

## **No Basis for High Insurance Rates:**

An Analysis of the 15 Largest  
Medical Malpractice Insurers  
2006 Financial Statements

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## **I. Introduction**

Medical malpractice insurers recently filed their financial statements for 2006, known as Annual Statements, with state insurance departments.

The data contained in these Statements demonstrate that the premise on which the insurance industry based its “tort reform” campaign of the last several years--that malpractice claims payments have been increasing--is false. Specifically, the 2006 Annual Statements reveal that the amount the leading malpractice insurers project they will pay out in claims in the future has declined; that the amount they have actually paid out in claims has declined; and that their surplus--the extra cushion they have accumulated over and above the amount they have set aside to pay claims in the future--has increased to an all time high. In addition, the 2006 Annual Statements reveal that notwithstanding the record surplus and profits of these carriers, they have generally declined to issue any dividends to their policyholders.

## **II. Incurred losses vs. earned premiums**

Contrary to the public statements the leading malpractice carriers made between 2003 and 2006 about malpractice claims allegedly increasing, the “incurred losses” of the 15 leading malpractice carriers dropped substantially<sup>1</sup> during that period. Specifically, as Table 1 indicates, the “incurred losses” of these carriers declined from \$2.598 billion in 2003 to \$1.349 billion in 2006, or by 48%.

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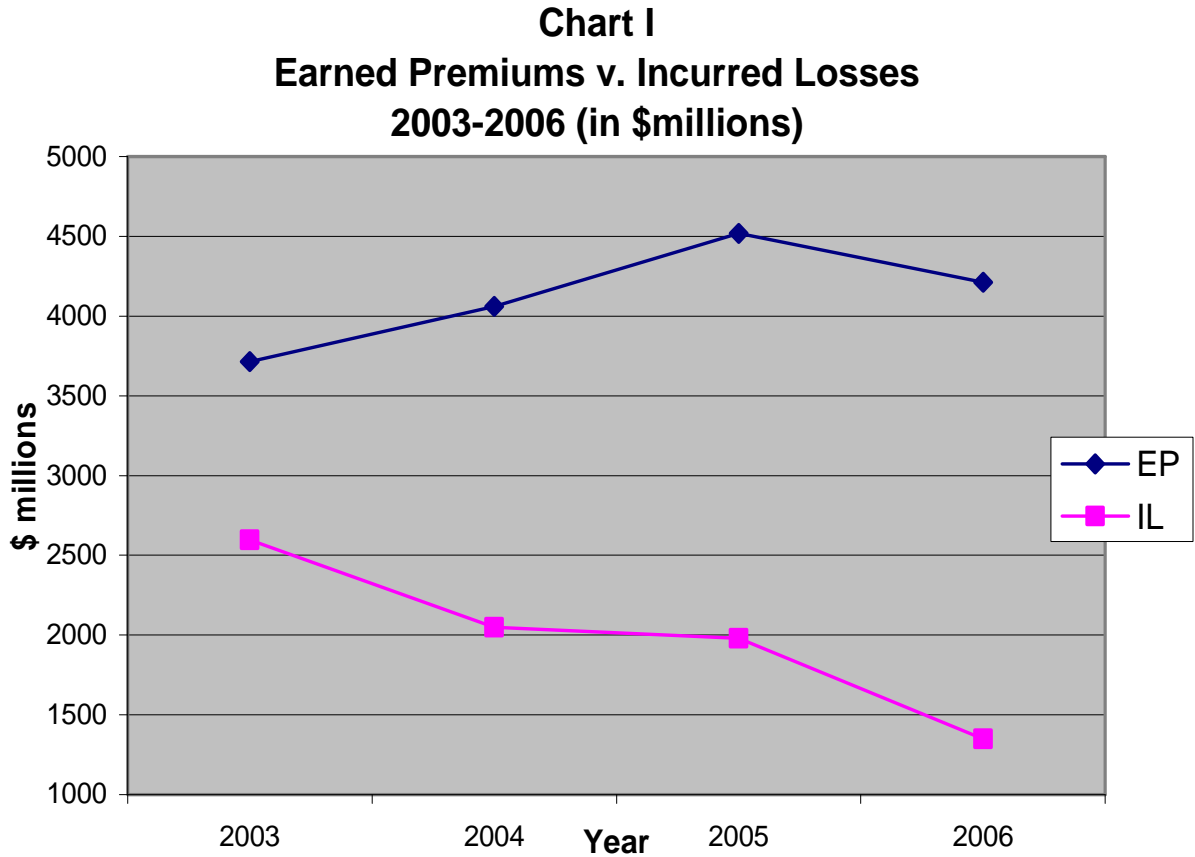
<sup>1</sup> The 2004 Annual Statements, which the original Falling Claims study was based on, disclosed incurred losses for 2003 and 2004. The 2006 Annual Statements disclose incurred losses for 2005 and 2006

**Table 1**  
**Earned Premiums v. Incurred Losses, 2003-2006 (in \$millions)**

<b>Company</b>		<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>Change 2003-2006</b>
Med Pro	EP	701.8	555.0	*-215.0	299.6	-57.3
	IL	441.9	281.2	*-184.1	114.7	-74.0
Lexington	EP	364.5	446.3	524.8	511.9	40.4
	IL	311.0	254.5	155.7	145.6	-53.2
TDC	EP	331.3	444.4	449.8	478.2	44.3
	IL	230.0	240.5	181.2	129.4	-43.7
HCI	EP	374.7	369.4	343.0	314.2	-16.1
	IL	334.0	175.7	205.2	61.2	-81.7
MedAssurance	EP	274.0	317.9	303.1	305.3	11.4
	IL	124.1	109.2	76.6	28.8	-76.8
Cont. Casualty	EP	227.3	293.3	376.3	425.1	87.0
	IL	185.3	183.5	196.0	151.8	-18.1
ISMIE	EP	257.7	247.8	242.2	243.2	-5.6
	IL	188.6	150.7	120.5	86.4	-54.2
ProMutual	EP	182.6	232.2	319.0	337.7	84.9
	IL	176.2	138.7	188.0	197.0	11.8
MAG Mutual	EP	131.4	201.3	269.1	283.7	115.9
	IL	121.6	81.3	147.5	147.4	21.2
Norcal	EP	202.1	198.7	190.4	192.8	-4.6
	IL	94.0	91.6	67.2	35.1	-62.7
ProNational	EP	178.9	190.8	195.5	191.4	7.0
	IL	91.0	63.2	25.1	30.6	-66.4
AP Capital	EP	146.4	181.4	161.2	151.7	3.6
	IL	120.5	100.0	68.8	52.4	-56.5
State Volunteer	EP	116.3	140.4	154.6	187.9	61.6
	IL	60.1	76.1	71.3	93.0	54.7
Evanston	EP	131.3	134.4	135.5	124.8	-5.0
	IL	66.7	57.9	35.6	13.2	-80.2
FPIC	EP	95.1	106.1	165.0	165.3	73.8
	IL	53.1	44.8	51.3	62.8	18.3
<b>Totals</b>	<b>EP</b>	<b>3715.4</b>	<b>4059.4</b>	<b>3614.5</b>	<b>4212.8</b>	<b>13.4</b>
	<b>IL</b>	<b>2598.1</b>	<b>2048.9</b>	<b>1405.8</b>	<b>1349.4</b>	<b>-48.1</b>

