



The Impact of Health Care Reform on the Medical Professional Liability Market

Presented by

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Overview of Recent Trends

- ◆ Profitability Has Been Outstanding ... and Unsustainable

How Will Health Care Reform Affect Medical Professional Insurers?

- ◆ The Impact of Health Care Reform on Loss Exposure
- ◆ Growth Opportunities Shift Under Reform Initiatives

Recommendations for Company Outperformance

- ◆ New Risk Management Focus
- ◆ Conclusions and Outlook

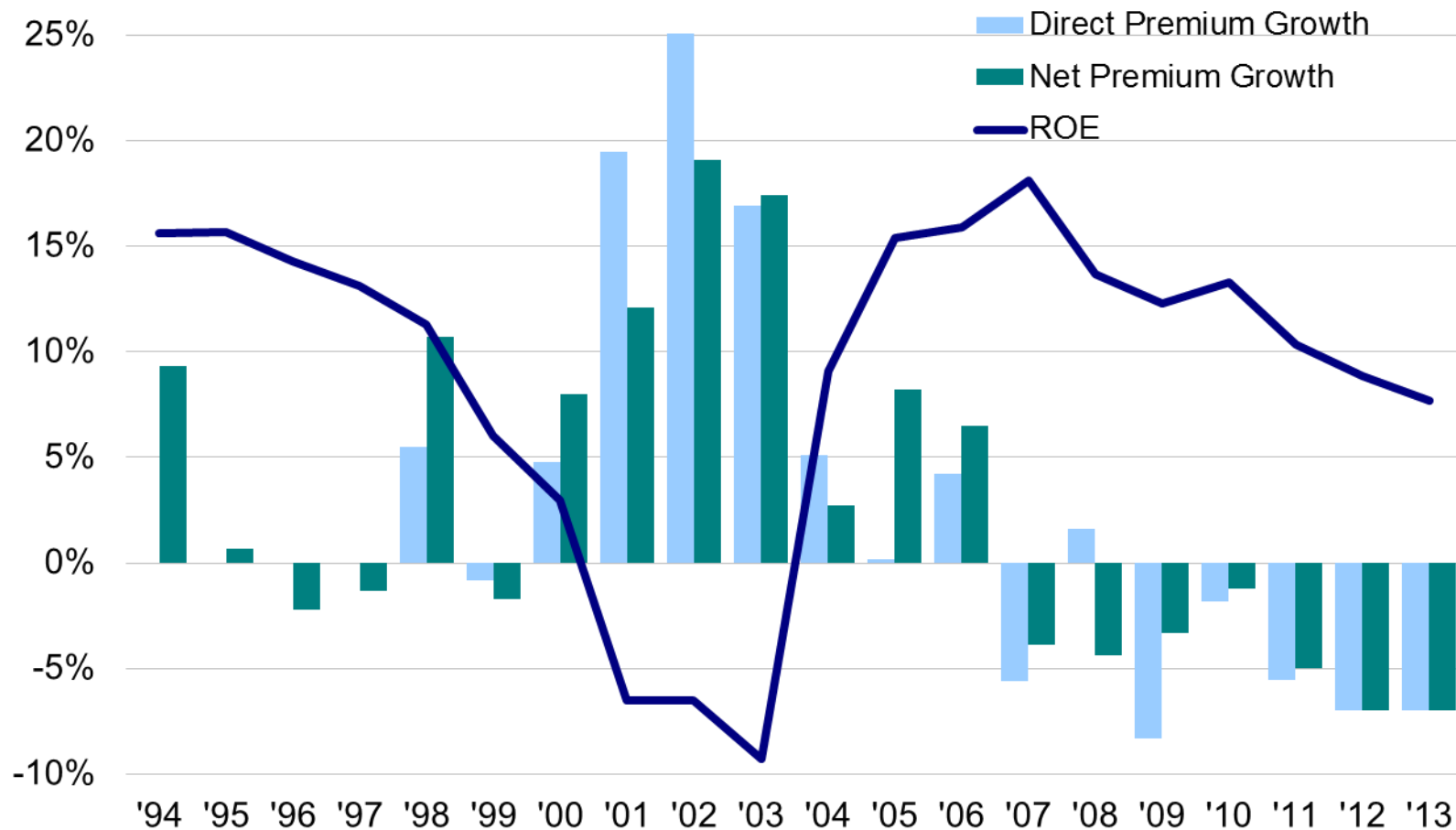
Historical Results and Conning Forecasts

Year	Net Premiums Written	Loss/LAE Ratio	Expense Ratio	Combined Ratio
2003	\$8,753	121.8%	17.0%	139.1%
2004	8,991	93.4%	15.4%	109.2%
2005	9,730	82.8%	17.3%	100.6%
2006	10,366	71.7%	17.7%	90.6%
2007	9,957	62.9%	19.0%	84.8%
2008	9,521	57.4%	19.3%	79.2%
2009	9,206	61.7%	21.3%	85.5%
2010	9,092	57.4%	23.9%	84.8%
2011F	8,638	63.0%	24.0%	90.0%
2012F	8,033	68.0%	24.5%	94.5%
2013F	7,471	73.5%	24.5%	100.0%

(\$ in millions)

