

Bracing for change

Medical professional liability (MPL) insurance costs at a crossroads

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Agenda

- Intro and current trends
 - Insurance rate trends
 - Challenges to state reforms
 - Increased healthcare utilization
- Healthcare reform law
 - PCORI
 - Federal funding for state tort reform alternatives
 - Consolidation within healthcare system

Intro and current trends

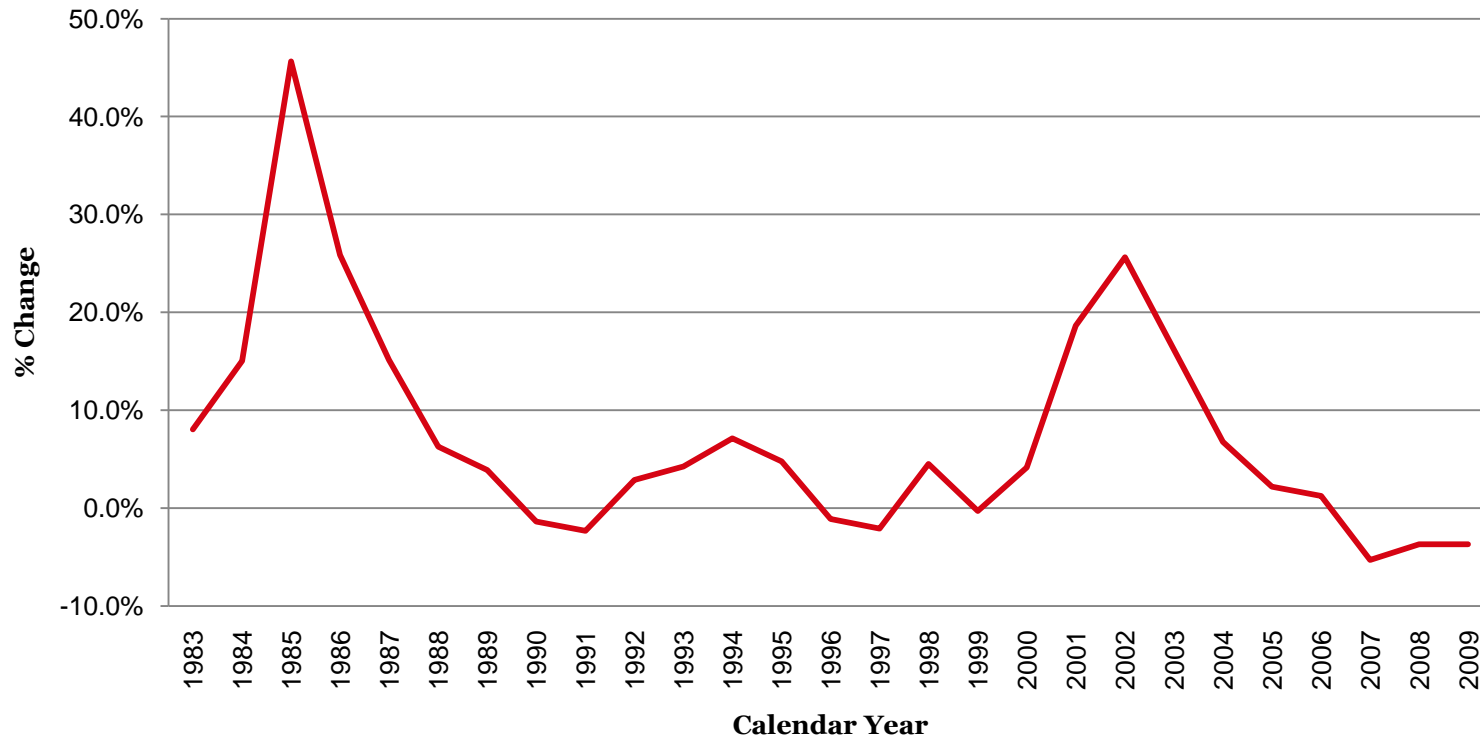
Costs are likely to increase in the near-term

- General inflationary pressures
- Recent trends in MPL insurance costs
- Successful challenges to MPL tort reform at state level
- Increased healthcare utilization

