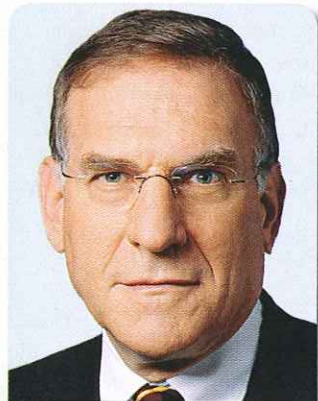


# State of the Medical Professional Liability Market

After several years of surprising drops in claims frequency, insurers and sector experts are bracing for a return to a more traditional—and possibly volatile—environment.



**DR. RICHARD ANDERSON**

Chairman and CEO of California-based The Doctors Co., an insurer of more than 45,000 physicians around the United States.



**MARC ZIMMERMANN**

Senior vice president and CFO of American Physicians Insurance Co. Physicians has been writing in Texas for more than 33 years and also writes coverage in Oklahoma and Arkansas.



**STANCIL STARNES**

Chairman and CEO of ProAssurance, which is publicly traded on the New York Stock Exchange. It insures 55,000 policyholders in the health care field throughout the United States.



**LAWRENCE DOWNS**

General counsel at the Medical Society of New Jersey. The Princeton-based professional organization for physicians of all specialties represents some 9,000 physician members.



**PAUL TURNER**

A lawyer with Chicago-based firm McCullough, Campbell and Lane. The firm primarily represents excess insurers and reinsurers of self-insured hospitals throughout the United States.



**CHAD KARLS**

A principal and consulting actuary in the Milwaukee office of Milliman. Karls specializes in actuarial consulting to the medical professional liability sector.



**HENRY WITMER**

Assistant vice president at the A.M. Best Co. Witmer leads a team of rating analysts who follow all the dedicated medical professional liability insurers.

Webinar moderator: Lee McDonald, group vice president communications, A.M. Best Co.

The entire transcript and video replay of the webinar can be accessed at [www.ambest.com/multimedia/medical110.html](http://www.ambest.com/multimedia/medical110.html).



The editors of *Best's Review* were joined by a panel of experts and insurers to examine the state of the medical professional liability insurance market, including coverage trends, the competitive landscape and issues affecting the financial strength of insurers serving this crucial market serving doctors, hospitals and other health professionals. This is an edited transcript of the webinar.

## A.M. Best Co. on the Medical Liability Marketplace

**“One of the things that we see in the impairment studies is that excessive growth is one of the main reasons for companies becoming impaired or experiencing severe financial stress. Right now we're not seeing too much of that aggressive growth, at least at this stage. Most companies are trying to hold on to their current books of business.”**

—Henry Witmer,  
A.M. Best Co.

**McDONALD:** What are the biggest factors shaping the medical liability environment today?

**WITMER:** The two main issues are competition and insuring rate adequacy. In almost all jurisdictions we're receiving reports of very competitive or moderately competitive market conditions. This is exhibited by and is caused by some rate decreases and the more aggressive use of premium credits or discounts. It's also exacerbated by some new entrants that are attempting to establish a market presence in some of the areas.

This of course does vary considerably by state and by the type of medical specialties that are included in various companies' books of business. But for the majority of the carriers we follow, rates still are adequate although they are under pressure.

**McDONALD:** What are we saying about the general financial condition of the medical liability sector?

**WITMER:** Well, right now we're still viewing the industry as stable as a whole. So far, despite those competitive conditions, the insurers that we do rate are exercising a significant amount of underwriting discipline and aggressive claims handling. Along with reaping the benefits of some of the conservative loss reserve setting, we are seeing improvements in

the financial strength among those insurers that we do follow. Nonetheless, this is a cyclical business and we are watching developments very carefully.

**McDONALD:** Can you put that in terms of some of the key metrics or ratios that we consider when we look at the sector and companies? How are they doing?

**WITMER:** We look at the combined ratio and other profitability ratios, a variety of leverage ratios, growth rates and liquidity. Since about 2000, from our data, the industry's calendar year combined ratio has improved. It peaked around 2003 at about 131.3 and now is down to about 82.7 as of 2008. A somewhat higher combined is expected for 2009 due to some declining premium rates.

Similarly, from a peak from 5.2 in 2003, the industry net leverage ratio is down to about 3.4 in 2008, and looks to be around there for 2009. These are good numbers and will lead to favorable Best's Capital Adequacy Ratio model calculations.