\*These numbers are negative due to the acquisition of Medical Protective by Berkshire Hathaway in 2005, and the manner in which that acquisition was accounted for.

Chart 1 displays the information in Table 1 graphically.



An insurer's "incurred losses" in a given year are not the actual claims payments it makes in that year. Rather, they are the claims payments the insurer projects it will make in the future for injuries that occurred in that year, plus any changes in the amount the insurer has reserved to pay claims that arose in prior years. A decline in an insurer's "incurred losses," therefore, can mean two things. First, it can mean that the insurer's projected claims payments for injuries occurring in a given year are less than its projected claims payments for injuries occurring in a previous year. Second, it can mean that the insurer has reduced its projected claims payments for injuries occurring in prior years. The dramatic decrease in the incurred losses reported by the 15 leading carriers in 2006 necessarily means that in 2006

they reduced the amount they had initially projected they would pay out for claims covered by prior years' policies. Because the rate increases of the last several years were based on those excessive projections, those rate increases were by definition excessive.

Nine carriers reduced their incurred losses by more than 50% between 2003 and 2006. Those carriers, and the extent to which they reduced their incurred losses, were as follows:

<u>Carrier</u>	<u>Change in incurred losses, 2003 to 2006</u>
Lexington	-53.2%
MedPro	-74.0%
HCI	-81.7%
MedAssurance	-76.8%
ISMIE	-54.2%
Norcal	-62.7%
ProNational	-66.4%
AP Capital	-56.5%
Evanston	-80.2%.

Notably, two of the carriers who have most stridently argued that malpractice claims were increasing—ISMIE and Norcal—were among those whose incurred losses dropped by more than 50%.

The sharp decline in incurred losses of the 15 leading carriers also means that their “incurred loss ratio” – which insurers refer to simply as the “loss ratio” – has declined sharply. That ratio is the ratio between incurred losses and earned premium. All other things equal, the lower the loss ratio, the more profitable the insurer. As Table 2 indicates, the

incurred loss ratio of the 15 leading malpractice carriers declined substantially in each of the last five years,<sup>2</sup> reaching a low of 31.4 in 2006.

**Table 2**  
**Incurred Loss Ratios, 2000-2006**

<b>Company</b>	<b>2000</b>	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>
ISMIE	83.6	72.4	100.7	73.2	60.8	49.7	35.6
MAG Mutual	66.8	58.4	81.3	61.9	60.4	54.8	52.0
TDC	42.5	73.5	69.1	69.4	54.1	40.3	27.1
Med Pro	41.1	50.4	78.9	63.0	50.7	85.6	38.3
ProMutual	128.9	117.6	101.4	96.5	59.7	58.9	58.3
AP Capital	58.8	90.5	75.7	82.3	55.2	42.7	34.5
State Volunteer	75.9	69.6	72.3	51.7	54.2	46.1	49.5
HCI	74.4	97.2	88.1	89.1	47.6	59.8	19.5
Norcal	56.9	60.5	41.7	46.5	46.1	35.3	18.2
FPIC	70.6	72.9	64.1	55.8	42.2	31.0	38.0
Med Assurance	21.7	45.9	45.9	45.3	34.4	25.3	9.4
ProNational	82.4	93.8	61.4	50.8	33.1	12.8	16.0
CCC	62.1	215.4	54.1	81.5	62.6	51.1	35.7
Evanston	75.7	63.8	58.8	50.8	43.1	26.4	10.6
Lexington	71.8	153.8	56.9	85.3	57.0	29.7	28.4
<b>Average, all 15 insurers:</b>	<b>67.5</b>	<b>89.0</b>	<b>70.0</b>	<b>66.9</b>	<b>50.7</b>	<b>43.3</b>	<b>31.4</b>

<sup>2</sup> The data in this report for the years 2003-2006 are taken from the Annual Statements for 2003-2006. Data for years prior to 2003 are taken from an earlier study entitled "Falling Claims and Rising Premiums in the Medical Malpractice Insurance Industry," released by the Center for Justice and Democracy in July 2005.

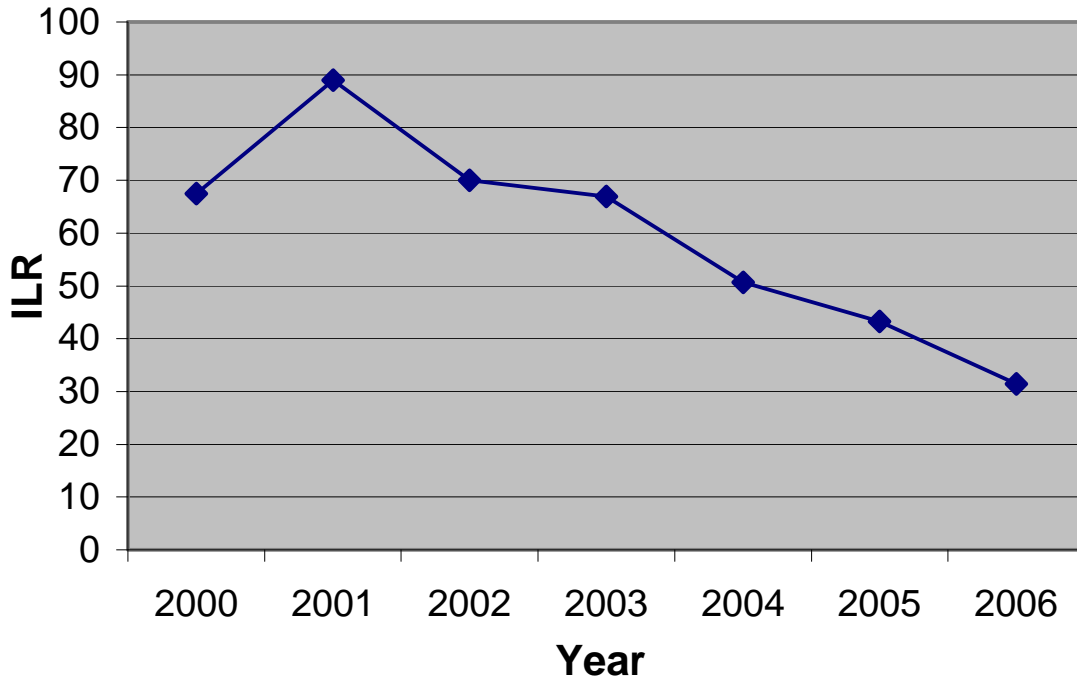
A 31.4% incurred loss ratio is very low: it means that in 2006 the 15 leading carriers projected that they will ultimately pay out in claims 31.4 cents for each premium dollar they earn, with the remaining 68.6 cents of the premium dollar going for overhead--e.g., executive salaries, marketing and advertising, and lawyers and lobbyists--and profit. That profit is in addition to the profit provided by the income they earn on their investments.