MPL insurance costs cycle

Pattern of crisis or near crisis followed by relative calm since the 1970s

Medical Malpractice Direct Written Premiums Annual Percentage Change

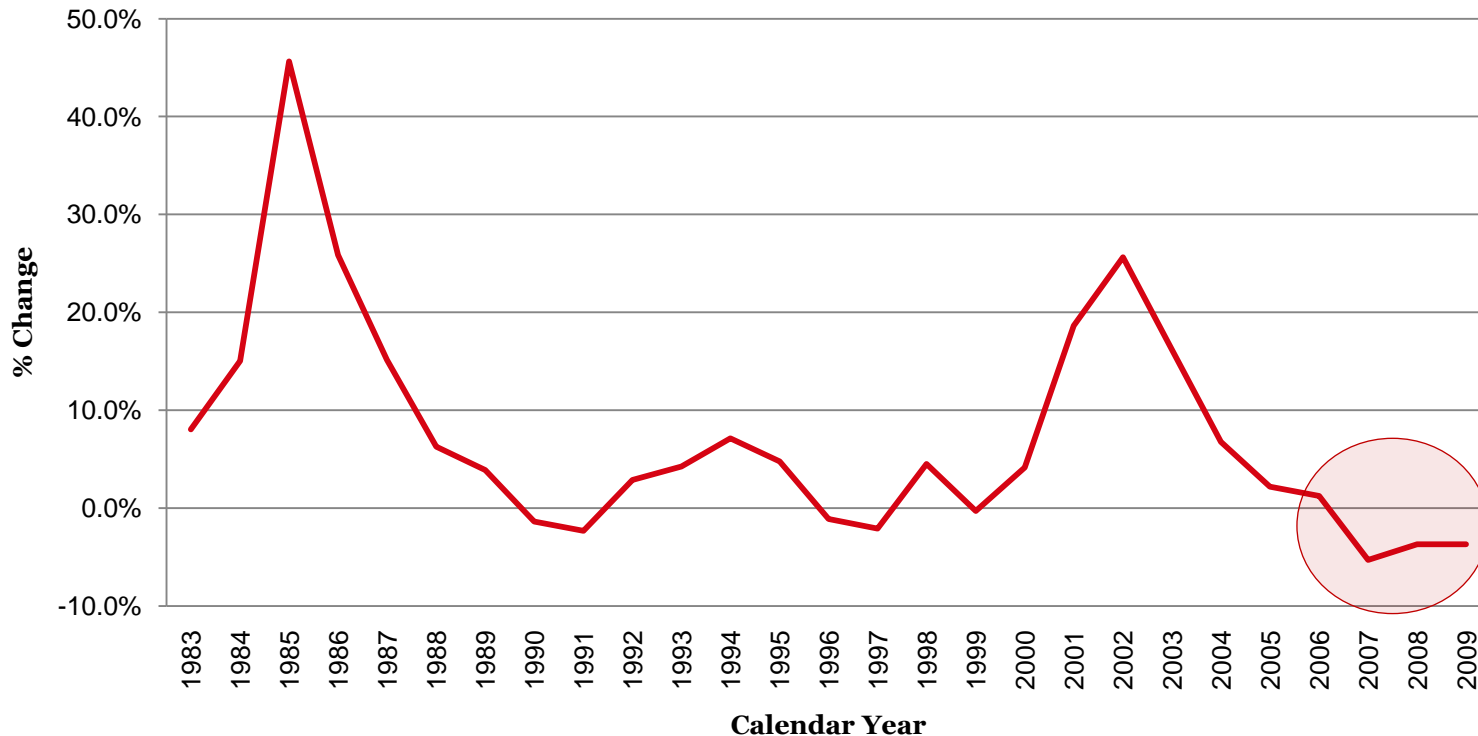


Source: 1983-1993 - A.M. Best Aggregates & Averages, 2003 P/C edition; 1994-2005 - Information included in statutory filings as collected by Highline data; 2006-2009 - SNL Financial.

