

September 5, 2006

**Actuarial Analysis of
Office of Insurance Regulation
Filing Number 06-10750
Physicians & Surgeons Professional Liability
First Professionals Insurance Company**

Office of the Consumer Advocate
State of Florida

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PRELIMINARY

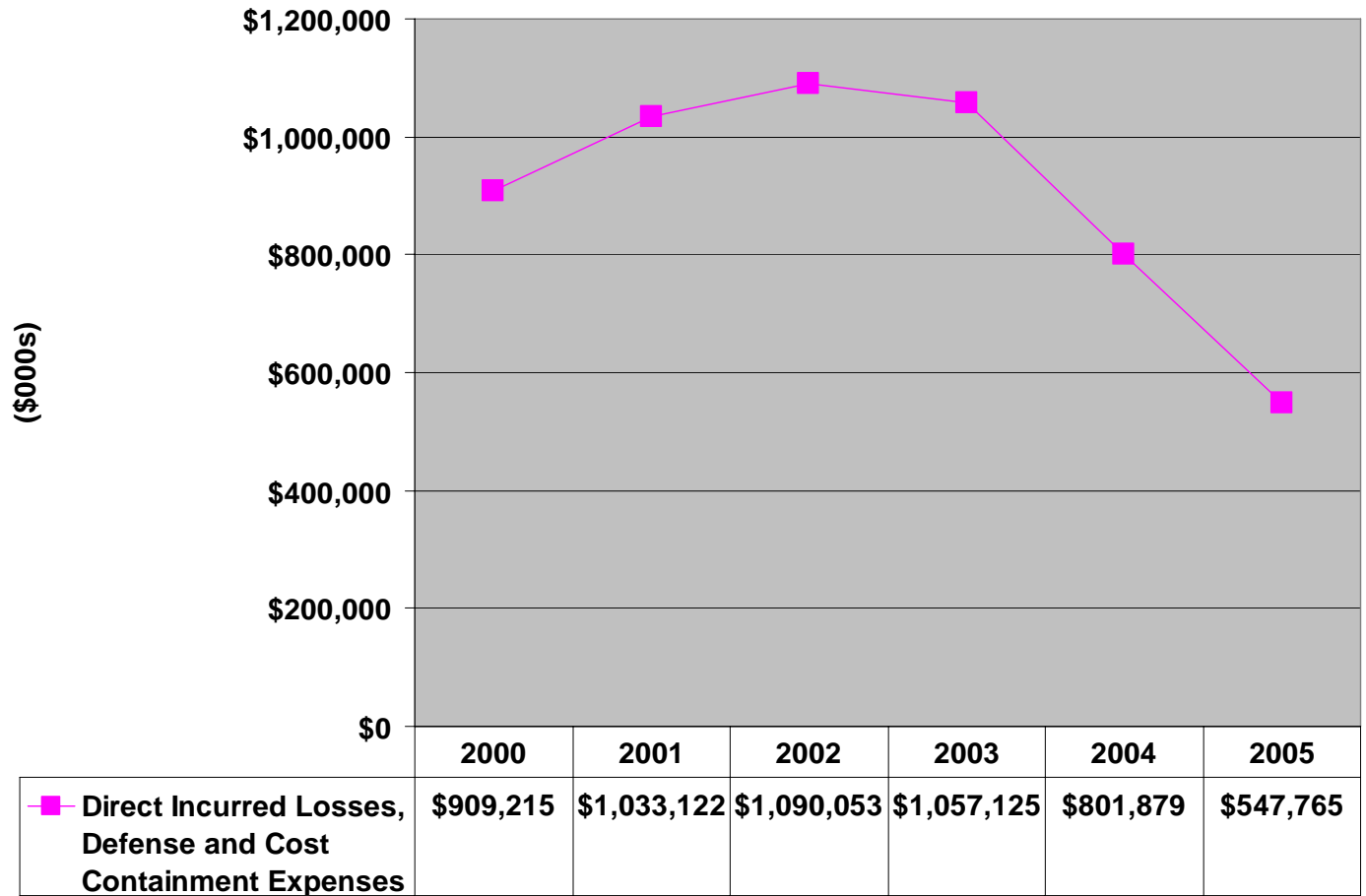
CONCLUSIONS AND RECOMMENDATIONS

Using First Professionals Insurance Company's (FPIC) methodology, but reducing the projected loss ratio to 48.1% from FPIC's 77.2%, FPIC's rates should be decreased 40.1% rather than 11.2% as requested by FPIC. Therefore, any decrease less than 40.1% should be disapproved, because the resultant rates are "likely to produce a profit from Florida business that is unreasonably high in relation to the risk involved in the class of business" 627.062 (2)(e)1. Florida Statutes.

The Office of Insurance Regulation should issue an informational memorandum to all medical malpractice insurers stating that it is no longer acceptable to use a "presumed factor" in its rate indications. Medical malpractice rate filers are still using a presumed factor pursuant to informational memorandum OIR-03-020 issued on November 10, 2003 based on a Deloitte and Touche study of the presumed effect of the tort reforms effective September 15, 2003. The law requiring the use of a presumed factor (627.062 (8) Florida Statutes) only required that it be applied to a single rate filing to take effect no later than January 1, 2004. This statute did not require that a presumed factor continue to be applied in each subsequent filing.

In its analysis, FPIC reduced its rate indication by 4.6% based upon the Deloitte and Touche study. However, the impact of tort reform has been far greater, as can be seen in the following chart, which shows that direct incurred losses, defense and cost containment expenses in Florida have decreased by 48.2% from \$1,057,125 in the 2003 calendar year to \$547,765 in the 2005 calendar year (source AM Best):