Source: Conning Property-Casualty Forecast & Analysis By Line of Insurance

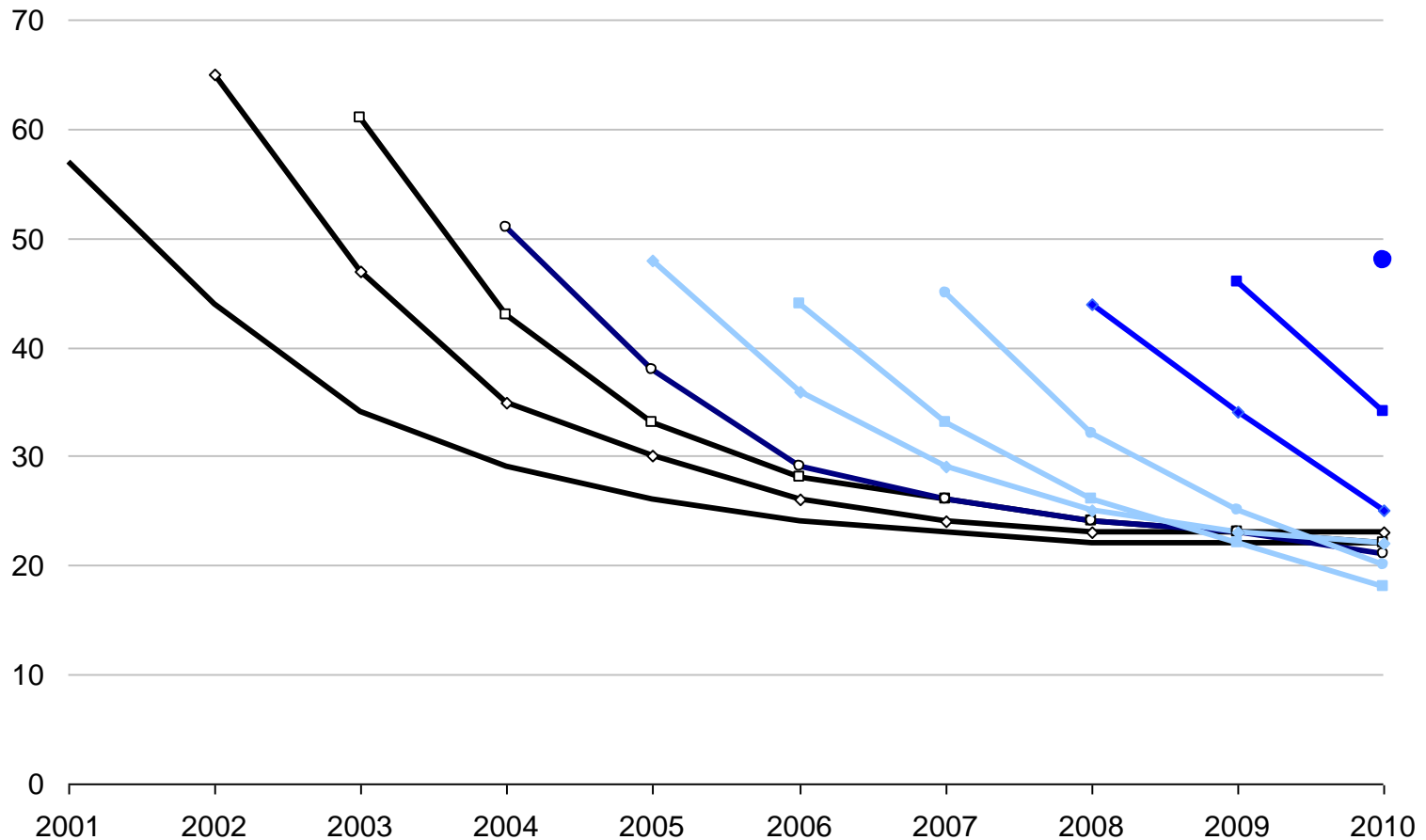
Returns Are Highly Cyclical



Source: Conning Property-Casualty Forecast & Analysis By Line of Insurance

Continued Strong Reserves Based on Successful Defense

Property-Casualty Industry Claim Counts (Outstanding and Closed)
Medical Professional Liability—Claims-Made *(in thousands)*



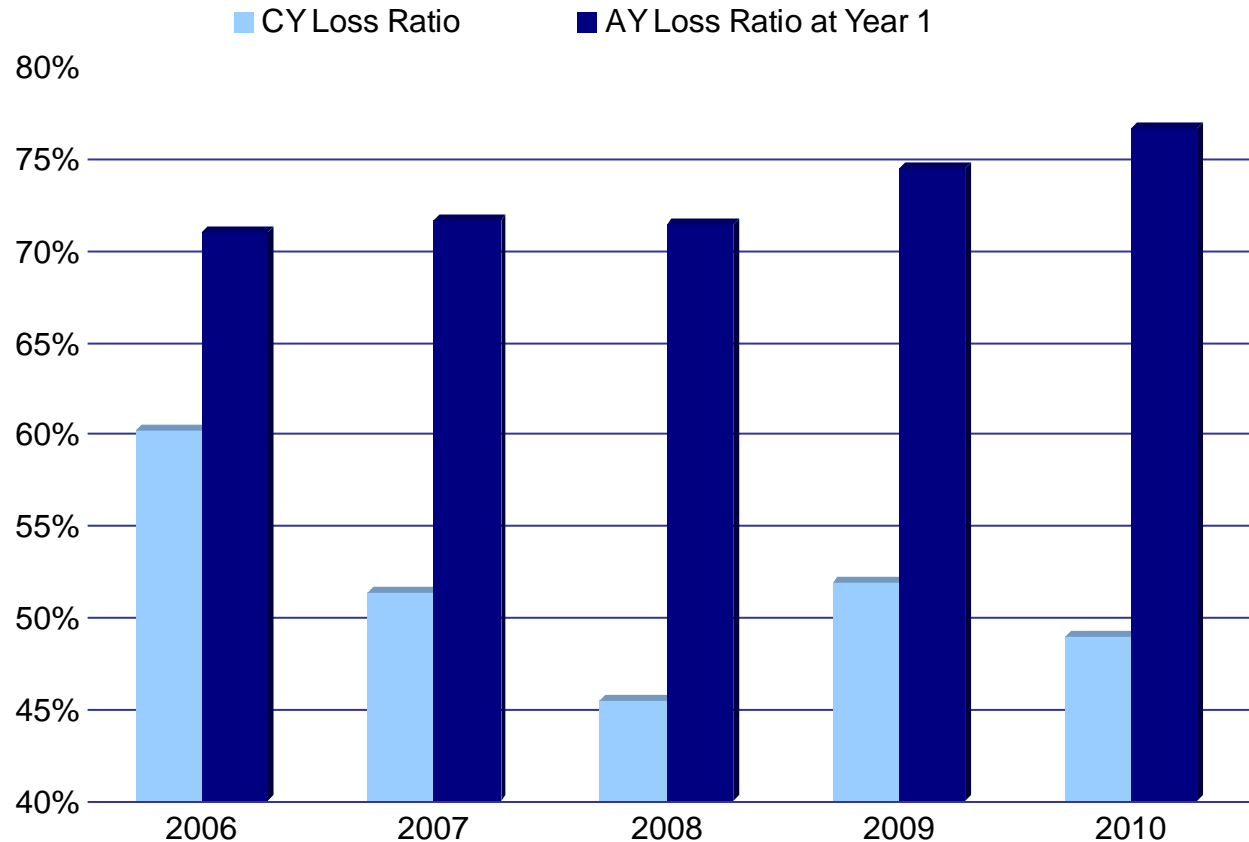
Source: Company statutory filings, Conning Research & Consulting analysis

