit{Id.} at ___, 684 P.2d at 1116.
\item \textsuperscript{20} \textit{Id.} at ___, 684 P.2d at 1118.
\item \textsuperscript{21} \textit{Id.}
\end{itemize}
IV. Analysis

A. Developments Leading to Hafer

The Hafer decision announced the final step in an eight year trend away from dependence on medical impairment factors. A claimant now may seek permanent partial disability benefits under Montana Code Annotated section 39-71-703 for actual loss of earning capacity.22 Prior to Hafer, the court considered many factors in determining loss of earning capacity. Chief among these was the medical impairment factor, which often dominated the final disability rating.23 After Hafer, a claimant pursuing benefits for loss of earning capacity will no longer have the medical impairment factor clouding his claim. The decision requires that permanent partial benefits be determined according to earning capacity impairment, when that evidence is available.24

In 1977, a chain of cases began eroding the importance of medical impairment. In Ramsey v. Duncan and Baier,26 the court held that the evaluation of permanent disability goes beyond medical expertise. Many factors besides medical impairment ratings may be properly considered in the determination of a claimant’s disability. "Medical impairment ratings do not conclusively establish limits on compensation awards in all cases."26 The court first focused on earning capacity rather than strict medical impairment in Fermo v. Superliner Products.27 The Workers’ Compensation Court had granted Fermo an award for an extremity injury. The supreme court affirmed the award even though Fermo had returned to the same job after the injury and was earning more money. The court indicated that Fermo suffered a loss of performance capacity and a "loss of ability to compete and earn in the open labor market."28 In Walker v. H.F. Johnson, Inc.,29 the court lauded the earning capacity factor as a complement to the concept of permanent partial disability. The permanent partial disability concept presupposes an ability to return to the labor market in some capacity, albeit with limitations. The court found if a worker earns a greater salary in future years due to increases in the salary base, then the increases should not work against the worker in de-

24. Hafer, ___ Mont. at ___, 684 P.2d at 1118.
26. Id. at 440, 571 P.2d at 385.
27. 175 Mont. 245, 574 P.2d 251 (1978).
28. Id. at 257, 574 P.2d at 253.
terming the worker's true loss of earning capacity.\textsuperscript{30}

The court abandoned the method of basing computation of benefits primarily on medical impairment, and placed greater emphasis on earning capacity in \textit{Walter v. Public Auction Yards}.\textsuperscript{31} The court in \textit{Walter} held that many factors besides medical impairment ratings must be considered in determining disability. The court stated, "Disability is a hybrid quasi-legal and medical concept, in which are co-mingled in endless combinations, the inability to perform and the inability to obtain suitable work."\textsuperscript{32} The drift away from the medical impairment basis continued in the case of \textit{Holton v. F.H. Stolze Land & Lumber Co.}\textsuperscript{33} The court held the determination of disability did not depend merely on medical evidence of impairment, but also on the claimant's age, work experience, actual wage loss, and loss of future earning capacity.\textsuperscript{34} Thus, the conceptual chain that began in 1977 set the stage for \textit{Hafer}.

\textbf{B. The Court's Reasoning}

The \textit{Hafer} court cogently separated the key factors for determining permanent partial disability. It discarded the old medical impairment theory and adopted a more accurate assessment of the claimant's true economic position. "Factors other than earning capacity impairment are only relevant to the determination of permanent partial disability when the Worker's Compensation Court is unable to make an independent determination of the degree to which the claimant's earning capacity has been impaired."\textsuperscript{35} The supreme court found claimant Hafer's arguments persuasive and incorporated them into its reasoning.\textsuperscript{36} It stated, "[The] degree of disability is calculated under most acts by comparing actual earnings before the injury with earning capacity after the injury."\textsuperscript{37}