**State of Florida
Medical Malpractice Insurance
Direct Incurred Losses, Defense and Cost Containment Expenses**



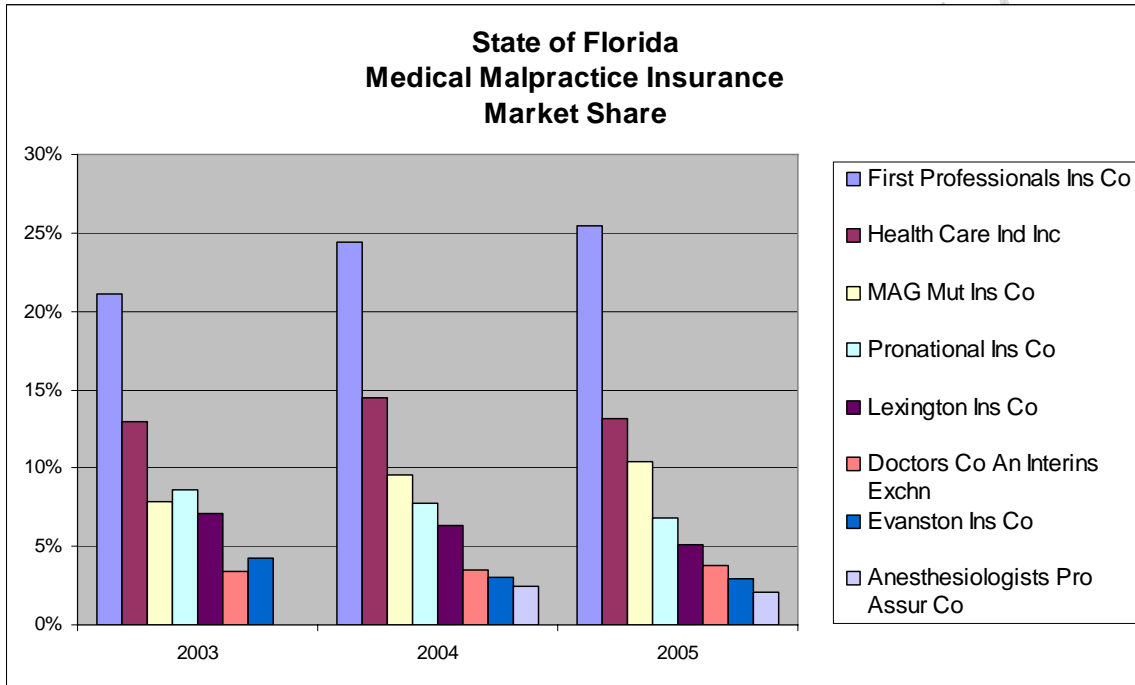
AUTHORITY

This actuarial examination is conducted pursuant to Section 627.0613 Florida Statutes, which provides that: “the Chief Financial Officer must appoint a consumer advocate who must represent the general public of the state before the department and the office. The consumer advocate must report directly to the Chief Financial Officer, but is not otherwise under the authority of the department or of any employee of the department. The consumer advocate has such powers as are necessary to carry out the duties of the office of consumer advocate, including, but not limited to, the powers to:

- (1) Recommend to the department or office, by petition, the commencement of any proceeding or action; appear in any proceeding or action before the department or office; or appear in any proceeding before the Division of Administrative Hearings relating to subject matter under the jurisdiction of the department or office.
- (2) Have access to and use of all files, records, and data of the department or office.
- (3) Examine rate and form filings submitted to the office, hire consultants as necessary to aid in the review process, and recommend to the department or office any position deemed by the consumer advocate to be in the public interest.
