

We are a company built by doctors, for doctors. We are on a mission to relentlessly defend, protect, and reward doctors who advance the practice of good medicine. When one of our own is attacked, we take it personally. Speaking loudly and clearly for tort reform, we are

M&A in MPL: What Does It All Mean?

your voice. We are committed to protecting doctors. We loathe litigation, so we work hard to reduce risk. We are devoted to rewarding doctors. We are more than an insurance company. We are The Doctors Company.

Jeff Donaldson, FCAS, MAAA



Overview

- Why are there acquisition opportunities in MPL?
- State of the market
 - Underwriting cycle
 - Loss cost trends
 - Reserve evaluations
 - Investment markets
- Reserving considerations

M&A Opportunities

- Fiscally challenged companies
 - Top line erosion
 - Rising expense ratios
 - Report year results deteriorating
- Hard market ... moved to stable ... now going toward soft
 - Some prices hit peak levels
 - Sell before the market is soft

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M&A Opportunities

- Changes in healthcare delivery
 - Consolidation across state lines
 - Formation of Alternative Care Organizations (ACO's)
 - Hospital employment of doctors
- Ability to gain economy of scale
- Ability to decrease volatility

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M&A Opportunities

- New company formations in early 2000's
 - Small companies
 - Lack economies of scale
 - Limited surplus
 - Limited prospects
- Good acquisition targets

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State of the Market

- Underwriting market soft in mid-90's through early-00's
- Calendar year combined ratios over 130% ('00-'03)
- Possible to
 - Gain economy of scale (expense ratio)
 - Decrease volatility
 - Increase geographic spread
 - Increase state market share
 - Access to new markets and MPL expertise

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Underwriting Cycle

- Pricing became weaker in late '90's through mid 2001
 - Substandard market shares declined
 - Large account flexible rating tended to bend downward
 - Brokers provided less detailed information for large accounts
- St. Paul left the market in late 2001
- Market hardened
 - Standard coverage not provided to every doctor
 - No coverage expansions
 - Large rate increases filed (mid 2001 – 2004)

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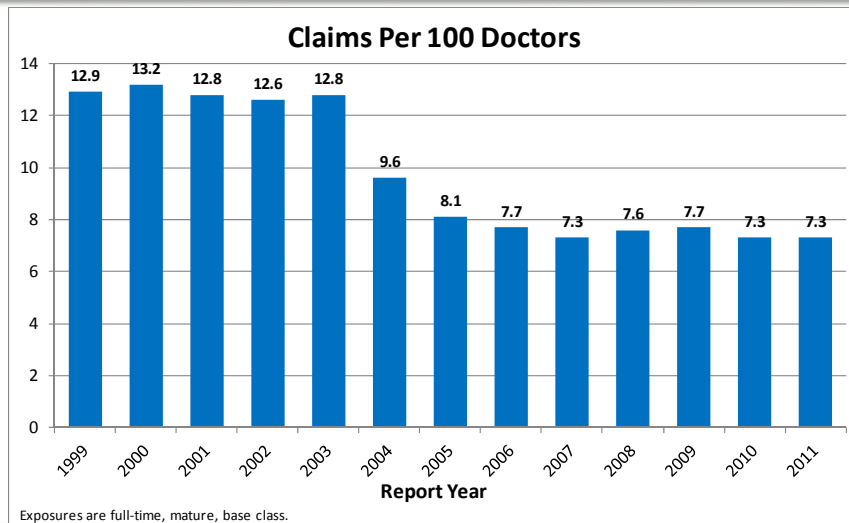
Loss Cost Trends

- Doctors view prices as too high
 - Large rate increases
 - Pressure builds into 2003
 - White coat marches
- Tort Reform
 - 2003 State of the Union speech for federal response
- States implemented tort reforms
- Claim counts started dropping around 2004
- Frequency decline of about 40% - occurred in most states

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Frequency Change



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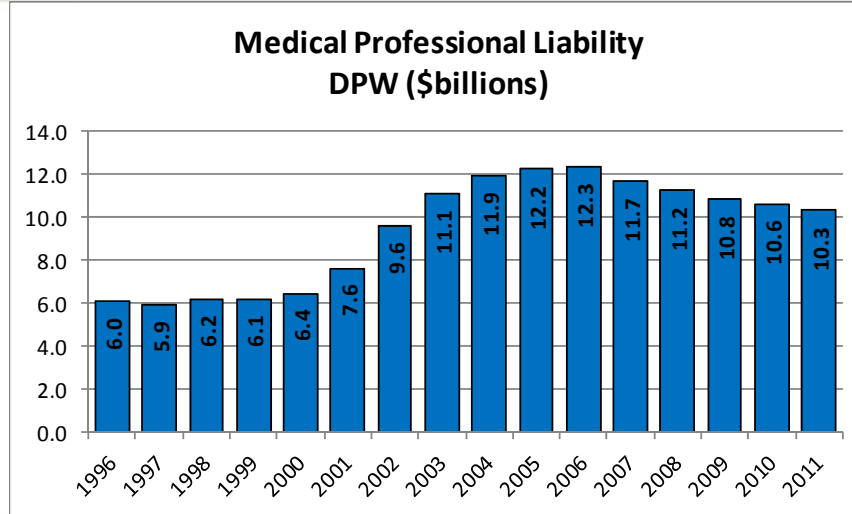
Other Trends

- Earned price increases led to 100% combined ratios by report year 2004
 - Manual rates started to modestly decline
 - Premium credits increasing
 - Expect price decline in 2012
 - Past 2012 ???