Thus, the decision subtly shifted from comparing old wages with new wages, to comparing old wages with new \textit{earning capacity}. At first, this appeared to be an "apples and oranges" approach. The court, however, went on to explain that earning capacity is

\begin{itemize}
\item \textsuperscript{30} \textit{Id.} at 412, 591 P.2d at 185.
\item \textsuperscript{31} 181 Mont. 109, 592 P.2d 497 (1979).
\item \textsuperscript{32} \textit{Id.} at 116, 592 P.2d at 501 (quoting 3 A. Larson, \textit{Workmen's Compensation Law} § 79.53 (1976)).
\item \textsuperscript{33} 195 Mont. 263, 637 P.2d 10 (1981).
\item \textsuperscript{34} \textit{Id.} at 266, 637 P.2d at 12.
\item \textsuperscript{35} \textit{Hafer}, ___ Mont. at ___, 684 P.2d at 1117.
\item \textsuperscript{36} \textit{Id.}
\item \textsuperscript{37} \textit{Id.} at ___, 684 P.2d at 1116 (citing Osborne v. Johnson, 432 S.W.2d 800, 803 (Ky. 1968) (quoting 2 A. Larson, \textit{Workmen's Compensation Law} § 57.10 (1968))).
\end{itemize}
actually a new wage within a market context. "The ultimate objective of the disability test is . . . to determine the wage that would have been paid in the open market under normal employment conditions to the [injured] claimant." Under this concept, medical percentages are not determinative. The real question becomes: What amount of wage control has the injured worker lost in the local labor market? To support its reasoning that potential economic loss, rather than medical impairment, should be the basis of a compensation award, the court quoted the Kentucky case of Osborne v. Johnson: "[T]he proper balancing of the medical and wage loss factors is . . . the essence of the disability problem in workers' compensation." The court in Hafer found that the degree of disability should be the ratio of pre-injury wages compared to the workers' post-injury earning capacity.

The Hafer court found factors other than earning capacity to be irrelevant, and went one step further when it accepted claimant Hafer's reasoning that "permanent partial disability," as defined by the Montana Code, means the extent to which a worker's earning capacity is reduced. The court thereby made earning capacity the exclusive determinant of permanent partial disability.

The decision carefully noted the reasoning of Workers' Compensation Court Judge Reardon. Judge Reardon had relied on the factors outlined in Flake v. Aetna Life & Casualty Co., which stated, "In determining disability, the Court should consider the claimant's age, education, work experience, actual wage loss, and loss of future earning capacity." Based on the variety and flexibility of these factors, Judge Reardon found that the 40% constant wage contour between an Anaconda ironworker and an Anaconda clerk was too speculative. He therefore concluded that Hafer was only 30% disabled.

38. Id.
39. Hafer, ___ Mont. at ___, 684 P.2d at 1116 (citing Osborne v. Johnson, 432 S.W.2d 800, 803 (Ky. 1968)).
40. Id.
41. Id. at ___, 684 P.2d at 1116 (citing Osborne, 432 S.W.2d at 803 (quoting 2 A. Larson, Workmen's Compensation Law § 57.10 (1968))).
42. Id. at 1117.
43. Mont. Code Ann. § 39-71-116(12) (1983) states, "Permanent Partial Disability" means that condition resulting from injuries as defined in this chapter that results in the actual loss of earnings or earning capability less than total that exists after the injured worker is as far restored as the permanent character of the injuries will permit.
44. Hafer, ___ Mont. at ___, 684 P.2d at 1118.
46. Id. at 129, 572 P.2d at 909.
47. Hafer, ___ Mont. at ___, 684 P.2d at 1117.
Judge Reardon wrote with persuasive logic, but the Montana Supreme Court embraced a more expansive view of Hafer's situation. While the Workers' Compensation Court merely focused on Hafer's job with a single employer, the high court looked at Hafer's employability on the open labor market. The testimony of the Job Service expert had established a 40% loss of earning capacity in that market. The supreme court adopted the more realistic perspective because of the probability that Hafer would not remain with Anaconda the rest of his working life.