The investment leverage side, especially in this day and age, is fairly conservative at this point, which is important and we are monitoring that. Growth rates for most companies also have been moderate lately. That's a key factor we follow because one of the things that we see in the impairment studies is that excessive growth is one of the main reasons for companies becoming impaired or experiencing severe financial stress. Right now we're not seeing too much of that aggressive growth, at least at this stage. Most companies are trying to hold on to their current books of business.

Also on the investment side, with most companies holding large cash positions and short durations on their bond portfolios, liquidity measures are fairly sound as well.

**McDONALD:** Any particular developments or factors, in addition to ratios, that we're paying close attention to at this point?

**WITMER:** Let me say that overall our focus is on durable financial strength and this will position a company through any ups and downs of the market cycles so they can provide secure coverage for their insureds. So, in addition to the quantitative measures that I mentioned already, we do pay close attention to the nuances and risks associated with the

The Financial Strength Rating opinion addresses the relative ability of an insurer to meet its ongoing insurance obligations. The ratings are not assigned to specific insurance policies or contracts and do not address any other risk, including, but not limited to, an insurer's claims-payment policies or procedures; the ability of the insurer to dispute or deny claims payment on grounds of misrepresentation or fraud; or any specific liability contractually borne by the policy or contract holder. A Financial Strength Rating is not a recommendation to purchase, hold or terminate any insurance policy, contract or any other financial obligation issued by an insurer, nor does it address the suitability of any particular policy or contract for a specific purpose or purchaser. In arriving at a rating decision, A.M. Best relies on third-party audited financial data and/or other information provided to it. While this information is believed to be reliable, A.M. Best does not independently verify the accuracy or reliability of the information. For additional details, see A.M. Best's Terms of Use at [www.ambest.com](http://www.ambest.com).



various types of business that are covered. This would include whether the insured base is physicians, dentists, chiropractors and other specialty types of practices and even hospitals and clinics that might be on the books. Each has its own exposures and limits of liability and various circumstances and we need to see how those companies manage that, what their plans are for the future and how they will execute on those plans effectively, given the available resources that they have.

What we also need to understand is what is the value-added proposition of the company.

How will they build on that for long-term viability?

## Frequency and Severity

**“The reduction in claims frequency that occurred, depending upon the state or the jurisdiction, may be in the 2003-2004 time period, in my view, that’s been the single most important reason for the industry’s favorable operating results of the past few years.”**

—Chad Karls,  
Milliman

**McDONALD:** Whenever you talk about the state of med mal, inevitably it gets to a discussion of what happened with frequency. Obviously the companion to that is severity. So apparently it’s dropped since 2004 and 2005 noticeably. When we talked earlier you were saying that may not be the case today, or at least you might be seeing some things that cause you to look more closely. What are you seeing?

**KARLS:** I think that’s an excellent point. The reduction in claims frequency that occurred, depending upon the state or the jurisdiction, may be in the 2003-2004 time period, in my view, that’s been the single most important reason for the industry’s favorable operating results of the past few years. Again, depending upon the state or market, it seems as though the claims frequency fell off somewhere in 2003 and 2004. It varied by company. It varied by market. The magnitude of that falloff obviously varied by company and market. There are some situations in which the magnitude of the frequency reduction has been upward of 40% to 50%, which is quite remarkable.

Of course a follow-up question that always comes up when we talk about what happened to frequency, and it is a very good one, and that is simply, why? Why did frequency do what it did? At least in my view, the short answer is nobody is really sure. There have been a number of commonly cited reasons, including in certain jurisdictions one could perhaps choose specific tort reforms that were enacted in a particular state. Certainly I think that has had an effect on claim frequency. I don’t think it can be the sole reason though, because not every state had tort reform passed around that time period, in the 2003-2004 time period.

So that can’t be the only reason. I certainly think it’s contributory. I would expect that to some degree the falloff in claim frequency is also related to the whole, what I’ll call the patient safety movement. An awful lot of attention was paid to that and continues to be paid to that, and for good reason. I’ve got to believe that has had an effect as well on raising the awareness in terms of how health care is being delivered, maybe in a safer way. I’d like to believe that too has contributed to the falloff in claim frequency that we’re seeing.

A third reason I’ve heard discussed a fair amount is that simply the economics have changed from the plaintiff attorney’s perspective in terms of the economic feasibility of bringing a claim with perhaps more limited damages, given the increasing costs of bringing forward a claim coupled, in some states anyway, with perhaps a cap on noneconomic damages.

Finally, some have said that part of the reason for the falloff in frequency is that there have been changes in society’s attitudes and propensities toward bringing claims against health care providers, particularly in light of what happened in the early part of the decade, with the rather well-publicized examples of the limitations in the access to health care that people were experiencing in certain parts of the country. It’s hard and frankly, impossible, to quantify, but I believe that on some level this, too, had an effect in terms of the falloff in claims frequency as of late.