Medical Professional Liability—Claims-Made

Lower calendar-year loss ratios illustrate the effect of reserve releases from prior years as claims continue to settle better than in past years.

The pricing environment has remained conservative in light of the improving claim settlement experience.

Differences Between Calendar- and Accident-Year Assumptions



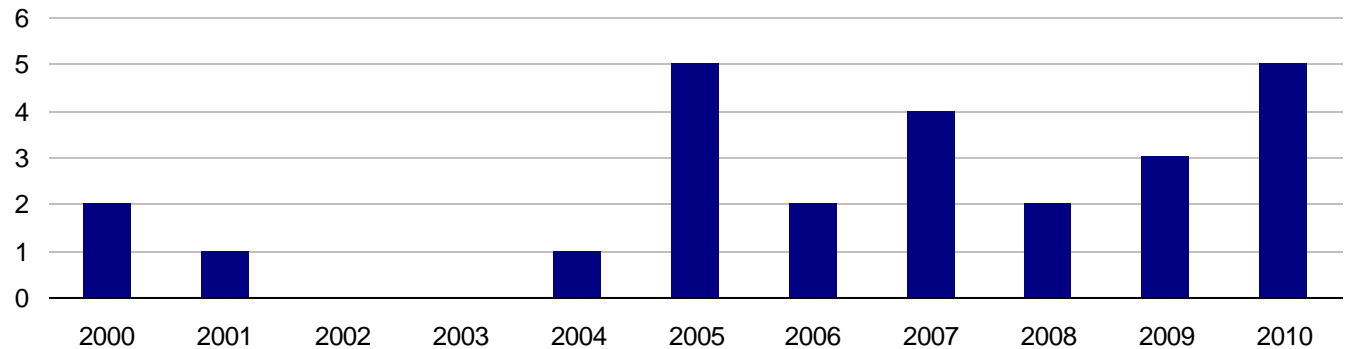
Source: Company statutory filings, Conning Research & Consulting analysis

Past Drivers of Positive Results Are Largely Behind

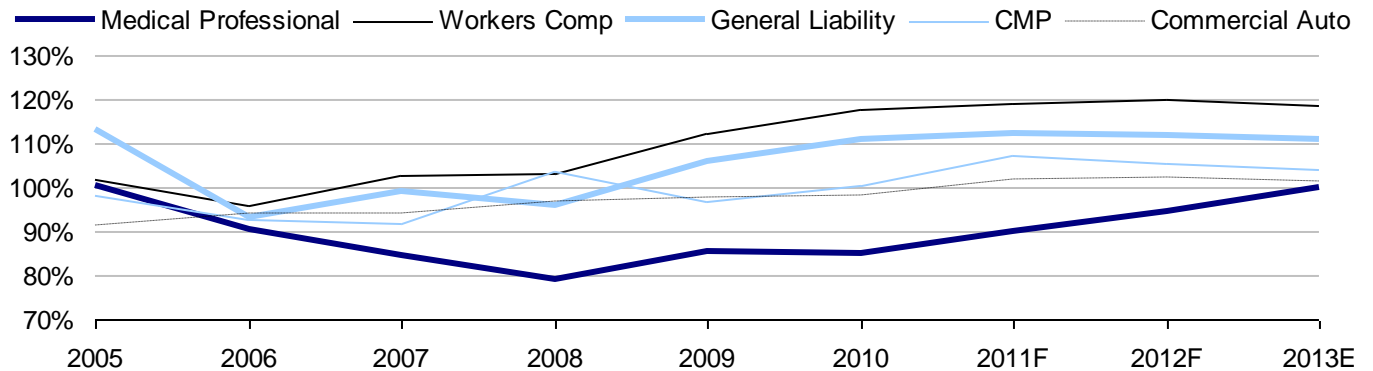
- ◆ Positive state tort reform over the past decade
- ◆ Higher earned premium (growing 10% per year from 2000 to 2006)
- ◆ The use of doctor-directed risk mitigation practices
- ◆ Better claims defense with expert witnesses