It is important to note that the denominator in the incurred loss ratio—earned premium—is a hard number, while the numerator—incurred losses—is an estimate. That estimate can be manipulated for political or other reasons, and often turns out to be substantially inaccurate, as explained above. Nevertheless, the industry uses the incurred loss ratio as a major indicator of an insurer's performance. The substantial decline in that ratio since 2000, and the decline of almost two-thirds in that ratio from its high of 89.0 in 2001, thus indicates a dramatic increase in the profitability of the 15 leading malpractice carriers over the last five years based on one of the primary metrics customarily used by the industry.

Chart 2 sets forth the decline in the average incurred loss ratio graphically.



**Chart 2  
Incurred Loss Ratios, 2000-2006**



### **III. Paid losses vs. written premiums**

The trend in the claims actually paid each year by the 15 leading malpractice carriers also demonstrates that the industry's claim that malpractice claims have been increasing is false. For example, as Table 3 indicates, the net paid claims<sup>3</sup> of these carriers decreased from \$1.344.4 billion in 2000 to \$1.147 billion in 2006, or by 14.7%, before accounting for inflation. Between 2003 and 2006--the same period during which their incurred losses decreased by 48%--their net paid losses decreased from \$1.216 billion to \$1.147 billion, or by 5.6%. Meanwhile, these carriers all increased their rates substantially.

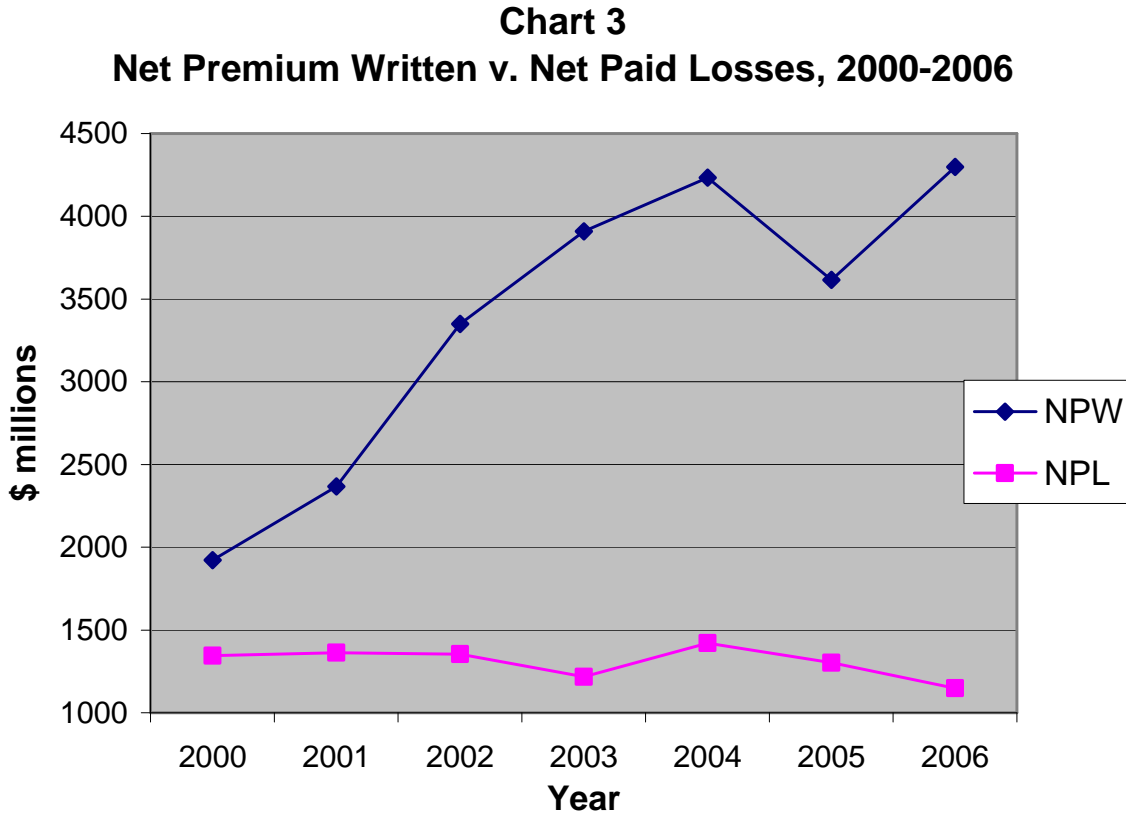
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<sup>3</sup> Net paid claims are paid claims before accounting for reinsurance transactions.