## Legal Issues

**“We’re still, I think by most observers, considered a very plaintiff friendly jurisdiction. We continually try to move some meaningful tort reform, everything from better statutes of limitations for cases to non-economic damage caps, without much success at all.”**

—Lawrence Downs,  
Medical Society of New Jersey

**McDONALD:** Why don’t we talk about the broad legal environment? Obvious there’s the whole issue of tort reform. Since you’re based in Chicago, you actually are the headline story of the past week with the reversal there. Could you talk about that for a minute?

**TURNER:** Sure. It may be headlines in other places but here in Cook County I think that the Supreme Court’s decision in *Lebron* was fully anticipated and discounted. None of the settlements that I’ve been involved in for the last couple of years paid the slightest attention to the caps anymore. There was almost a universal acceptance that it would be overturned by the Supreme Court. In fact it was overturned in Cook County two years ago. *Lebron* was a Cook County case going up, so the caps haven’t been law here for quite some time.

The decision itself though had a couple of interesting twists, I thought. It followed party lines. We elect our justices



here by party and all the Democrats voted to strike down the damage caps and all the Republicans, except for one who recused himself, voted to keep them. But what they said was kind of amusing because it starts with a couple of paragraphs saying how sorry President Obama is going to be because of this decision and how much it sets back his health care reform agenda. I'm not sure other people would agree with that but it was kind of a funny way for a court to open up a dissenting opinion.

The other interesting factor is that the majority held out an open invitation to pass tort reform again with anything except damage caps. A few years ago, the last time we had tort reform in Illinois, there was a decision called *Best v. Taylor Machine Works*. It had two rationales for striking down damage caps. One was that it was special legislation instead of general legislation because it affected different kinds of plaintiffs differently. Second, it violated the separation of powers because it was really a form of legislative remittitur whereas a remittitur is supposed to be a judicial remedy.

This time around, the court only used the second theory, which meant that it only applies to damage caps. It had to strike down the whole bill because there was an inseverability clause. The court came right out and said: General Assembly, if you want to give us another bill and this time include other items that were in the first bill, those won't fall under this decision and may well be acceptable.

So something like abolition of joint liability could be in the cards in Illinois, at least as far as this decision is concerned.

**McDONALD:** Larry, what's been the experience in New Jersey at this point?

**DOWNES:** Well, certainly the decision in Illinois last week did not help our chances if we had any kind of meaningful tort reforms in New Jersey. We're still, I think by most observers, considered a very plaintiff friendly jurisdiction. We continually try to move some meaningful tort reform, everything from better statutes of limitations for cases to noneconomic damage caps, without much success at all.

Recently we've had a Republican elected to our governorship. However, our Legislature is still very Democratic and is very adverse to meaningful reform in that arena. I think our

experience has been, any hope that we had certainly the Illinois decision is making the rounds within the political gossip columns in New Jersey and certainly makes it very difficult now for any efforts to instill damage caps in this jurisdiction.

## Overall Environment

**"If you assume that claim counts are going to continue to stay low and severity is going to continue to stay low and they don't, that's a recipe for disaster long-term."**

—Marc Zimmermann,  
American Physicians Insurance Co.

**McDONALD:** At this point we'd like to turn it over to our actual practitioners on the company side. Dr. Anderson, you're in a multistate environment. What are you seeing as far as competition and the whole environment?

**DR. ANDERSON:** We've just gone through a period that we seem to repeat even in the largest national and international macroeconomic cycles, of the bursting of a major bubble. We're always shocked and horrified when it occurs. We try to figure out what could we have seen in retrospect that might have allowed us to avert that.

Of course the more specific challenge in general is looking prospectively and trying to predict the inflection point on any curve. Where is the inflection point going to be? I think here in the med mal market we have, what I believe, is a real luxury in that it's quite obvious that we are in the middle of an inflection point, that the hard market, the true hard market that began around 2002 with the demise of St. Paul as a med mal carrier and ended in 2005, 2006, is transitioning to what almost surely will be a true soft market. We're right in the middle of that transition point now. What does that mean? It means that rates are softening everywhere around the country. It means that doctors who were formerly appropriately rated as substandard physicians in terms of insurability are now drifting back into the standard market. It means that competition for large custom accounts is heating up and that cash flow underwriting is looking more attractive. People are looking for large premium volumes in a single gulp, even if that premium doesn't represent an adequate price to cover the ultimate loss.