- (4) Prepare an annual budget for presentation to the Legislature by the department, which budget must be adequate to carry out the duties of the office of consumer advocate.”

BACKGROUND

The Office of Insurance Regulation (OIR) received the subject filing, OIR File Number: 06-10750 (Filing) on August 16, 2006. Filing proposes to reduce rates on average by 11.2%, effective December 1, 2006 for new and renewal business. FPIC was the largest writer of medical malpractice insurance in the state of Florida in 2005 with a 25.4% market share. The eight largest writers and market shares for the latest three years are shown in the following chart (source AM Best):



PREL

TORT REFORM

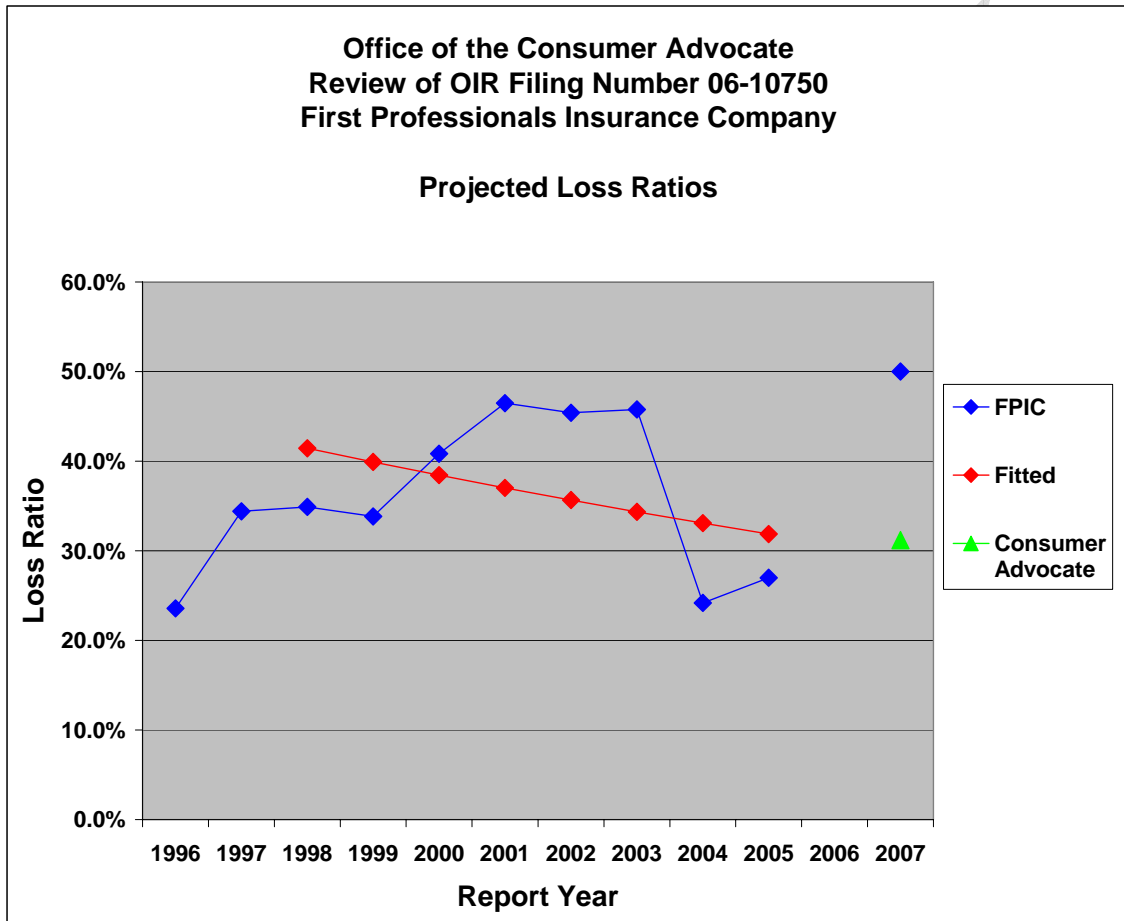
Florida enacted significant medical malpractice liability tort reform (damage caps) effective September 15, 2003. Florida's damage caps are as follows: for physicians, \$500,000 cap on non-economic damages per claimant with any one physician not responsible for more than \$500,000. For non-practitioners, \$750,000 cap on non-economic damages. The cap increases to \$1 million in non-economic damages for physicians if the negligence resulted in death or a permanent vegetative state or if the court finds that a manifest injustice would occur unless the non-economic damages cap was increased because the non-economic harm sustained by the patient was particularly severe and the defendant's negligence caused a catastrophic injury to the patient.