**Table 3**  
**Net Premium Written v. Net Paid Losses**

<b>Company</b>		<b>2000</b>	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>Totals 2000-2006</b>	<b>Change 2000-2006</b>
MedPro	NPW	267.1	345.0	538.4	713.5	526.3	-342.6	337.4	2,385.1	26.3%
	NPL	152.4	151.9	190.4	216.9	257.8	243.0	84.2	1,296.6	-44.8%
	Ratio	57.0%	44.0%	35.4%	30.4%	49.0%	NM	25.0%	54.0%	
Lexington	NPW	21.1	94.2	274.5	442.7	483.0	545.4	514.9	2,375.8	2340.3%
	NPL	12.2	33.4	25.9	14.6	65.1	59.3	89.5	300.0	633.6%
	Ratio	58.1	35.5	9.4	3.3	13.5	10.9	17.4	12.6	
TDC	NPW	209.7	274.1	389.2	332.0	457.2	454.2	492.9	2,609.3	135.1%
	NPL	115.1	123.8	171.5	167.6	143.2	140.0	154.3	1,015.5	34.1%
	Ratio	54.8	45.2	44.1	50.5	31.1	30.8	31.3	38.9	
HCI	NPW	197.1	260.3	318.6	377.0	370.1	344.5	312.9	2,180.5	58.8%
	NPL	231.8	168.0	182.5	190.7	157.6	139.9	141.2	1,211.7	-39.1%
	Ratio	117.6	64.5	57.3	50.6	42.6	40.6	45.1	55.6	
Cont. Cas.	NPW	114.3	89.5	196.5	245.1	347.1	407.5	449.0	1,849.0	292.8%
	NPL	208.7	188.7	71.5	-79.4	157.0	155.7	99.2	801.4	-52.5%
	Ratio	182.6	210.8	36.4	-32.4	45.2	38.2	22.1	43.3	
MedAssur.	NPW	170.5	156.9	227.0	294.2	321.7	297.0	287.3	1,754.6	68.5%
	NPL	48.2	68.1	62.5	48.1	32.0	30.2	21.0	310.1	-56.4%
	Ratio	28.3	43.4	27.5	16.3	9.9	10.2	7.3	17.7	
ProMutual	NPW	98.1	127.0	171.2	190.9	263.4	351.1	341.5	1,543.2	248.1%
	NPL	115.7	107.8	78.8	90.6	93.6	79.0	122.5	688.0	5.9%
	Ratio	117.9	84.8	46.0	47.5	35.6	22.5	35.9	44.6	
MAG Mutual	NPW	82.7	114.1	142.2	157.2	256.6	286.3	282.9	1,322.0	242.1%
	NPL	38.1	40.4	60.5	77.2	83.3	81.3	66.4	447.2	74.3%
	Ratio	46.1	35.4	42.6	49.1	32.5	28.4	23.5	33.8	
ISMIE	NPW	139.4	175.5	217.5	276.8	223.8	247.5	278.0	1,558.5	99.4%
	NPL	129.8	115.1	119.4	126.2	126.6	98.3	113.8	829.2	-12.3%
	Ratio	93.1	65.6	54.9	45.6	56.6	39.7	40.9	53.2	
Norcal	NPW	129.3	170.3	169.2	201.2	200.8	199.6	200.8	1,271.2	55.3%
	NPL	52.8	70.1	82.0	81.5	69.7	57.7	67.5	481.3	27.8%
	Ratio	40.8	41.2	48.5	40.5	34.7	28.9	33.6	37.9	
ProNational	NPW	110.1	132.1	148.7	193.0	197.2	189.2	184.9	1,155.2	67.9%
	NPL	67.6	77.3	56.9	53.1	25.0	22.7	34.8	337.4	48.5%
	Ratio	61.4	58.5	38.3	27.5	12.7	12.0	18.8	29.2	
AP Capital	NPW	157.1	179.6	208.7	109.8	170.9	154.1	146.8	1,127.0	-6.6%
	NPL	61.8	90.1	117.3	118.3	64.6	62.9	44.3	559.3	-28.3%
	Ratio	39.4	50.2	56.2	107.7	37.8	40.8	30.2	49.6	
State Volunteer	NPW	77.4	94.5	130.8	135.2	150.0	161.0	190.9	939.8	146.6%
	NPL	41.8	54.5	56.6	50.7	70.7	64.4	79.5	418.2	90.2%
	Ratio	54.0	57.6	43.2	37.5	47.1	40.0	41.6	44.5	
FPIC	NPW	110.3	93.6	94.0	103.4	136.5	183.8	162.0	883.6	46.9%
	NPL	45.0	53.2	48.3	27.9	49.1	42.1	-3.3	262.3	NM
	Ratio	40.7	56.9	51.4	27.0	35.9	22.9	-2.0	29.7	
Evanston	NPW	38.1	60.4	123.3	137.3	128.5	136.9	117.5	742.0	208.4%
	NPL	23.4	21.1	30.0	32.1	26.0	26.5	32.1	191.2	37.2%
	Ratio	61.4	34.9	24.3	23.4	20.2	19.4	27.3	25.8	
<b>Totals</b>	<b>NPW</b>	<b>1,922.2</b>	<b>2,367.1</b>	<b>3,349.8</b>	<b>3,909.3</b>	<b>4,233.1</b>	<b>3,615.5</b>	<b>4,299.7</b>	<b>23,696.7</b>	<b>123.7%</b>
	<b>NPL</b>	<b>1,344.4</b>	<b>1,363.5</b>	<b>1,354.1</b>	<b>1,216.1</b>	<b>1,421.3</b>	<b>1,303.0</b>	<b>1,147.0</b>	<b>9,149.4</b>	<b>-14.7%</b>
	<b>Ratio</b>	<b>69.9</b>	<b>57.6</b>	<b>40.4</b>	<b>31.1</b>	<b>33.6</b>	<b>36.0</b>	<b>26.7</b>	<b>38.6</b>	

The difference between the trend in net written premiums and the trend in net paid losses is graphically shown in Chart 3:



As Table 3 indicates, over the seven year period 2000-2006 five carriers substantially increased their premiums while their claims payments fell substantially. Those carriers, and the extent to which their net premiums rose and their claims payments fell during that period, are as follows:

<u>Carrier</u>	<u>Change in written premiums, 2000-2006</u>	<u>Change in paid losses, 2000-2006</u>
MedPro	+26.3%	-44.8%
HCI	+58.8%	-39.1%
Cont. Cas.	+292.8%	-52.5%
MedAssurance	+68.5%	-56.4%
ISMIE	+99.4%	-12.3%

Chart 4 illustrates graphically the extent to which these carriers increased their premiums while their claims payments fell.

