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Damages Pt. 6 – Availability of Prejudgment Interest

In this, the sixth installment in our series on damages, the attorneys at Pavlack Law discuss the issue of prejudgment interest and when it may be available to a successful plaintiff.

One aspect of damages that is often overlooked by both litigants and their attorneys is the role of prejudgment interest. While we are all comfortable and familiar with the expectation of interest on loan debts or bank accounts, the concept of prejudgment interest in a legal case may be a bit foreign. In order to fully appreciate why and when prejudgment interest might be available to a successful plaintiff, it is important to understand the underlining rationale.

The fundamental concept that supports a court awarding prejudgment interest is that there is a time value to money. What this means is that a dollar today is worth more than the same dollar a year from now. Now, many of you may be under the impression that this concept is somehow tied to inflation. However, I assure you that this concept exists independently of inflation – though inflation may impact the precise future value of that dollar. The time value of money is based on the ability to invest or otherwise utilize money to obtain a greater amount of it in the future. Magistrate Judge Roger B. Cosby of the Northern District of Indiana recently discussed the role of prejudgment interest in awarding damages:

Prejudgment interest is an element of damages—it is used to make the victim whole. . . . Prejudgment interest compensates the prevailing party for the loss of use of money during the time between the wrong and the conclusion of the litigation. . . . That is, [m]oney has a time value, and prejudgment interest is therefore necessary in the ordinary case to compensate a plaintiff fully for a loss suffered at time t and not compensated until $t + 1, 2, 3 \dots n$.

As Magistrate Cosbey notes the purpose of prejudgment interest is to help make the victim whole. If you recall from our previous post in Pt. 3 on our series of damages, the purpose of damages is to make the injured party whole. Since there is a recognized time value to money, the only way to make an injured person whole is for a court to award compensation for that lost time value. That award generally takes the form of prejudgment interest.

To illustrate the time value of money let us examine the calculation of the future value of money. The standard formula for calculating the future value of money is $FV = PV \times (1 + i)^n$, where FV is the future value of money, PV is the present value, i is the applicable interest rate, and n represents the number of years. To illustrate how to apply this formula let us attempt to determine the value of \$10,000 three years from now at a 6% rate of interest. The calculation should look like this. $FV = \$10,000 \times (1 + 6\%)^3 = \$10,000 \times (1 + .06)^3 = \$10,000 \times (1.06)^3 = \$10,000 \times (1.191016) = \$11,910.16$. So what this means, is that for a plaintiff to be made whole three years from now for \$10,000 worth of damages today, the plaintiff would need to be awarded almost \$12,000.

You might wonder why I chose to apply a 6% interest rate. I assure that my decision to do so was not arbitrary. Indiana statutory law does not fix a specific rate for calculating prejudgment interest. However, it does provide a fixed range between 6% and 10% from which a court can choose to apply. It is worthy of note that the future value formula discussed above deals with compound interest whereas the statute requires a court to use simple interest. The formula for the simple rate of interest is much less complex—though less effective at capturing the actual time value of money. The simple rate of interest formula is $I = P \times r \times t$, where P is the principal amount of money, r is the interest rate, and t is the amount of time. So, applying that to our example above: $I = \$10,000 \times 6\% \times 3 \text{ years} = \$10,000 \times .06 \times 3 = \$10,000 \times .18 = \$1,800$. Meaning, that in addition to the \$10,000 in damages, the court may also award \$1,800 in interest. But, since the calculation is simple interest and not compound interest, the plaintiff will lose out on \$110.16.

While prejudgment interest may be available in many if not most contract actions, there are very specific procedures that must be followed in order for a

plaintiff to collect prejudgment interest in a tort case such as a personal injury or car crash case. The Indiana Court of Appeals very recently discussed these procedures in the case *Kosarko v. Padula*. In that case the court stated:

A trial court may award prejudgment interest as part of a judgment in “any civil action arising out of tortious conduct.” Ind. Code § 34-51-4-1. The period during which prejudgment interest accrues may not exceed forty-eight months. Ind. Code § 34- 51-4-8. Prejudgment interest is not permitted if:

(1) within one (1) year after a claim is filed in the court, or any longer period determined by the court to be necessary upon a showing of good cause, the party who filed the claim fails to make a written offer of settlement to the party or parties against whom the claim is filed; (2) the terms of the offer fail to provide for payment of the settlement offer within sixty (60) days after the offer is accepted; or (3) the amount of the offer exceeds one and one-third (1 1/3) of the amount of the judgment awarded.

Ind. Code § 34-51-4-6. The purpose of these statutes is to encourage settlement and to compensate the plaintiff for the lost time value of money. . . . Prejudgment interest is recoverable not as interest but as additional damages to accomplish full compensation.

Thus, it is clear, in a tort case it is extremely important to follow the specific procedures of the statute because failure to do so can mean that a successful plaintiff who was otherwise able to recover prejudgment interest might lose out on thousands of dollars of recovery. This is yet another reminder that the law is a very complex minefield in which it is of the utmost importance to find an attorney who understands the intricacies of Indiana law, has experience defending the rights of injured persons, and will zealously advocate for his clients rights.

Join us again next week for another installment of our ongoing series on damages. And as always, remember, safety first, Pavlack Law second.

- Pt. 1 – Introduction to Damages and Loss of Consortium
- Pt. 2 – Duty to Mitigate Damages
- Pt. 3 – Diminished Value of Vehicle Due to Traffic Accident
- Pt. 4 – Damages for Negligently Inflicted Emotional Distress
- Pt. 5 – Assessing Damages When Injured Person is Partially at Fault

- Pt. 7 – Indiana Crime Victim's Relief Act
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- Pt. 9 – Damages for the Loss of Chance of Survival from Medical Malpractice
- Pt. 10 – Punitive Damages Under Indiana Law
- Pt. 11 – Wrongful Death
- Pt. 12 – Contract Damages

Sources

- *BKCAP, LLC v. Captec Franchise Trust 2000-1*, No. 307-cv-637, 2011 U.S. Dist. LEXIS 119846, at *6-7 (N.D. Ind. October 14, 2011).
- *Kosarko v. Padula*, 960 N.E.2d 810 (Ind. Ct. App. 2011), *vacated*, 979 N.E.2d 144 (Ind. 2012).
- Indiana Code Chapter 34-51-4.

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