Competitive Environment Heats Up

M&A Transactions Affecting Medical Professional Insurance



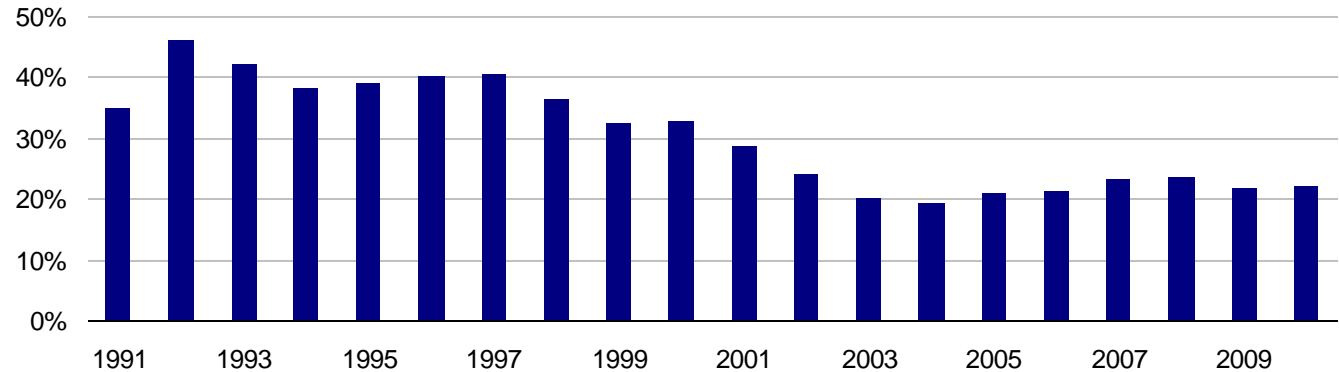
Historical and Forecast Combined Ratios by Line



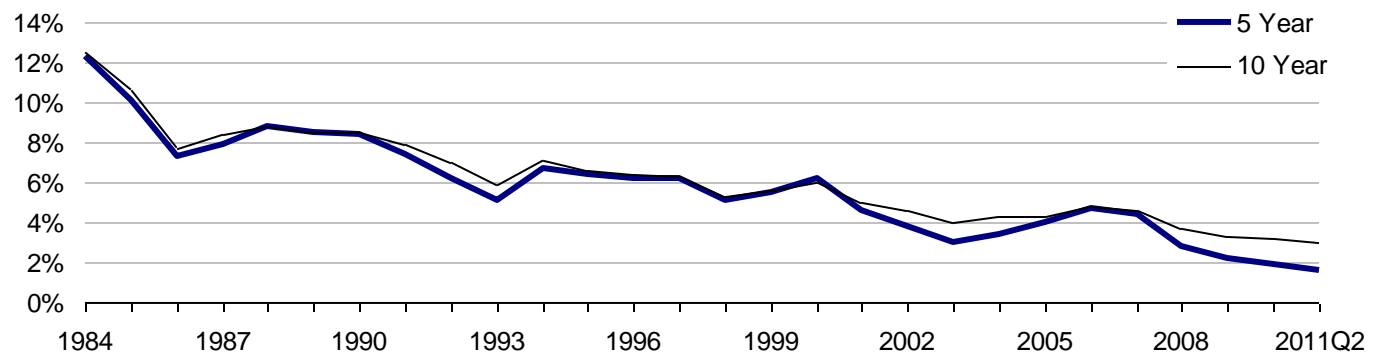
Sources: Council of Insurance Agents & Brokers, Conning proprietary database, Conning *Property-Casualty Forecast & Analysis by Line of Insurance*

Challenging Investment Income Environment

Medical Professional Liability Net Investment Income as a % of Premium



Market Yield on U.S. Treasury Securities



Source: U.S. Treasury, Conning *Property-Casualty Forecast & Analysis by Line of Insurance*

Signs of Erosion in Tort Reform

States Reporting Erosion of Tort Reform

Erosion of tort reform laws include:

- extending filing periods to report a claim

- increasing noneconomic damage limits for “special cases”