MPL insurance costs cycle

Costs have remained relatively stable over last five years

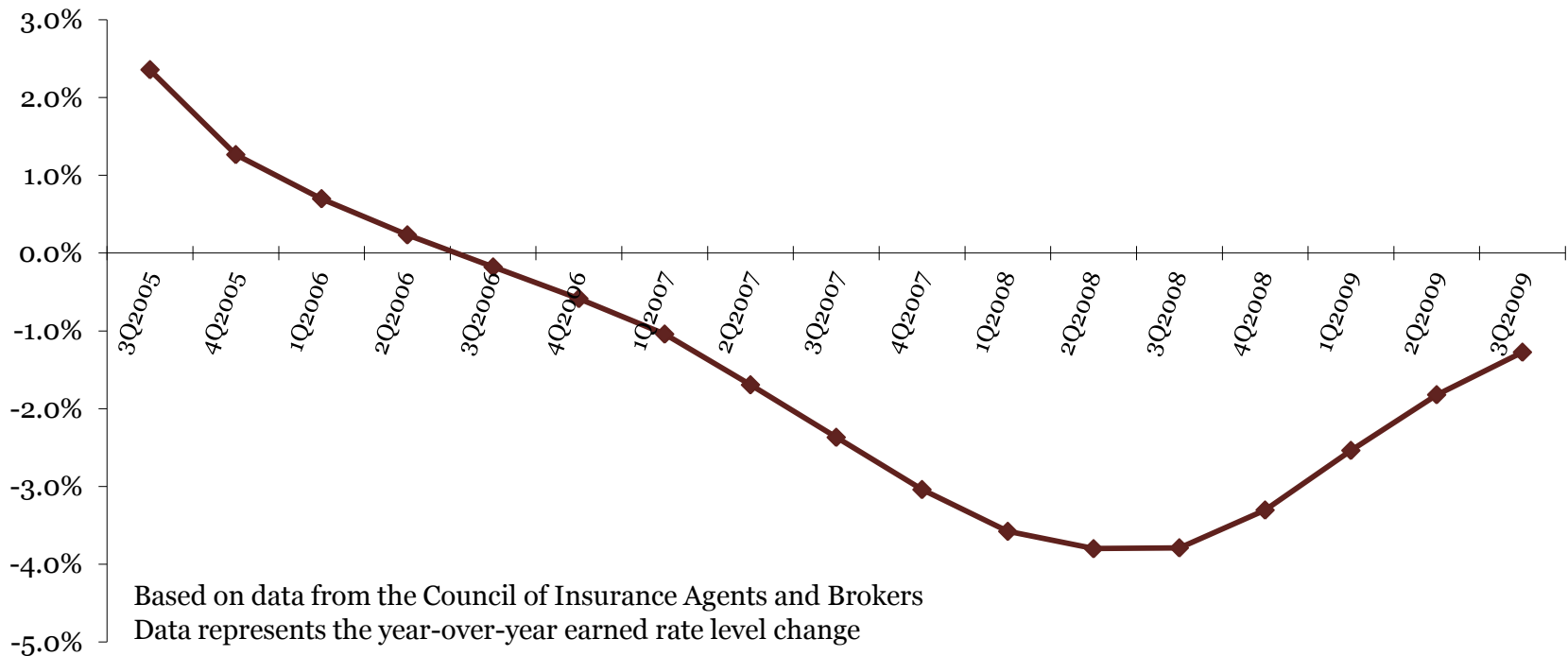
Medical Malpractice Direct Written Premiums Annual Percentage Change



Source: 1983-1993 - A.M. Best Aggregates & Averages, 2003 P/C edition; 1994-2005 - Information included in statutory filings as collected by Highline data; 2006-2009 - SNL Financial.