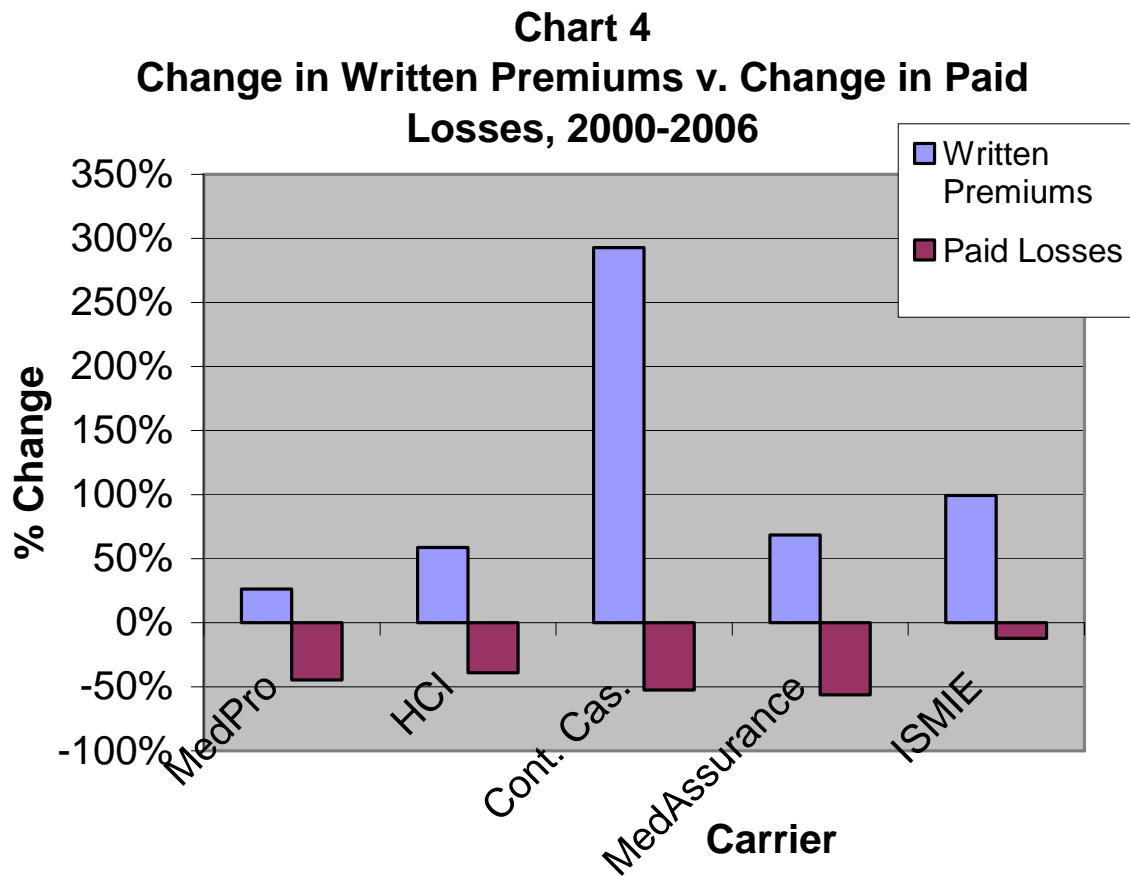


Table 4 compares gross written premium with gross paid losses. It indicates that during the 2003-2006 period in which incurred losses fell by 48.1%, gross paid losses fell by 10%. Between 2000 and 2006, gross malpractice claims payments<sup>4</sup> rose by 2% before accounting for inflation, and fell after accounting for inflation, while gross premiums rose by 123%.

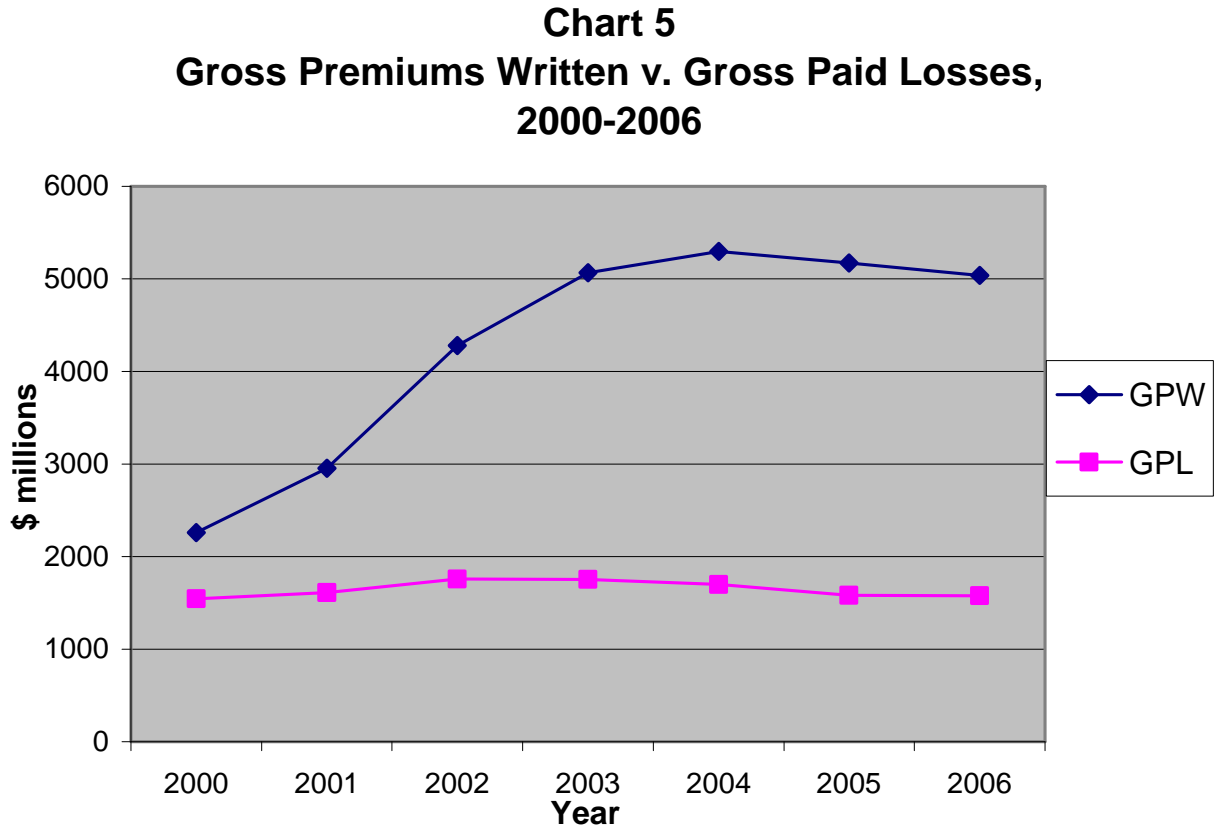
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<sup>4</sup> Gross paid claims are paid claims before accounting for reinsurance transactions.