Challenges to tort reform

Texas

California

Wisconsin

Michigan

Washington

Nevada

Oregon

Missouri

Illinois

Georgia

Maryland

California

Reversals of tort reform measures

Wisconsin

Washington

Oregon

Missouri

Illinois

Georgia

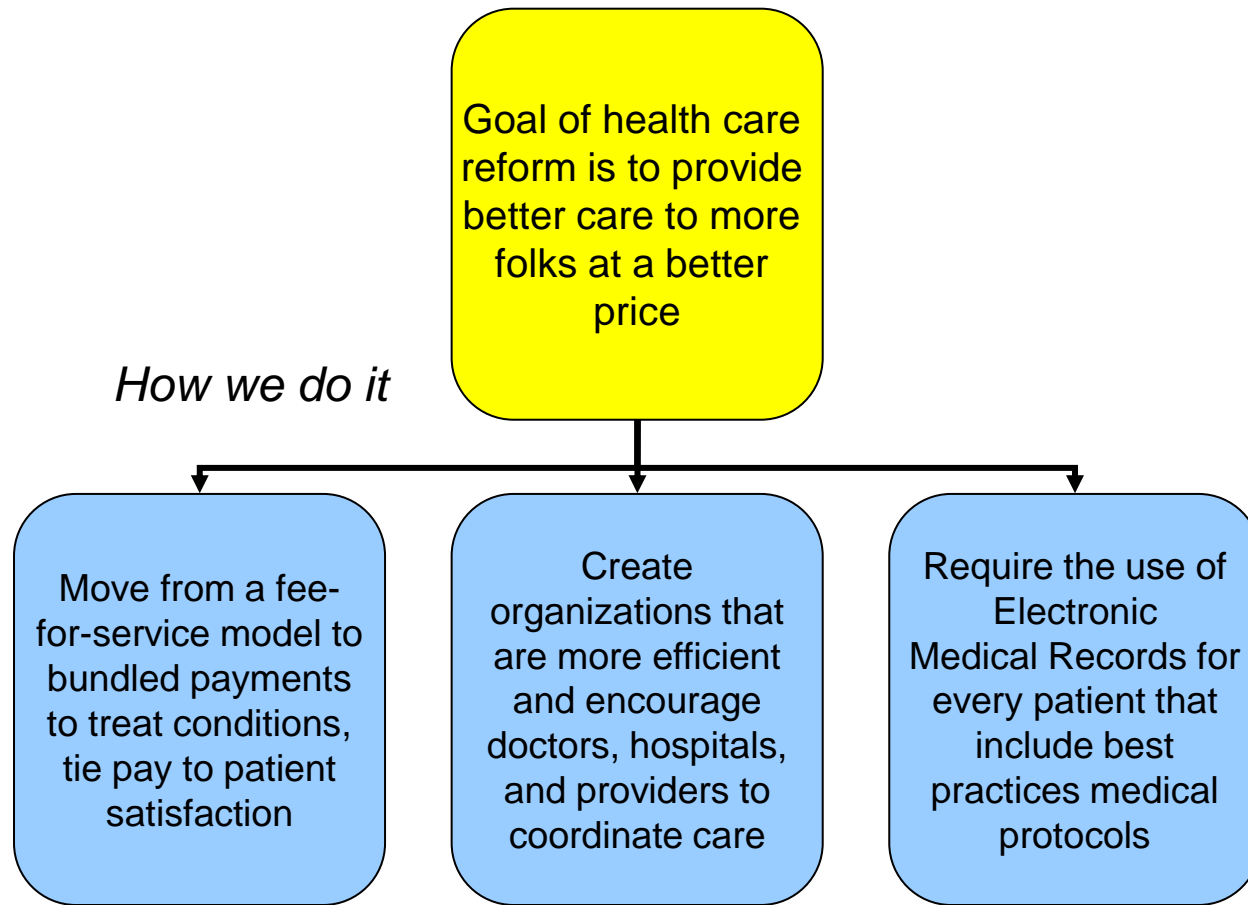
Overturn of noneconomic damage caps

Illinois in 2010

Georgia in 2010

Source: *Business Insurance*, various

Health Care Reform Initiatives—a Snapshot



...and add 32 million to ranks of insured in 2014!!!

Health Care Reform Initiatives Influence Liability Exposure

1. Shifting more care and higher acuity care to nurse practitioners and other mid-level care providers
2. Ease of access to more complete electronic medical records
3. Challenges to and changes in the quality of care

◀ Expanding the Role of Practitioners Under Reform ▶

- ◆ CareFirst BlueCross BlueShield of Maryland announced that it will start letting **nurse practitioners** participate in its health care provider networks as independent primary care providers, **citing growth of insureds under health care reform as the reason**
- ◆ Montana allows **nurse practitioners** to work without any doctor supervision
- ◆ 28 states are debating further loosening of restrictions that prevent **nurse practitioners and physician assistants** from performing more tasks independently

Blurring the Line of Providers

- ◆ Federal funding programs support advanced degrees for nurses
- ◆ National enrollment of **nurse doctorates**—from 70 in 2002 to 5,000 in 2009
- ◆ States push against AMA to allow nurses to use the “Doctor” preface

...An expanded role of mid-level care providers raises exposure

◀ What Is the Standard of Care for Independent Nurses? ▶

Minute Clinics, on its website, holds out that they set “new standards for clinical quality that exceed the national guidelines established for store-based clinics.”

The American Academy of Nurse Practitioners’ website states that “NPs (nurse practitioners) provide health care that is equal to, or superior to that of physicians.”

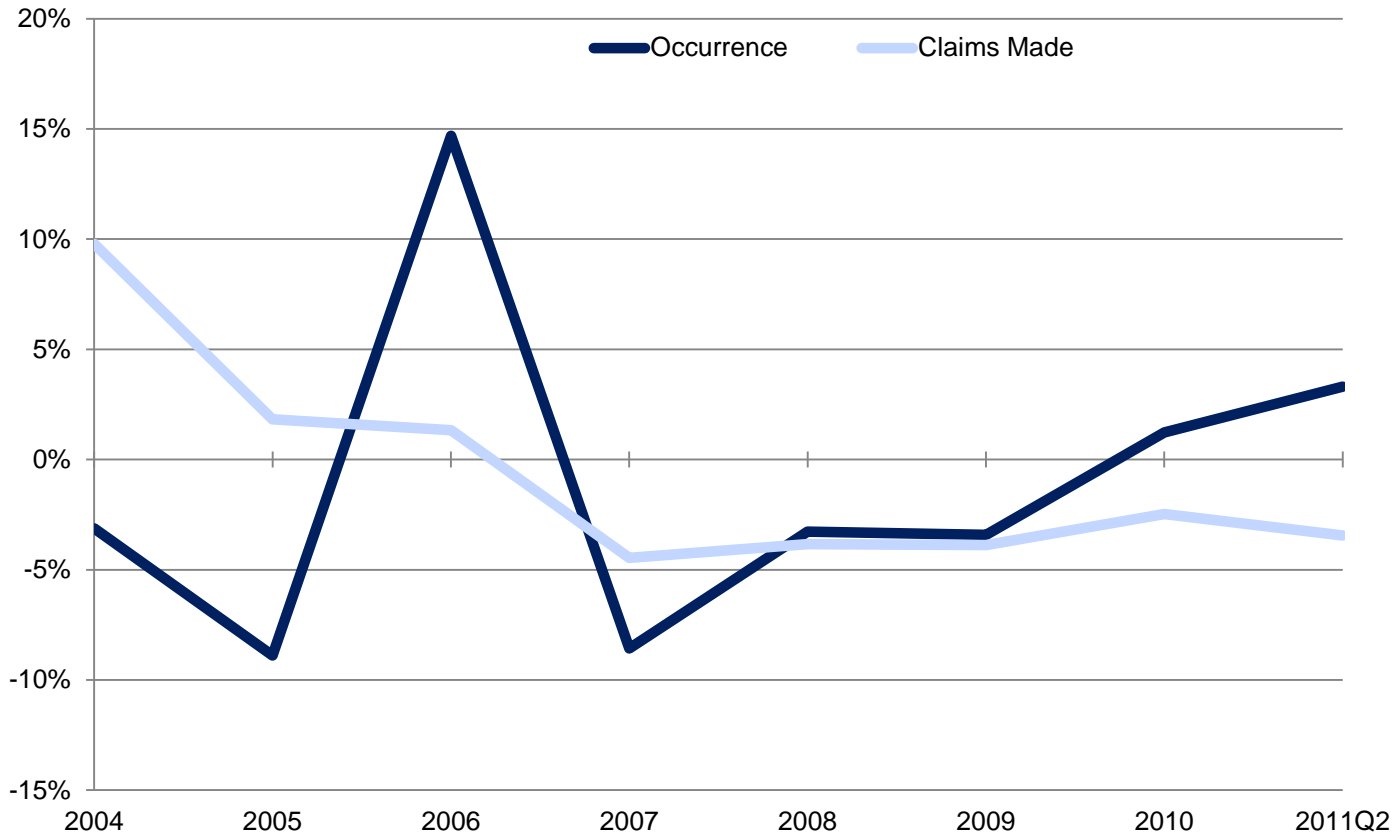
What is standard of care?