MPL insurance rate trends

Commercial medical malpractice insurance rate level change



Relevant for healthcare payers and insurers, but also useful as proxy for trends in self insurance costs

MPL insurance rate trends

- MPL rates peaked in early 2006 and have continued to drop since then
- Steady decline in average price of commercial MPL insurance from 2006 through 2009
- Current rates may prove to be unprofitable for some insurers
- Decrease in premium rates partially driven by state MPL tort reforms, affecting both claim frequency and claim severity

MPL insurance rate trends

- Claim frequency
 - Bottomed out?
 - Decreased to a low point in 2006
 - Has steadily increased since 2006
- Claim severity
 - Has continued to increase over the last several years due to general inflationary pressures
 - Medical cost inflation continues to exceed general inflation

MPL tort reforms

Examples include:

- Caps on damages
 - Non-economic (e.g. pain and suffering)
 - Economic (actual monetary loss due to negligence)
- Shortened period for statutes of limitation
- Limitation of attorney fees
- Expert witness standards improving claims defense

Have helped control MPL insurance cost inflation and have led to lower insurance and self insurance costs

MPL tort reforms

- Approximately 30 states limit damages in MPL cases through statute
- Approximately 20 of these states specifically limit non-economic damages
- Recent challenges in several states
 - 7 states have already overturned previous caps on non-economic damages
 - Most recent challenges in Georgia (March 2010) and Illinois (February 2010)

Continued repeal of state tort reforms will accelerate increase in insurance and self insurance costs beyond normal inflationary and market trends

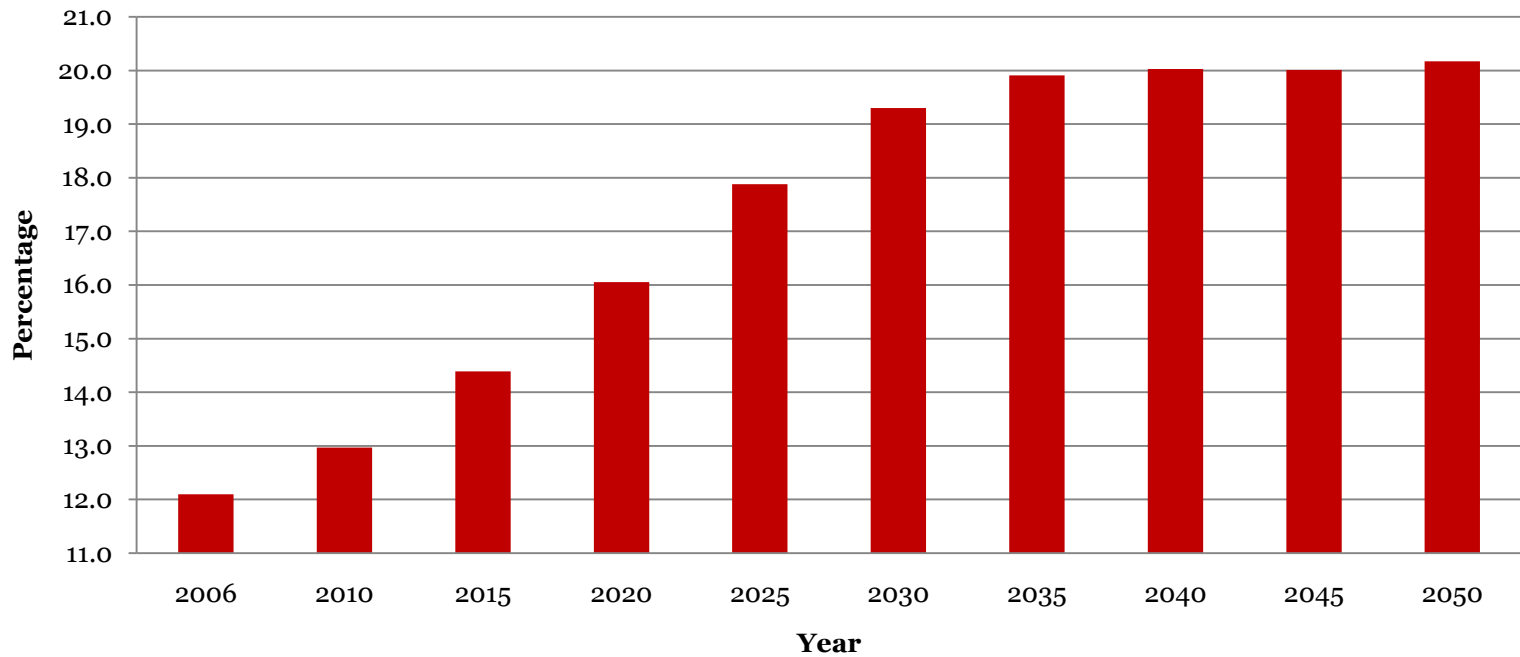
Increased healthcare utilization

“Baby boomers”