**Table 4**  
**Gross Premiums Written v. Gross Paid Losses, 2000-2006**  
**(in \$millions)**

<b>Company</b>		<b>2000</b>	<b>2001</b>	<b>2002</b>	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>Totals 2000-2006</b>	<b>Change 2000-2006</b>
Lexington	GPW	71.8	170.4	567.4	788.9	778.6	718.7	658.8	3,754.6	817.5%
	GPL	23.9	75.7	65.9	100.1	124.2	101.8	139.8	631.4	484.9%
	Ratio	33.3%	44.4%	11.6%	12.7%	16.0%	14.2%	21.2%	16.8%	
MedPro	GPW	298.6	380.2	586.5	849.3	736.5	672.1	678.0	4,201.2	127.1%
	GPL	200.2	189.3	230.0	250.9	296.8	280.0	206.9	1,654.1	3.2%
	Ratio	67.5%	49.8%	39.2%	29.5%	40.3%	41.8%	30.5%	39.4%	
TDC	GPW	236.6	311.3	428.1	431.3	489.6	497.4	522.8	2,917.1	121.0%
	GPL	130.4	140.7	196.0	197.5	155.0	165.3	176.7	1,161.6	35.5%
	Ratio	55.1%	45.2%	45.8%	45.8%	31.7%	33.2%	33.8%	39.8%	
ISMIE	GPW	164.8	209.0	265.6	364.3	425.3	405.3	386.4	2,220.7	134.5%
	GPL	163.8	141.3	158.1	165.2	153.4	144.8	154.1	1,080.7	5.9%
	Ratio	99.4%	67.6%	59.5%	45.3%	36.1%	35.7%	39.9%	48.7%	
HCI	GPW	243.6	288.4	344.7	386.5	382.2	344.7	321.3	2,311.4	31.9%
	GPL	276.8	193.5	237.3	206.9	187.1	144.4	145.0	1,391.0	-47.6%
	Ratio	113.6%	67.1%	68.8%	53.5%	49.0%	41.0%	45.1%	60.2%	
MAG Mutual	GPW	87.8	131.4	216.3	286.9	358.7	361.4	351.0	1,793.5	299.8%
	GPL	48.8	50.8	79.1	95.6	102.7	111.7	104.7	593.4	114.5%
	Ratio	55.5%	38.7%	36.6%	33.3%	28.6%	30.9%	29.8%	33.1%	
Med Assurance	GPW	196.3	224.5	292.3	335.8	357.0	339.5	309.9	2,055.3	57.9%
	GPL	76.4	96.4	83.5	60.5	59.9	44.2	31.3	452.2	-59.0%
	Ratio	38.9%	42.9%	28.6%	18.0%	16.8%	13.0%	10.1%	22.0%	
ProMutual	GPW	107.0	148.4	182.8	216.2	273.3	360.4	346.3	1,634.4	223.6%
	GPL	122.3	123.5	84.9	92.3	100.6	80.4	126.1	730.1	3.1%
	Ratio	114.3%	83.2%	46.5%	42.7%	36.8%	22.3%	36.4%	44.7%	
FPIC	GPW	179.3	212.2	295.8	287.0	285.2	277.7	245.4	1,782.6	36.9%
	GPL	59.7	79.1	70.3	78.9	101.7	105.9	111.9	607.5	87.4%
	Ratio	33.3%	37.3%	23.8%	27.5%	35.7%	38.1%	45.6%	34.1%	
State Volunteer	GPW	98.0	120.4	164.0	212.6	241.5	259.2	266.7	1,362.4	172.1%
	GPL	51.7	61.8	64.1	59.3	76.9	74.4	87.0	475.2	68.3%
	Ratio	52.7%	51.3%	39.1%	27.9%	31.8%	28.7%	32.6%	34.9%	
Norcal	GPW	150.7	179.0	181.9	212.2	209.5	208.0	212.3	1,353.6	40.9%
	GPL	57.4	85.0	89.8	86.1	73.7	59.4	68.4	519.8	19.2%
	Ratio	38.0%	47.5%	49.4%	40.6%	35.2%	28.6%	32.2%	38.4%	
ProNational	GPW	139.6	151.9	167.8	203.6	207.5	199.5	191.8	1,261.7	37.4%
	GPL	81.4	89.4	68.2	67.5	39.4	30.6	49.5	426.0	-39.2%
	Ratio	58.3%	58.9%	40.6%	33.2%	19.0%	15.3%	25.8%	33.8%	
Cont.Casualty	GPW	72.2	140.2	177.5	173.0	196.6	190.1	250.6	1,200.2	247.1%
	GPL	165.7	150.7	151.8	111.9	108.4	131.9	82.7	903.1	-50.1%
	Ratio	229.5%	107.5%	85.5%	64.7%	55.2%	69.4%	33.0%	75.2%	
AP Capital	GPW	170.0	209.7	236.8	135.7	192.3	175.0	156.9	1,276.4	-7.7%
	GPL	69.7	109.2	142.1	142.9	88.1	75.2	51.2	678.4	-26.5%
	Ratio	41.0%	52.1%	60.0%	105.3%	45.8%	43.0%	32.6%	53.1%	
Evanston	GPW	45.1	78.1	171.2	182.4	164.5	162.7	141.5	945.5	213.7%
	GPL	26.2	23.7	36.1	38.4	30.9	32.4	40.6	228.3	55.0%
	Ratio	58.1%	30.3%	21.1%	21.6%	18.8%	19.9%	28.7%	24.1%	
<b>Totals</b>	<b>GPW</b>	<b>2,259.6</b>	<b>2,955.1</b>	<b>4,278.7</b>	<b>5,065.7</b>	<b>5,298.3</b>	<b>5,171.7</b>	<b>5,039.7</b>	<b>30,068.8</b>	<b>123.0%</b>
	<b>GPL</b>	<b>1,544.4</b>	<b>1,610.1</b>	<b>1,757.2</b>	<b>1,754.0</b>	<b>1,698.8</b>	<b>1,583.3</b>	<b>1,575.9</b>	<b>11,523.7</b>	<b>2.0%</b>
	<b>Ratio</b>	<b>68.3%</b>	<b>54.5%</b>	<b>41.1%</b>	<b>34.6%</b>	<b>32.1%</b>	<b>30.6%</b>	<b>31.3%</b>	<b>38.3%</b>	

The difference between the trend in gross written premiums and the trend in gross paid losses is graphically shown in Chart 5:



Interestingly, over the seven-year period 2000-2006 both the ratio between net paid losses and net written premiums, and the ratio between gross paid losses and gross written premiums, were approximately 38.5. Because the premiums an insurer receives in a given year are used to pay for claims it pays in future years, start-up or very fast-growing companies with low paid loss ratios are not necessarily profitable, since for such companies premiums grow very fast in the early years, while the paid claims covered by those premiums grow very fast in later years. Conversely, mature companies with high paid loss ratios are not necessarily unprofitable, since the claims they pay in a given year are covered by policies for which they have collected the premium in prior years. Nevertheless, for most mature

companies the paid loss ratio over time can be a relevant indicator of performance, particularly in combination with other measures.