The Challenge of Pricing Nurse Practitioners

- ◆ Most policies written on an occurrence form
- ◆ Auditing nurse practitioners is not an easy task
- ◆ Raising rates or changing to a claims-made form in a competitive environment?

MPL Occurrence Outgrowing Claims Made

Medical Professional Liability Change in Direct Premium by Type



Source: Company statutory filings, Conning Research & Consulting analysis

Electronic Medical Records Required

- ◆ Electronic medical records (EMRs) are required for every patient under the new health care reform law
- ◆ An August 2010 American Hospital Association poll of 3,100 members showed that only 12% use EMRs
- ◆ EMRs will use protocols/electronic prompts to ensure best practices
- ◆ EMR's will allow doctors, patients, and nurses to transfer more complete medical records/history quickly and efficiently

Risks of EMRs

- ◆ *What if an electronic medical protocol is ignored by a doctor because he/she thinks it doesn't apply?*
- ◆ **Medical protocols—the standard of care? One size fits all?**
- ◆ Other risks with EMR:
 - ❖ Is redundant testing really redundant?
 - ❖ Time
 - ❖ Input errors
 - ❖ Software errors
 - ❖ Coding errors
 - ❖ AND E-Discovery!

Increased Exposure to E-Discovery from EMRs

- ◆ Lawyers will have greater and easier access to more
- ◆ Two federal organizations now have “blue button” technology on their websites, with the Department of Veteran Affairs offering complete, real-time medical records for its patients
- ◆ Expect plaintiff lawyers to data mine EMR’s & metadata
- ◆ Easier access to claims data is likely to raise claims frequency, defense costs

◀ What Happens to Quality of Care Under Reform? ▶

Does the quality of care decline if...

More nurse practitioners provide higher level care currently in physician domain?

Doctors are financially incented to provide more cost-effective care?

Does the standard of care remain high?

Will it be impacted by new federal reimbursements?

Will it be defined by medical protocols in EMRs?

Is the standard that nurses provide the same as a doctor?

◀ Does Establishing Malpractice Become Easier?

- ◆ If quality of care declines but current higher standards of care remain, does establishing negligence become easier?

The *New York Times* article notes that cancer care in the U.S. costs \$100 billion a year

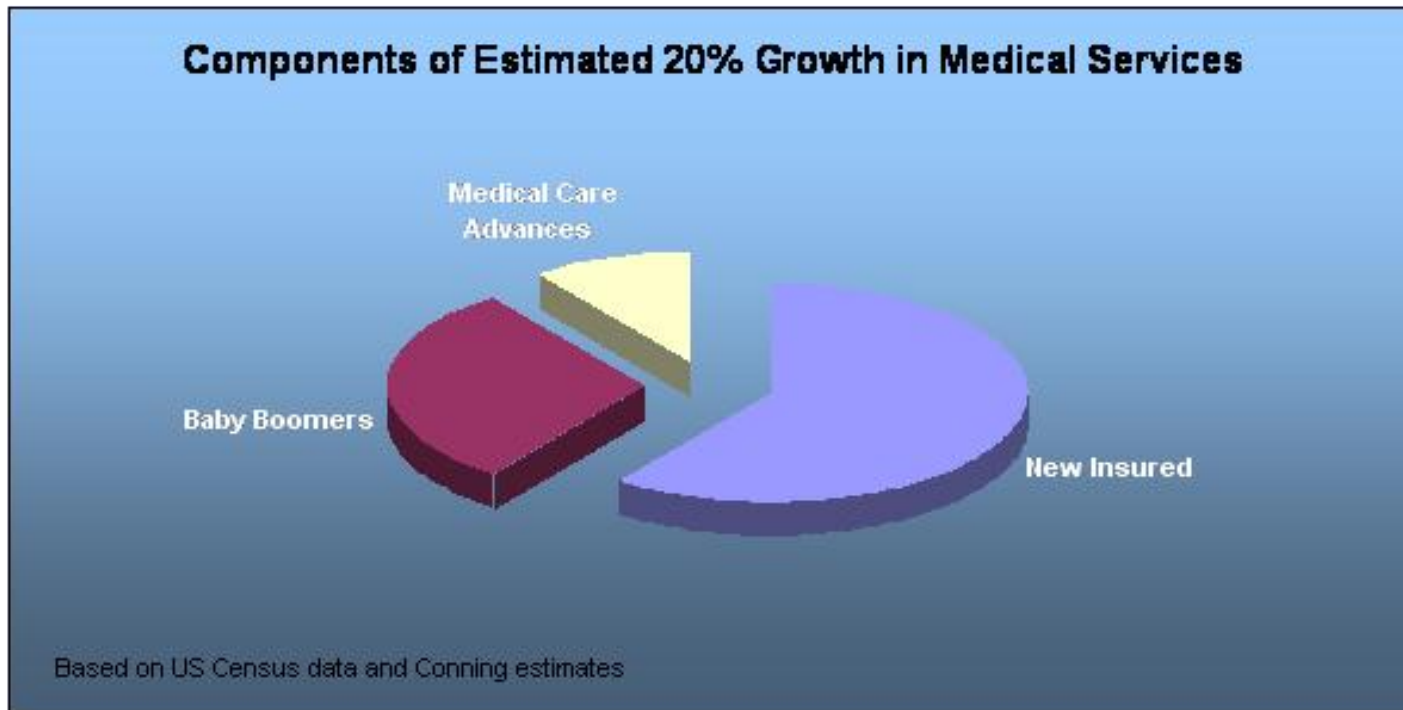
Example: A New York Times article from October of 2010 focuses on how five oncology practices are testing reducing costs for cancer treatments.