- Born between 1946 and 1964
- First baby boomers just starting to reach retirement age
- Beginning to access healthcare through Medicare
- Baby boomers’ demand for healthcare services will increase as they age
- Will contribute to increase in healthcare utilization

Increased healthcare utilization

**Percent Distribution of Population
65 Years and Older**



Source: Population Division, U.S. Census Bureau
2006 - 2009 actual figures; 2010 and subsequent projections

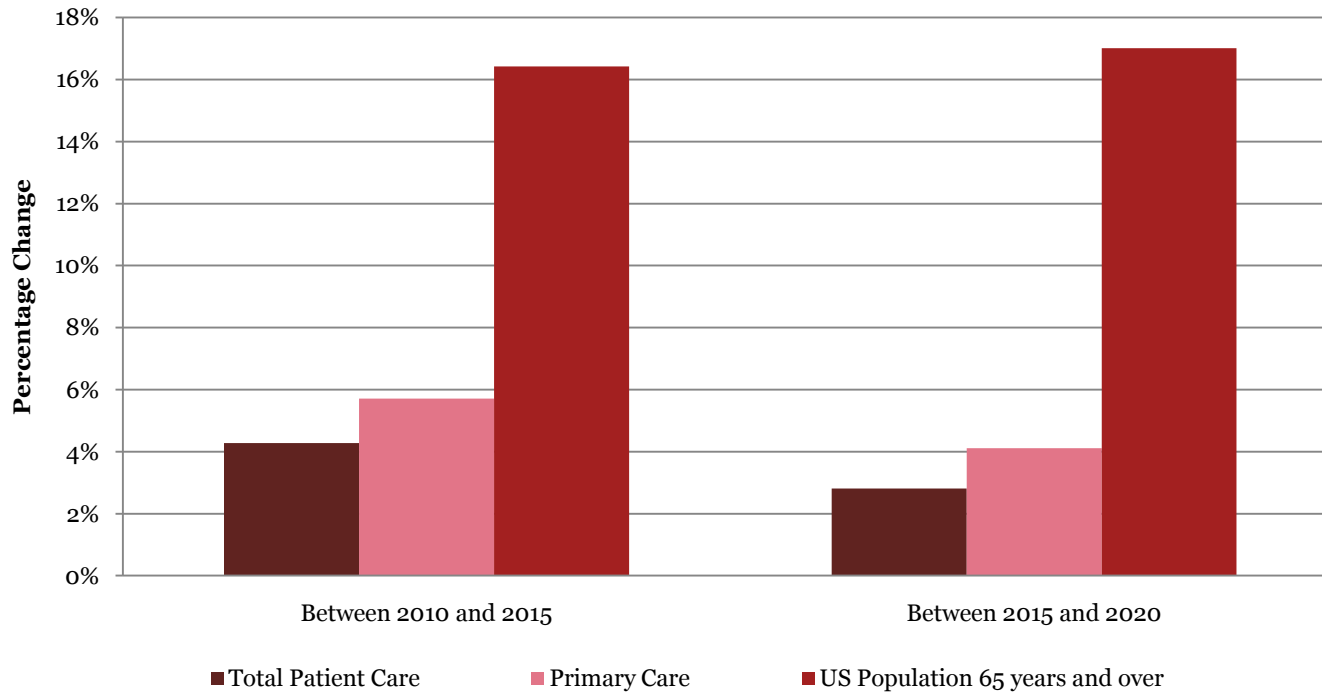
Increased healthcare utilization

Patient Protection and Affordability Care Act and the Healthcare and Education Reconciliation Act of 2010 (“healthcare reform law”)