On April 22, 2004, Circuit Court Judge Marlene Alva issued a short written order stating that the application of the new law was unconstitutional, because it retroactively took away vested rights of patients who were already injured by malpractice before the date the new legislation was enacted. The court's ruling is limited solely to the retroactivity issue, and what it means is that there is no immunity for any negligence occurring before September 15, 2003. The same legal reasoning should also apply to the retroactive application of the damage caps in other cases.

ANALYSIS

The following chart shows: 1) FPIC's estimated ultimate losses and allocated loss adjustment expense (ALAE) divided by earned premiums adjusted to current rates, 2) an exponential trend line fitted to the latest eight loss ratios at current rates, 3) FPIC's estimated loss ratio for 2007 if rates are not changed, and 4) the Consumer Advocate's estimated loss ratio for 2007 if rates are not changed.

Exhibit 3



FPIC's estimated loss ratio at current rates for the 2007 report year is based upon a selected 7.0% annual loss trend applied to all of FPIC's loss ratios at current rates over the last ten years. Using this methodology, FPIC projected a 50.0% loss ratio at current rates for the 2007 report year. The Consumer Advocate's estimated loss ratio at current rates for the 2007 report year is based upon a selected 7.0% annual loss trend applied to only the latest two years' experience that reflect tort reform. Using this methodology, the Consumer Advocate's projected loss ratio is 31.2% at current rates for the 2007 report year.

It should be noted that the above projected loss ratios do not include discounts; death, disability and retirement loading (DD&R); unallocated loss adjustment expenses (ULAE)

or a provision for losses in excess of policy limits (XPL). After these adjustments, the projected loss ratios for FPIC and the Consumer Advocate are respectively 77.2% and 48.1% (Exhibit 1, Row (8)).

FPIC's loss ratios declined dramatically after tort reform and have now begun to stabilize. It is estimated that approximately 60% to 65% of FPIC's claims reported in 2005 occurred after the September 15, 2003 effective date of the reforms, and therefore are subject to the reforms. Furthermore, it is estimated that nearly all claims reported in 2006 will be subject to tort reform. By 2007 the windfall benefits of tort reform will probably be over, and the upward trend in loss ratios should resume due to inflation in claim costs.