*The physicians in the test practices are **motivated by fees that “encourage doctors to follow standard treatments”** rather than opting for individualized and unproven courses of therapy, which can often include expensive drug treatments.”*

OPINION: Legal opinion from risk managers at Stevens & Lee is that, as more doctors, hospitals, and health care organizations are compensated this way under health care reform, medical best practices will shift.

◀ Growth Outlook for Medical Services

We estimate that the overall growth in medical services will likely be near 20% over the next five to ten years.



- ◆ **Accountable Care Organizations: the new delivery of care?**
 - ❖ A concept to managing the whole patient, by providing one primary care physician to oversee the needs of patients within a community of providers. Test models are in the works, focusing initially on coordinated care for chronically ill patients. Within the category of ACOs, the Patient-Centered Medical Home is seen as the most promising delivery model.

- ◆ **Retail Stores, Even Truck Stops, Supplying Clinical Care**
 - ❖ Walk into a CVS and get a physical? Have you been to a CVS MinuteClinic yet? How about Target and Wal-Mart? The Convenient Care Association counts approximately 1,200 retail clinics in 32 states, and the figure is expected to triple by 2015.

- ◆ **The Medical Hotel**
 - ❖ With overcrowding of hospitals in certain markets, there is a growing necessity to serve high-acuity patients for shorter stays. Currently, new medical hotels are being built near targeted hospitals to take some of the burden.

◀ The New Efficient Health Care Models (continued)

◆ Workplace-Based Care

- ❖ Pitney Bowes and Quad Graphics are examples of companies that have set up a limited medical provider network. Some provide coordinated care as an extension to primary doctors; others provide full primary care and coordinate with hospitals and specialists.

◆ Remote Patient Monitoring

- ❖ The Center for Technology and Aging in California cites that better technology and patient interest in staying home is driving a market for remote patient monitoring, allowing for quality care without office visits or outpatient care facilities.

Growth in hospital care (while increasing) will be slower than growth in outpatient and clinical care facilities due to the relative cost benefits of moving lower-acuity care out of hospital and emergency room settings (the Bureau of Labor Statistics)

Growth Opportunities Shift Under Reform Initiatives

- ◆ Exposure is expected to increase as physicians consolidate with larger health care organizations
 - ❖ Increased severity and complexity of enterprise risks
 - ❖ Potential increased exposure with EMR technology

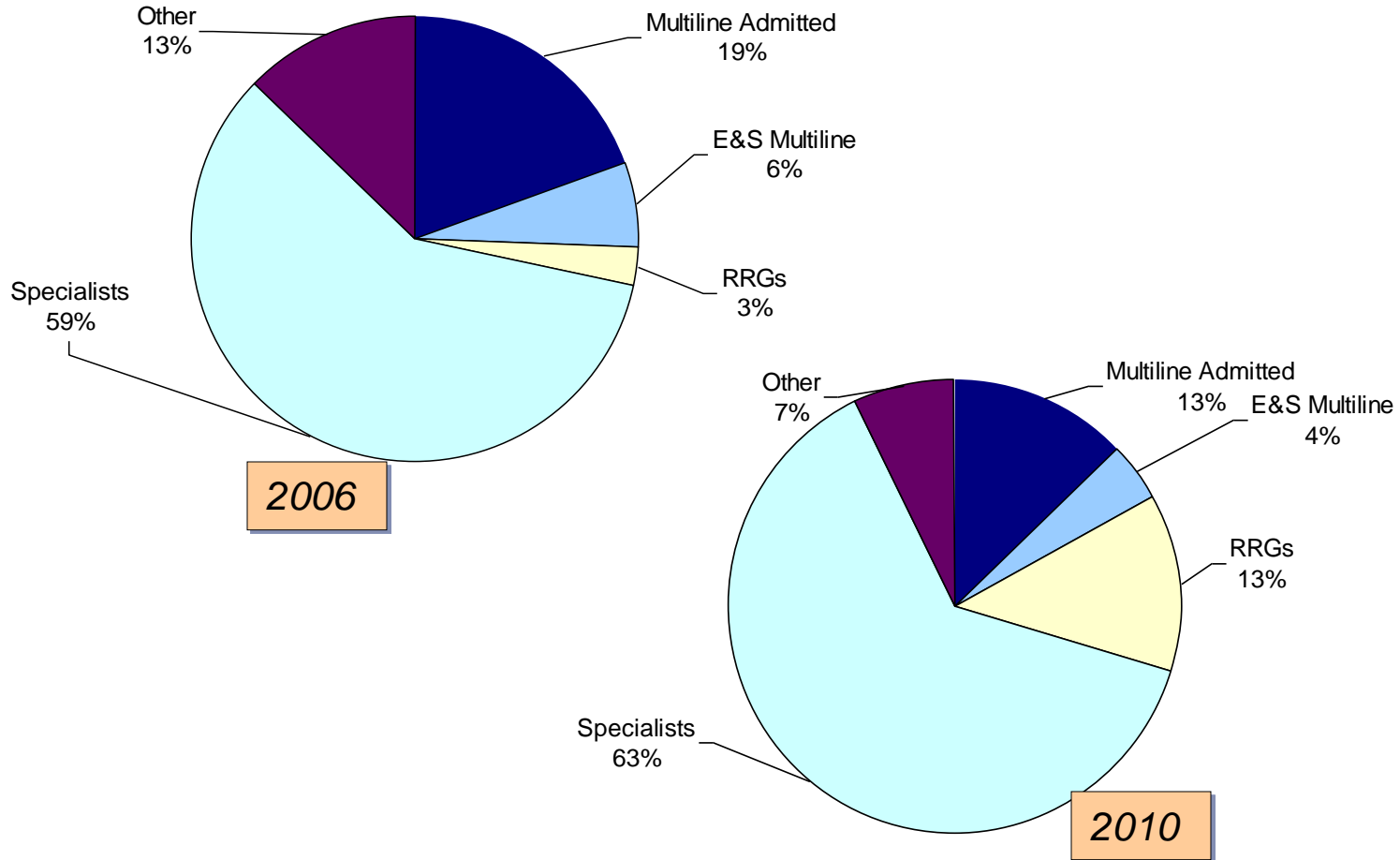
- ◆ The primary market for smaller physician group practices is shrinking
 - ❖ Smaller physician-owned practices merging with hospitals and now ACOs and larger health organizations continues under reform