- Expansion of Medicaid eligibility
- Requirements for healthcare insurance coverage for all Americans (including those with pre-existing conditions)
- Will contribute to increase in healthcare utilization

Increased healthcare utilization

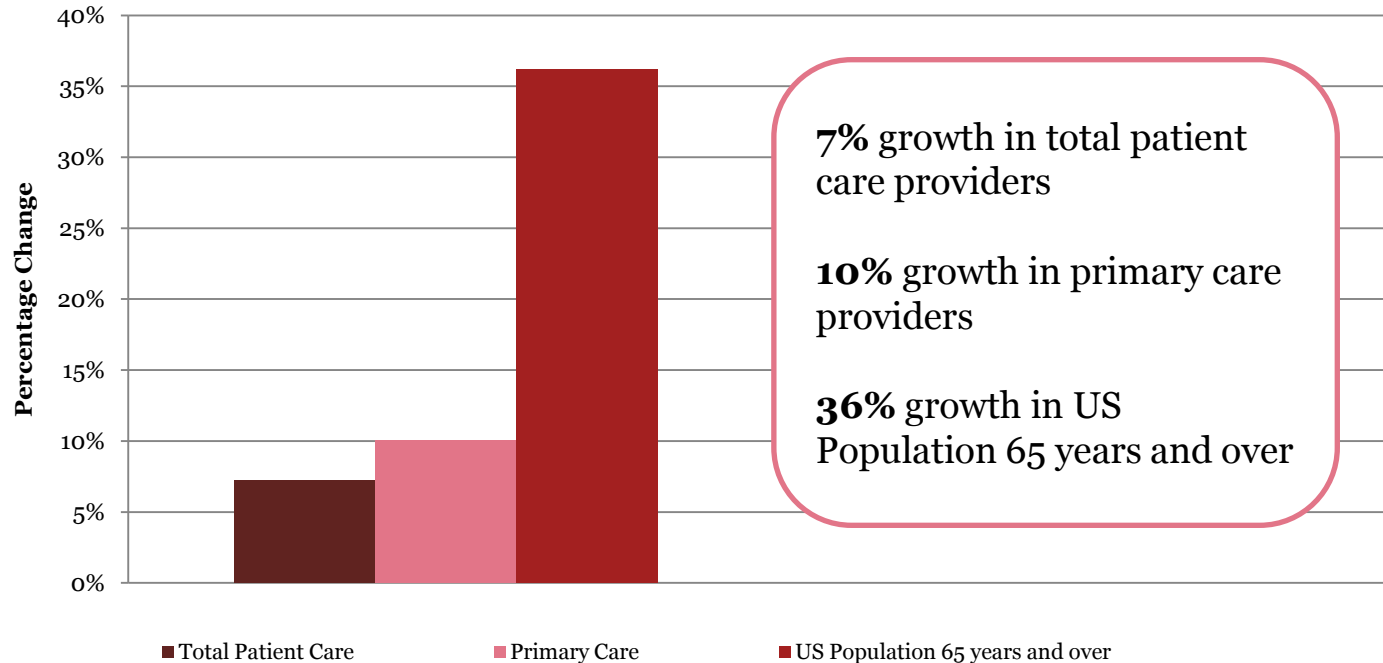
Comparison of Growth in Patient and Primary Care to Aging Population



Source: Population Division, U.S. Census Bureau
Physician Supply and Demand: Projections to 2020. U.S. Department of Health and Human Services.

Increased healthcare utilization

Comparison of Growth in Patient and Primary Care to Aging Population *Cumulative Growth Between 2010 and 2020*



Source: Population Division, U.S. Census Bureau
Physician Supply and Demand: Projections to 2020. U.S. Department of Health and Human Services.