From my point of view, what we are experiencing with virtual certainty is the transition from a hard market to a soft market. Where we are right now is a situation with general reserve redundancy and price adequacy but with all those indicators now heading in a negative direction.

**McDONALD:** What are you seeing in terms of the competitive environment and what do you think about each day when you look out at your business?

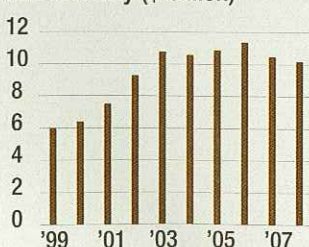
**STARNES:** As you evaluate this business I think you have to recognize that every state is indeed a different business. If you write, say business in 50 states, you're in the 50 different businesses and you have to accommodate the nature of each state in deciding what business you're going to write and how you're going to execute that business.

## Medical Professional Liability

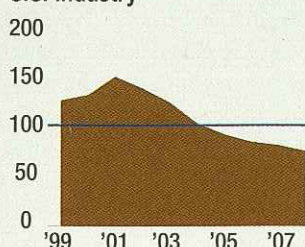
Policies provide professional liability coverage for physicians and other medical professionals against lawsuits alleging negligence or errors and omissions during the care of their patients.



### Direct Premiums U.S. Industry (\$ billion)



### Combined Ratio U.S. Industry



Source: 2009-2010 *The Guide to Understanding the Insurance Industry*,  
BestLink.



The difficulty that every carrier faces today are the challenges that are created by the confluence of a soft insurance market, a low interest rate investment environment and a great uncertainty as to the consequences of health care reform.

Each of those three things has a direct impact on our future, both near-term and long-term future. It is in evaluating each of those things and attempting to maintain the prudence and the rationality in our operations in which we will either succeed or fail. All of those things mean that it is more important than ever that we remain very adequately reserved and, if we walk away from inadequate rates, that we are in a position to fulfill the promises we make to our insureds, which, in our long-term business will have to be met four or five or six years from now. So, I think it's acutely important that we keep all of that in mind and recognize that we are operating today in an ever more challenging environment created by those very unique conditions.

**McDONALD:** Could you start out just by explaining for people who are not in Texas what makes your environment a little bit different in terms of reform and how that's affected the market and then go into what you're seeing through your company's eyes?

**ZIMMERMANN:** In regards to Texas, tort reform is a little bit different than what you've seen on a national level. We have a cap on noneconomic damages but what's important in our reform is it's a constitutional amendment that was voted on by popular election. So that obviously makes it more difficult to overturn and while it's seen its

recent challenges—in the foreseeable future we do not see any meaningful attacks against it. As we look at our state and we look at what we've been able to do, post-tort reform, most of the carriers have performed very well. The companies have produced exceptional combined ratios, driven by reform, which has resulted in favorable development of reserves. Soft markets do vary by state, also in regard to the timing of rate decreases. We've seen substantial capacity through increased competition in Texas. Currently, physicians have multiple options at renewals. What we saw immediately before and then directly after the passage of tort reform was a significant increase in the number of claims reported, then a significant drop in the number of claims. Then rate decreases peaked in 2005, 2006 and 2007, and have begun to moderate. But we are seeing a lot of aggressive pricing by carriers out to win market share, bordering on irrational. Several competitors are booking their current accident years at low levels and writing at low-level prices, which doesn't leave much room for error in your pricing given the long-tail nature of the MPL line of business. I use the housing analogy. If your financial model includes the thought that housing prices are going to continue to go up and they don't, and on the flip side of our business, if you assume that claim counts are going to continue to stay low and severity is going to continue to stay low and they don't, that's a recipe for disaster long-term. **BR**

## Are your defense legal bills out of control?



Recent legal publications have reported that some large law firms now charge hourly fees that approach **\$1000 per hour**, while many so-called "litigators" have little or no actual trial experience.

When you need **TRIAL** counsel in Missouri, Illinois, or to coordinate defense counsel nationally, at fair and reasonable rates that aren't inflated to compensate for less profitable law firm "departments" or expensive firm overhead costs, choose a boutique insurance defense litigation firm with a proven track record in court, and a reputation as a firm that is not afraid of the challenges of major litigation.

Visit our website or call for further information

**EM** ECKENRODE ■ MAUPIN  
ATTORNEYS AT LAW

8000 Maryland Avenue, Suite 1300

St. Louis, Missouri 63105

(314) 726-6670

[www.eckenrode-law.com](http://www.eckenrode-law.com)

**SMALL Firm Attention**

**LARGE Firm Service**

The choice of a lawyer is an important decision and should not be based solely on advertisements.