The 38.5% paid loss ratio of the 15 leading malpractice carriers over the last seven years means that their claims payments have been little more than one-third of the premiums they collected during that period.

#### **IV. Surplus analysis**

The surpluses the 15 leading malpractice carriers have accumulated as of year-end 2006 also demonstrate the falsity of the medical malpractice insurance industry's public statements. An insurer's surplus is the extra cushion it holds over and above the amount it has reserved to pay claims in the future. An insurer increases its surplus to the extent that, after setting aside a sufficient amount to pay its projected claims, it both earns a profit and declines to distribute that profit to its shareholders (in a stock company) or policyholders (in a mutual company).

As Table 5 indicates, the 2006 Annual Statements reveal that since 2003 the surpluses of the 12 leading "monoline" carriers—those which write only medical malpractice insurance—have risen by 43%, from \$3.202 billion to \$4.586 billion.



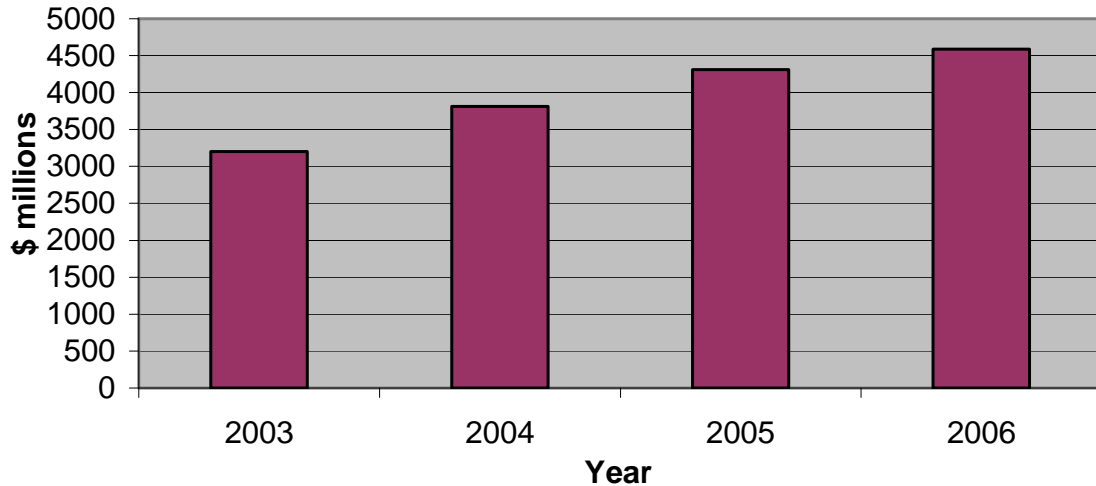
**Table 5**  
**Increase in Surplus of 12 Leading Monoline Carriers, 2003-2006 (in \$millions)**

Company	2003 Surplus	2004 Surplus	2005 Surplus	2006 Surplus	Change (\$) 2003- 2006	Change (%) 2003- 2006
HCI	626.5	767.8	800.3	521.9	-104.6	-16.7%
Med Pro	442.9	510.8	571.3	645.9	203.0	45.8%
TDC	350.2	405.6	503.2	657.4	307.2	87.7%
ProMutual	342.7	378.5	418.0	504.7	162.0	47.3%
Norcal	246.0	309.1	336.7	398.9	152.9	62.2%
MedAssurance	238.7	276.9	328.7	429.1	190.4	79.8%
ProNational	187.9	241.8	320.2	231.7	43.8	23.3%
ISMIE	201.7	212.5	235.9	293.9	92.2	45.7%
AP Capital	113.3	200.1	225.7	233.8	120.5	106.4%
MAG Mutual	177.2	194.9	215.5	251.1	73.9	41.7%
State Volunteer	155.9	167.9	184.3	217.4	61.5	39.4%
FPIC	118.9	145.4	172.9	200.4	81.5	68.5%
<b>Totals</b>	<b>3,201.9</b>	<b>3,811.3</b>	<b>4,312.7</b>	<b>4,586.2</b>	<b>1,384.3</b>	<b>43.2%</b>

Table 5 makes clear that three carriers increased their surplus by at least 75% between 2003 and 2006, led by Medical Assurance, which more than doubled its surplus.

Chart 6 graphically sets forth the increase in the surpluses of the 12 leading monoline malpractice carriers:

**Chart 6**  
**Surplus of 12 Leading Monoline Malpractice**  
**Carriers, 2003-2006**

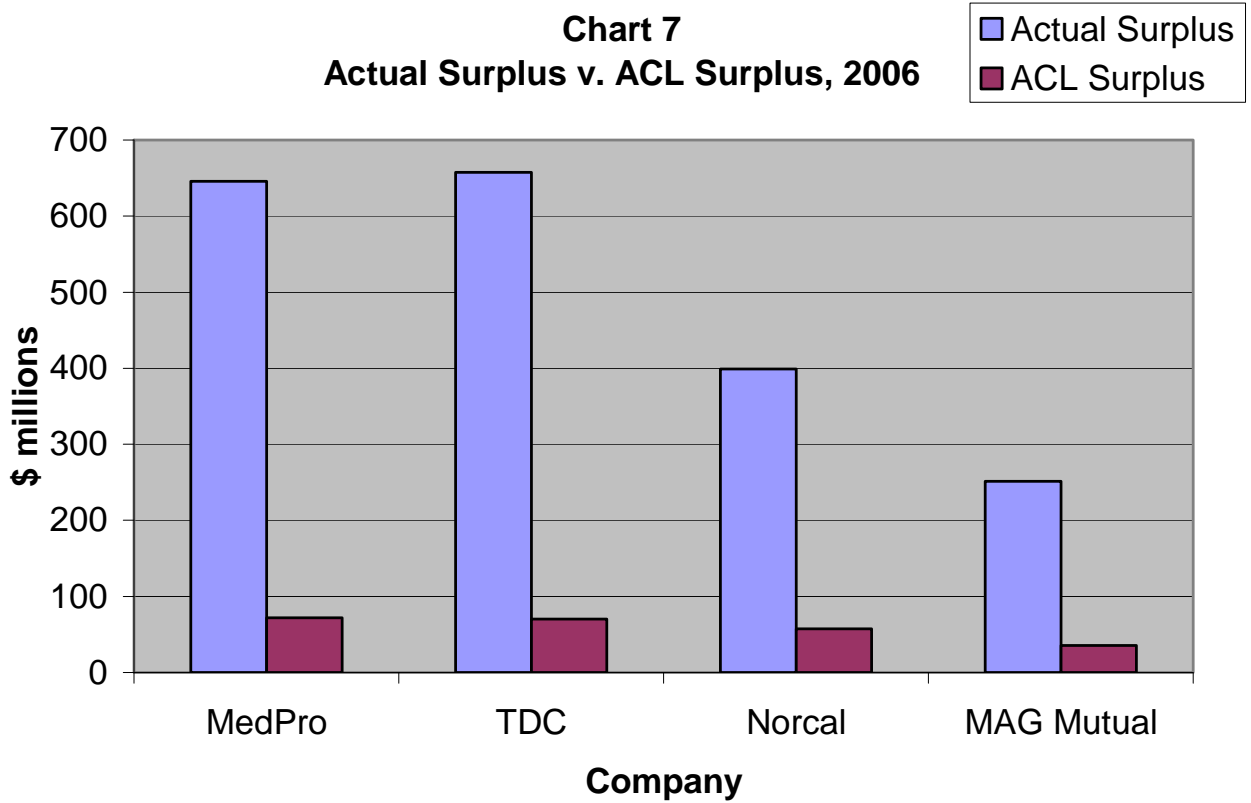


The extent to which the surpluses of these carriers exceed the minimum surplus the NAIC requires them to hold has also risen dramatically. The NAIC has adopted a formula that calculates a minimum level of surplus, called the authorized control level, or “ACL,” for each insurer, based on the risk assumed by the insurer and the quality of the assets it holds. Under state law, the commissioner is authorized to put an insurer into rehabilitation if it has less than the ACL level of surplus. If the carrier has surplus of less than 200% of the ACL level, it must file a plan with the commissioner describing how it will attain 200% of ACL. The NAIC does not require insurers to have surplus exceeding 200% of ACL. Table 6 reveals, however, that each of the leading malpractice carriers has a surplus that far exceeds 200% of ACL.

**Table 6**  
**Actual Surplus v. ACL Surplus, 12 Leading Monoline Malpractice Carriers, 2006**

<b>Company</b>	<b>Actual Surplus (in \$millions)</b>	<b>ACL Surplus (in \$millions)</b>	<b>Ratio of Actual Surplus to ACL Surplus</b>
HCI	521.9	173.5	<b>300.8%</b>
Med Pro	645.9	72.0	<b>897.0%</b>
TDC	657.4	70.3	<b>935.2%</b>
Norcal	398.9	57.6	<b>692.6%</b>
Med Assurance	429.1	69.9	<b>613.8%</b>
Pro National	231.7	60.2	<b>385.2%</b>
AP Capital	233.8	46.1	<b>507.8%</b>
MAG Mutual	251.1	35.4	<b>709.4%</b>
ISMIE	293.9	63.7	<b>461.8%</b>
FPIC	200.4	30.4	<b>659.2%</b>
State Volunteer	217.4	35.3	<b>616.8%</b>
<u>Pro Mutual</u>	<u>504.7</u>	<u>151.6</u>	<u><b>333.0%</b></u>
<b>Totals:</b>	<b>4,586.2</b>	<b>866.0</b>	<b>530.0%</b>

Chart 7 sets forth the actual surplus and ACL surplus of the four carriers whose actual surplus exceeds their ACL surplus to the greatest extent.



While the NAIC has not established a maximum level of surplus for each insurer, there is necessarily some level above which the accumulation of additional surplus serves no legitimate policyholder-related purpose. This is particularly true with respect to carriers who have routinely over-reserved—set aside more money to pay claims than actually proves to be necessary to pay those claims—as most malpractice carriers have in recent years.

## **V. Dividends analysis**

While both the profitability and surplus of the leading carriers have increased sharply since 2003, most of those carriers issued no dividends to policyholders in any of the last four years, as the following table indicates.

**Table 7**  
**Dividends Issued to Policyholders by 12 Leading Monoline Malpractice Carriers,**  
**2003-2006**  
**(in \$millions)**

	<b>2003</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>
Pro Mutual	1.7	1.4	3.2	1.9
State Volunteer	-	-	-	-
FPIC	-	-	-	-
Pro National	-	-	-	-
MAG Mutual	-	-	-	-
TDC	-	-	-	21.0
ISMIE	-	-	-	-
AP Capital	0.4	-	-	-
Norcal	-6.8	0.0	12.0	11.7
Med Assur.	-	-	-	-
HCI	-	-	-	-

The failure of mutual insurance companies with very high profits and very large surpluses to issue dividends to their policyholders is particularly noteworthy. Unlike stock companies, mutual insurance companies are owned by their policyholders; unlike the directors of stock companies, who must act in the best interests of their stockholders, directors of mutual insurers must act in the best interests of their policyholders. The failure of State Volunteer Mutual, MAG Mutual, and ISMIE Mutual to issue any dividend to policyholders in any of the last four years notwithstanding their sharply increased profits and surplus is thus particularly difficult to justify.

## **VI. Conclusion**

As Tables 3 and 4 indicate, after more than doubling in five years the premium volume of the 15 leading carriers has leveled off over the last two years. Specifically, after increasing by 134%--from \$2.260 billion to \$5.298 billion--between 2000 and 2004, gross premiums written declined by 4.9%, to \$5.040 billion, between 2004 and 2006. On a net basis, the \$4.300 billion in premium these 15 carriers wrote in 2006 was 1.6% higher than the \$4.233 they wrote in 2004 before accounting for inflation; after accounting for inflation, net premium volume declined between 2004-2006. Since premium volume reflects changes in the number of doctors insured as well as rate changes, there is not a one-to-one correlation between rates and premiums. Nevertheless, the decline in premium volume is a sign that rates are beginning to decrease. Rates can reasonably be expected to continue to decline--just as they did after the substantial rate increases of the mid-1980's--given the declining claims payments, record low loss ratios, record high surpluses and record profits of the major malpractice carriers.