Increased healthcare utilization

Increased demand for services without commensurate increases in healthcare professionals could lead to

- More medical errors and misdiagnoses
- Delays in diagnoses
- Longer wait times to see primary care physicians

...all leading to an increase in the number of MPL lawsuits and corresponding increase in insurance rates and self insurance costs

Healthcare reform law

Patient Protection and Affordability Care Act and the Healthcare and Education Reconciliation Act of 2010 (“healthcare reform law”)

Several components of the law could have an indirect impact on MPL insurance costs:

- Establishment of Patient-Centered Outcomes Research Institute (PCORI)
- Federal funding for state tort reform alternatives
- Cost control pressures spurring more providers to consolidate

Patient-Centered Outcomes Research Institute (PCORI)

- Established by the healthcare reform law to improve availability of unbiased, quality research
- A private, non-profit entity
- Not an agency or establishment of the US government
- Over time expected to provide doctors with better research, which could result in
 - better patient care
 - quicker positive outcomes
 - lower incidence of MPL lawsuits

Patient-Centered Outcomes Research Institute (PCORI)

Impact of PCORI on liability costs uncertain

- Could provide doctors with clearer guidance on outcomes of various treatments, giving them a defensible position in the event of a lawsuit
- Could increase the risk of liability for some doctors if PCORI research suggests that an alternative treatment is preferable to treatment selected by the doctor
- Could increase the incidence of medical errors (or omissions of treatment) if doctors limit treatments based on PCORI research

Funding for state tort reform alternatives

- Most direct effect of the healthcare reform law on MPL
- \$50 million in federal grants to states for “demonstration projects”
- Exploring cost containment alternatives to tort reform litigation system

Funding for state tort reform alternatives

Might include the following types of programs:

- Health Courts
- Early Offers
- Apology Programs
- Medical Review Panels
- No-fault system

Could have a beneficial impact on MPL insurance costs and overall healthcare costs

Consolidation within the healthcare system

Cost control pressures spurring more providers to consolidate

- Strong incentives in recent years to control costs
- Difficult for individual and small group physician practices and community-based hospitals to continue operating independently
- Since early 2010, have seen numerous consolidations within the healthcare system
- Healthcare reform law increases pressures on healthcare providers to control cost, providing more incentive to consolidate

Consolidation within the healthcare system

Consequences of increased consolidation

- Consolidated systems may be more inclined to retain risk than smaller systems or individual physicians
 - *Increase self insured retentions or deductibles*
- Liability insurers likely to see continued reduction in first dollar coverage
 - *Revise underwriting guidelines to ensure collecting adequate premiums from healthcare providers that continue to purchase first dollar coverage*

Recent developments and uncertainties

- Changes for Congress with recent elections
- Uncertain how or if future congressional action will impact healthcare reform law
- Many states have filed lawsuits challenging the constitutionality of healthcare reform law

Regardless, healthcare providers, liability insurers and medical professionals should think about the issues now so that they are prepared for changes when they occur

PwC recommendations for healthcare providers

- Plan for likely MPL insurance cost increases over next few years
- Seek opportunities to partner with other healthcare providers to self insure larger portions of risk
- Review current risk management programs and practices to determine if current legislation or cost drivers warrant a change in the focus of these programs
- Develop a strategy to remain vigilant on emerging issues in MPL

PwC recommendations for MPL insurance companies

- Plan for a reduction in primary, or first dollar, insurance coverage
- Revisit underwriting, ratemaking and business strategies to ensure the collection of adequate premium for remaining coverage written

John Gibson

John has thirty-one years of experience as a P&C actuary and is a principal of the US P&C actuarial practice of PwC. John's insurance and reinsurance company experience includes loss and loss expense reserving, pricing and risk transfer analysis for automobile liability, general liability, medical professional liability, personal lines, workers' compensation and mortgage guaranty insurance. John has also performed numerous evaluations of self-insurance programs for large corporations, associations, hospitals, and municipalities and has extensive experience performing reserve reviews and special projects for healthcare entities.

Dorothy Woodrum

Dorothy has nine years of experience as a P&C actuary and is a director of the US P&C actuarial practice of PwC. Dorothy's experience includes loss and loss expense reserve analyses for large commercial programs, associations and hospital programs with retained risks as well as insurance companies, reinsurance companies and captive insurance companies. Her reserving work has included professional liability, medical professional liability, workers' compensation, general liability, auto liability and mortgage guaranty insurance. Dorothy has provided actuarial services to numerous healthcare clients.

