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Medical Professional Liability Sector: The State of the U.S. Market

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US MPL Segment Highlights

- US MPL segment started 2023 with some optimism following solid improvement in underwriting results in 2022 and rising yields on fixed-income portfolios.
- Overall profitability in 2023 was buoyed by a significant rise in net investment income.
- Improvement in underwriting results stalled in 2023, driven in part by rising expenses, both underwriting and loss adjustment expenses.
- In 2023, prior year reserve development was again favorable—for the 15th year in a row – but remains well below historical levels.
- The effects of prior pricing actions are now evident in accident years 2022 and 2023.

US MPL – Ultimate Incurred Loss & DCC Ratios, 2013-2023

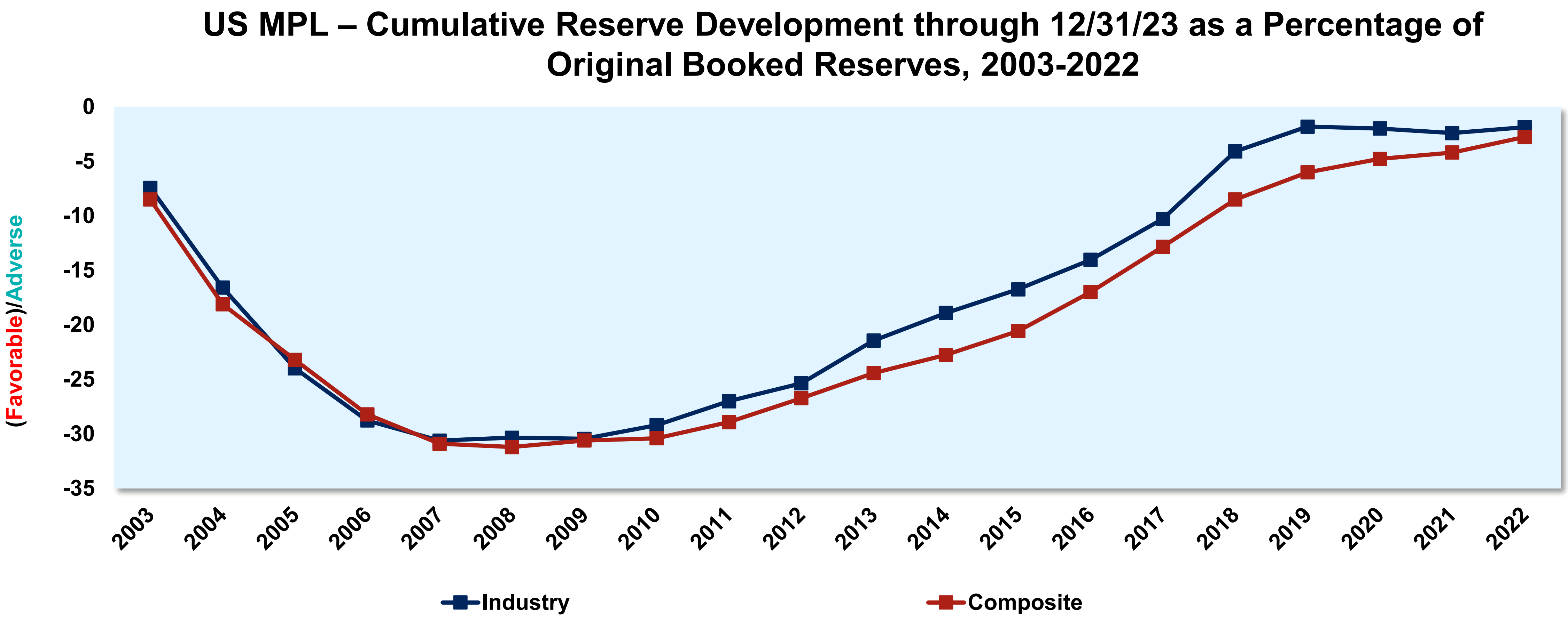
Accident Year	Initially Booked	Developed Through 12/22	Estimated Ultimate
2013	79.2	68.4	68.8
2014	81.2	71.5	71.3
2015	81.3	73.1	73.3
2016	80.9	79.2	78.9
2017	81.7	81.3	81.2
2018	80.4	86.1	87.4
2019	82.9	84.3	84.5
2020	82.3	81.5	76.1
2021	78.9	76.1	66.8
2022	76.3	76.3	64.0
2023	--	--	65.5

Source: Am Best data and research

US MPL Industry Reserve Position

- The MPL industry's reserve position has stabilized over the past couple of years.
- AM believes that 2023 calendar year-end booked net loss and LAE reserves will ultimately prove to be redundant by $2.4 billion, including the effect of $0.6 billion in statutory discounting.
- Expect the industry to maintain its redundancy at ~$2.0 billion for the near term
- Even though industry reserves overall appear to be redundant at calendar year-end 2023, reserve positions will vary greatly by insurer
- Redundancies for insurers in the MPL composite have been slightly higher over the last decade than for the MPL industry overall.