- ◆ The market for more affordable and more efficient health care providers is expanding, creating growth opportunities
 - ❖ Retail health clinics, outpatient facilities, and remote care monitoring

Will Specialist Companies and RRGs Continue to Expand?

Reported Direct Premiums Written by Type of Insurer

By our estimates, 50% or more of premium equivalents is in captives or otherwise not reported



Source: Company statutory filings, Conning analysis

Financial Advantages of Alternatives

Advantages: (Hope and Change)

- ◆ (Perception of) preferred risk pools, peer group selection
- ◆ Tax benefits if in a captive
(deductibility of premium or incurred loss vs. paid loss)
- ◆ Flexible capital and funding rules
- ◆ Flexible coverage and policy forms/ ability to include broader risks
- ◆ Reduced regulatory requirements

Financial Disadvantages of Alternatives

Disadvantages: (Unintended Consequences)

- ◆ In some cases, members can be assessed for shortfalls
- ◆ Greater risk with lower capitalization—silos of capital
- ◆ Exit strategy unclear and perilous
- ◆ Start-up costs—necessary scale of operations
- ◆ Demands on board and management—skills and resource drain

Qualities of Best-Performing Multilines

Attributes of Best Multilines:

- A core portion of the business is excess coverage over self-insured hospitals, doctors, and health care organizations
- Nearly all of the companies are publicly traded
- The larger multiline companies leverage their intellectual and monetary capital strength to support the self-insured and specialty marketplace

Best-Performing Multiline Insurers, 2008-2009

(\$ in thousands)

Company	Net Premiums Written, 2008 & 2009 Combined
AIG	\$906,766
Markel	237,705
W. R. Berkley	203,706
Zurich	223,025
OneBeacon	208,310
TIG	148,984
Allied World	147,391
ACE USA	143,926
Alleghany	110,211
Arch Capital	22,926
Meadowbrook	20,272
Western World	12,859
Pharmacists Mutual	10,830
HCC	6,127
Farmers	5,633
State Farm	4,438
Chubb	3,036
Total Above Companies	\$2,416,145

Source: Company statutory filings, Conning Research & Consulting analysis

Best-Positioned Insurers Offer an Enterprise Focus

- ◆ Insurance companies may need to bring a more successful value proposition
 - *MDAdvantage announced it will offer coverage for employment practices liability, privacy and data security, and medical practice administration at no extra charge*
 - *The Doctors' Company and Chubb have announced free products to cover cyber risks*

- ◆ New policies bundle more competitive products and services (including new risk management)

- ◆ Some M&A driven by hunger for product diversification

Success of Health Care Reform Tied to Economics

- ◆ Massachusetts enacted reform in 2006, and showed growing physician shortages in lower economic urban and rural markets
- ◆ Reform initiatives have a better chance of success in more affluent regions where coordination of care, patient accountability, and supply of high quality physicians/ nurses is greatest
- ◆ More challenging regions need to be identified and monitored
- ◆ As reforms phase in, “past performance may not be indicative of future results” in states and regions

Refocus Risk Management Practices:

1. Focus risk management on mid-level care providers (nurses, clinicians, and practitioners), train in proper use of EMRs and in how to improve patient relationships
2. Monitor exposure of new efficient medical care facilities
3. Audit the EMR
4. Educate and defend against new legal discovery trends
5. Question/monitor quality of care and expected standards of care in all settings

Conclusions and Outlook

- ◆ Near-term challenges
 - ❖ Competitive environment
 - ❖ Erosion of tort reform
 - ❖ Lower investment yields

- ◆ Longer-term challenges with health care reform
 - ❖ Use of EMR/New electronic discovery
 - ❖ Physician shortages, increasing use of nurse practitioners, further scope creep in providers
 - ❖ Potential impact on quality of care

- ◆ But a path exists for better-informed companies to grow and improve profitability

ABOUT CONNING

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