The Hafer court reemphasized its stance that the principal aim of workers' compensation coverage is social insurance which protects the injured workman against disability from a work-related injury. The Hafer court continued, "Obviously, the purpose of workers' compensation is to protect the worker against economic loss. Therefore, any disability rating which does not achieve this goal must be set aside and a figure representing potential economic loss must be substituted." In essence, a claimant's degree of earning capacity impairment is the bottom line and other variables need not be considered. The court concluded, "Since the court has determined that Hafer's earning capacity has been reduced by 40%, that is the figure to be used in computing his benefits."

In addition, the Hafer court restricted the application of the disability factor. It declared that the disability factor, in this case 40%, could only be used to calculate the proper weekly benefit, "and will no longer . . . limit the number of weeks for which the benefit is payable."

C. Future Implications

Hafer adds a key element to the determination of permanent partial disability. In the future, the percentage of a worker's partial disability will be determined by comparing the amount of wages the claimant can earn in the kind of employment available to him, to the amount of wages he could have earned before the injury.

The decision does not provide a passkey to the compensation fund. By basing the compensation on a diminution in earning ca-
capacity, the fund pays benefits regardless of actual wage loss. This concept cuts two ways: The ironworker who lost the use of his arm, yet has returned to work at higher wages, still receives the scheduled amount of benefits. Conversely, if he remains unemployed because of his disability, the benefits expire after 280 weeks.55

_Hafer_ wisely recognizes that compensation awards should bear a reasonable relation to a claimant's past earnings, and be based on the reduction of earning capacity, rather than arbitrary amounts dictated by the type of medical injury sustained.56 The _Hafer_ court limits the doctor's medical testimony to the question of what jobs the claimant can physically perform, taking into account the claimant's qualifications and training.57 The actual medical loss due to the injury is only one variable in determining that capability.

By incorporating medical impairment into the larger category of earning capacity, _Hafer_ represents a flexible compromise which assesses the claimant in the context of the local job market. In our increasingly transient society, _Hafer_ permits an injured worker to move freely between jobs without impairing his compensation, because his earning capacity travels with him.

The decision promotes efficient distribution of compensation benefits and reduces waste of compensation dollars on nondisabling losses.58 The _Hafer_ decision hinges compensation on loss of earning capacity, thereby benefitting truly disabled workers and reducing cash awards to workers whose injuries have not significantly impaired their earning capacity. After _Hafer_, the amount of compensation will be predicated on the degree to which the injury reduces the worker's ability to do his job.59

_Hafer_'s emphasis on earning capacity may also reduce the disability evaluation quarrels which have plagued the Workers' Compensation Court.60 Expert witnesses will still disagree on the claimant's earning capacity in the open labor market, but that market may be easier to quantify than the doctors' estimates of physical impairment.

55. _MONT. CODE ANN. § 39-71-705(1) (1985)_ states in relevant part, "[Benefits] shall be paid for the following periods: one arm at or near the shoulder. . . 280 weeks."
57. _Hafer_, Mont. at ___, 684 P.2d at 1114.
58. Larson, _supra_ note 56, at 524.
59. _Hafer_, Mont. at ___, 684 P.2d at 1118.
V. Conclusion

The Hafer decision allows a more realistic appraisal of the claimant's true economic position. It tailors compensation to the actual damage a claimant suffers to his employability. The loss of earning capacity concept leaves room for adjustments in both pre- and post-injury earnings, and allows for an accurate representation of the true impact attributable to the injury. Hafer permits economic increases in wage levels, anticipates changes in the claimant's age, training, or hours, and recognizes the impermanence of particular post-injury earnings.\footnote{2 A. Larson, The Law of Workmen's Compensation §§ 57.32 to 57.40 (1983).}

The Hafer case reflects contemporary social developments. As our society moves toward increasing job specialization, identical injuries do not have identical effects on specialized workers. Today, economists have the statistical tools to measure the vitality of a region's economy. Within that economic framework, labor analysts have the expertise to accurately evaluate the local job market. Hafer allows today's worker to be plugged into that matrix to determine earning capacity.

Most importantly, the decision defends the welfare of the worker. It looks at potential, rather than impairment. Hafer wisely removes the focus of permanent partial disability from the injury itself and emphasizes the worker's future employability.