The above estimates rely upon the assumption that FPIC's claims occurring in a given calendar year will be reported over the 5 years after occurrence in approximately the following percentages: 35.0% within the first year, 60.0% within 2 years, 83.0% within 3 years, 92.0% within 4 years and 100.0% within 5 years.

PRELIMINARY

EXHIBITS

Exhibit 1: Indicated Rate Change

Exhibit 2: Projected Loss Ratio

PRELIMINARY

Office of the Consumer Advocate
 Review of OIR Filing Number 06-10750
 First Professionals Insurance Company

Indicated Rate Change

	(1)	(2)
	FPIC	Consumer Advocate
(3) Manual Loss & ALAE Ratio	50.0%	31.2%
(4) Average Discount	25.0%	25.0%
(5) DD&R	1.050	1.050
(6) ULAE	1.060	1.060
(7) XPL	1.040	1.040
(8) Net Loss & LAE Ratio	77.2%	48.1%
(9) Expenses	19.6%	19.6%
(10) Permissible Loss Ratio	80.4%	80.4%
(11) Indicated Manual Rate Change	-4.1%	-40.1%
(12) Presumed Factor	95.4%	n/a
(13) Indicated Rate Change Net of Presumed Factor	-8.5%	-40.1%
(14) Class Offset	-1.4%	-1.4%
(15) Indicated Base Rate Change	-7.2%	-39.3%
(16) Selected Base Rate Change	-10.0%	-39.3%
(17) Overall Selected Rate Change	-11.2%	-40.1%

Notes:

- (1) Based on FPIC Filing Exhibit 1
- (3) Column (2) from Exhibit 2, Row (22)

Office of the Consumer Advocate
 Review of OIR Filing Number 06-10750
 First Professionals Insurance Company

Projected Loss Ratio
 Losses Limited to \$250,000

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)
Report Year	Earned Base Equiv @ Current Relativities	Current Basic Limits Base Rate	Earned Premium @ Present Rate	FPIC Selected Ultimate Losses	FPIC Selected Ultimate ALAE	FPIC License & Investigation Ultimate ALAE	FPIC Total Ultimate Losses & ALAE	FPIC Projected Loss Ratio at Current Rates	Consumer Advocate Projected Loss Ratio	8 Point Fitted
(12)	1996	9,554	14,004	133,800,840	19,644,508	11,600,000	283,740	31,528,248	23.6%	
(13)	1997	11,585	14,004	162,239,018	36,300,000	19,100,000	425,000	55,825,000	34.4%	
(14)	1998	11,332	14,004	158,700,270	33,000,000	21,800,000	575,000	55,375,000	34.9%	41.4%
(15)	1999	10,458	14,004	146,446,888	29,000,000	19,750,000	785,000	49,535,000	33.8%	39.9%
(16)	2000	9,689	14,004	135,678,018	31,500,000	23,400,000	505,000	55,405,000	40.8%	38.4%
(17)	2001	10,067	14,004	140,985,112	32,500,000	32,500,000	530,000	65,530,000	46.5%	37.0%
(18)	2002	13,919	14,004	194,919,250	41,500,000	46,500,000	515,000	88,515,000	45.4%	35.7%
(19)	2003	13,975	14,004	195,707,185	44,800,000	44,500,000	265,000	89,565,000	45.8%	34.3%
(20)	2004	15,284	14,004	214,039,487	28,500,000	23,000,000	280,000	51,780,000	24.2%	33.1%
(21)	2005	15,363	14,004	215,147,631	32,500,000	25,000,000	575,000	58,075,000	27.0%	31.9%
(22)	12/1/2007							50.0%	31.2%	

Notes:

- (1) - (9) Based on FPIC Filing Exhibit 2
 (10) Average of Column (9), Rows (20) and (21) trended at 7.0% per annum to 12/1/2007
 (11) Based on exponential curve

PRELIMINARY