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Premium Volume Changes



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Other Trends

- Unexpected frequency decline in 2004
- No immediate response to frequency decline
 - Financial positions still needed improvement (see AM Best)
 - Takes time to understand if loss costs responded like frequency
- Combined ratios well below 100%

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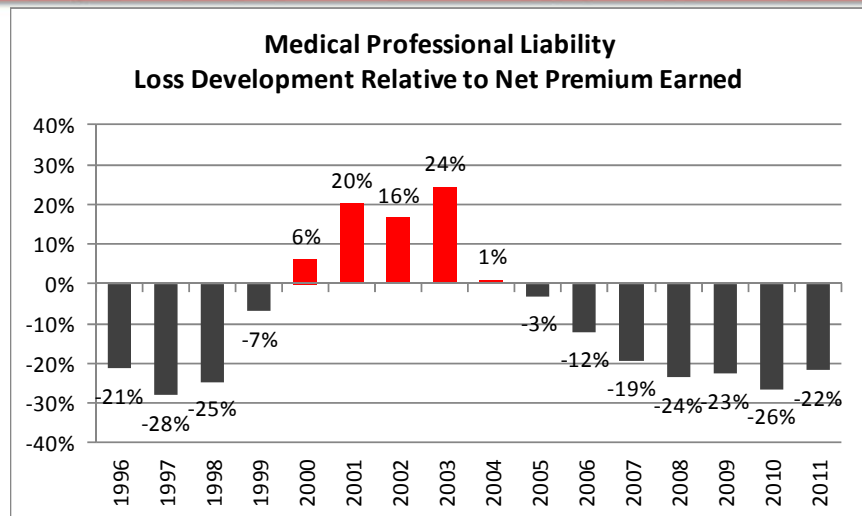
Reserve Evaluations

- Adequate pricing by 2004
- Frequency reduction had unknown impact on losses
- Prudent to reserve conservatively given uncertainty of changing circumstances
- Frequency decline led to a similar adjustment in loss costs
- Favorable development in 2005-2011
 - Pricing declines from 2006-2011 (... and continuing)
 - Stable frequency, with rising severity

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MPL Loss Development



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Investment Markets

- Declining benefit of investment income
 - Large rate increases
 - Lower interest rates
 - Stock market adjustments
- Investment income about 40% of premium in 1990's
- Investment income about 20% of premium in 2000's
- Bond yields dropped dramatically from 1990's to 2000's
- Significant annual gains in the stock market in the 90's, flat from 2000-2012

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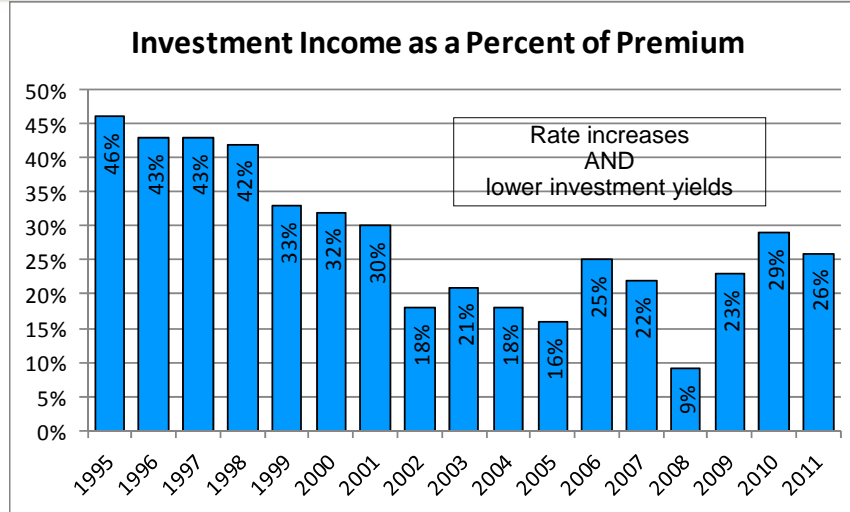
Investment Markets

- Changing investment markets leads to:
 - Lower investment income
 - Lower combined ratio required
 - Rate increase needed to reflect
 - Loss cost growth
 - Reduced investment income

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MPL Investment Performance



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Reserving Considerations

- Need to understand the value of the company
 - Statement of Actuarial Opinion (SAO)
 - Company or consulting actuary
 - Your own evaluation
 - Can be employed and/or consulting actuary
- Develop an expectation for future profitability
 - Company rate reviews
 - Reserve evaluations
 - Pricing considerations

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Reserving Considerations

- Review actuarial work papers from the SAO
- Discuss assumptions with the opening actuary
- Receive company input from claims and underwriting

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Reserving Considerations

- Claims-made, Occurrence, and Pre-Paid Tail
- Tail liability
 - Purchased
 - Death, Disability, and Retirement (DD&R)
- DD&R Unearned Premium Reserve
- Other lines of business
 - Hospitals
 - Facilities
 - Assumed re
 - Dentists, Podiatrists, Chiropractors, ...

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Reserving Challenges

- Case Reserving
 - Not a simple process to determine case reserves
 - Adequacy can change over time
- Closing Rates
 - Patterns can change – watch the volume of claims
- DD&R
 - Age distribution
 - Probabilities of lapsing, retiring, death & disability
 - Probabilities need to vary by age

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Reserving Information

- National Practitioner Data Bank (NPDB)
 - Physician data available by state
 - Also has other types of providers, such as dentists
 - Indemnity value of claims by closure year
- Department of Insurance Data Calls (e.g. Ohio, Florida)
- Annual Statement
 - Value depends on the company being reviewed
- Jury Verdict Research

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Where will we land?

- Underwriting
 - Pricing declining
 - Frequency flat
 - Severity rising
 - Tort reforms maturing
 - New competition
 - Investment income yield is low
 - Healthcare Reform?
- Loss ratios are rising