MPL Composite – Cumulative Reserve Development



Source: AM Best data and research

US MPL Segment Headwinds

MPL Insurers continue to face many of the same headwinds as in years prior:

- Social inflation and the growing frequency of high severity losses
- Erosion of tort reforms in some jurisdictions
- Consolidation in healthcare continues, driven in part by private equity investment
- Trend towards larger physician groups & integrated healthcare systems
- Escalating burnout rates, staffing shortages, and further growth of alternative care providers
- Growing complexity of medical care and acceleration of telehealth and digital health service

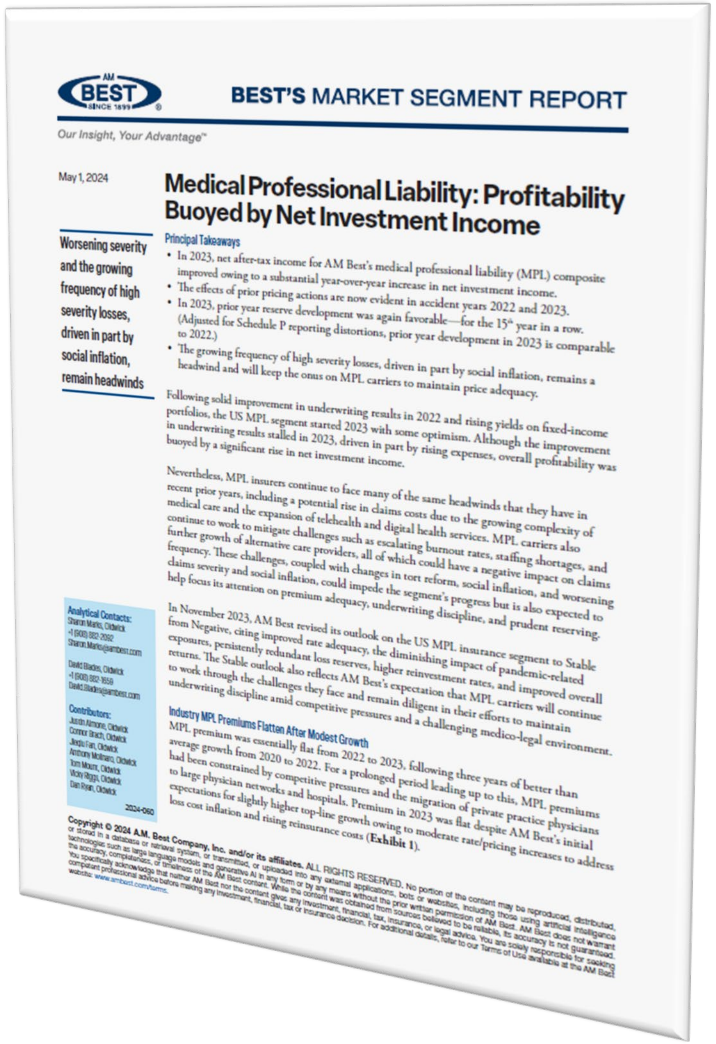
US MPL Segment Outlook

In November 2023, AM Best Revised its Outlook on the US MPL Segment to Stable from Negative, Reflecting the Segments:

- Capital strength and resiliency through continued headwinds
- Improved rate adequacy
- Diminishing impact of pandemic related exposures
- Consistently redundant loss reserves
- Higher reinvestment rates and improved overall returns
- Expectations for continued diligence and underwriting discipline

Additional Report Highlights

- **Other issues that are important for MPL insurers:**
  - Top writers and M&A impact
  - Composite financial results & insights
  - Social inflation impacts on MPL
  - Tort reform challenges
  - Cyber security risks remain a major concern
  - Evolving risks that are challenging healthcare providers and the carriers that insure them
  - The benefits of innovation and its increasing level of importance in the healthcare industry, and for insurers of medical professional liability



BEST'S MARKET SEGMENT REPORT

Our Insight, Your Advantage™

May 1, 2024

Medical Professional Liability: Profitability Buoyed by Net Investment Income

Worsening severity and the growing frequency of high severity losses, driven in part by social inflation, remain headwinds

Principal Takeaways

- In 2023, net after-tax income for AM Best's medical professional liability (MPL) composite improved owing to a substantial year-over-year increase in net investment income.
- The effects of prior pricing actions are now evident in accident years 2022 and 2023.
- In 2023, prior year reserve development was again favorable—for the 15th year in a row. (Adjusted for Schedule P reporting distortions, prior year development in 2023 is comparable to 2022.)
- The growing frequency of high severity losses, driven in part by social inflation, remains a headwind and will keep the onus on MPL carriers to maintain price adequacy.

Following solid improvement in underwriting results in 2022 and rising yields on fixed-income portfolios, the US MPL segment started 2023 with some optimism. Although the improvement in underwriting results stalled in 2023, driven in part by rising expenses, overall profitability was buoyed by a significant rise in net investment income.

Nevertheless, MPL insurers continue to face many of the same headwinds that they have in recent prior years, including a potential rise in claims costs due to the growing complexity of medical care and the expansion of telehealth and digital health services. MPL carriers also continue to work to mitigate challenges such as escalating burnout rates, staffing shortages, and further growth of alternative care providers, all of which could have a negative impact on claims frequency. These challenges, coupled with changes in tort reform, social inflation, and worsening claims severity and social inflation, could impede the segment's progress but is also expected to help focus its attention on premium adequacy, underwriting discipline, and prudent reserving.

In November 2023, AM Best revised its outlook on the US MPL insurance segment to Stable from Negative, citing improved rate adequacy, the diminishing impact of pandemic-related exposures, persistently redundant loss reserves, higher reinvestment rates, and improved overall returns. The Stable outlook also reflects AM Best's expectation that MPL carriers will continue to work through the challenges they face and remain diligent in their efforts to maintain underwriting discipline amid competitive pressures and a challenging medico-legal environment.

Industry MPL Premiums Flatten After Modest Growth

MPL premium was essentially flat from 2022 to 2023, following three years of better than average growth from 2020 to 2022. For a prolonged period leading up to this, MPL premiums had been constrained by competitive pressures and the migration of private practice physicians to large physician networks and hospitals. Premium in 2023 was flat despite AM Best's initial expectations for slightly higher top-line growth owing to moderate rate/pricing increases to address loss cost inflation and rising reinsurance costs (**Exhibit 1**).

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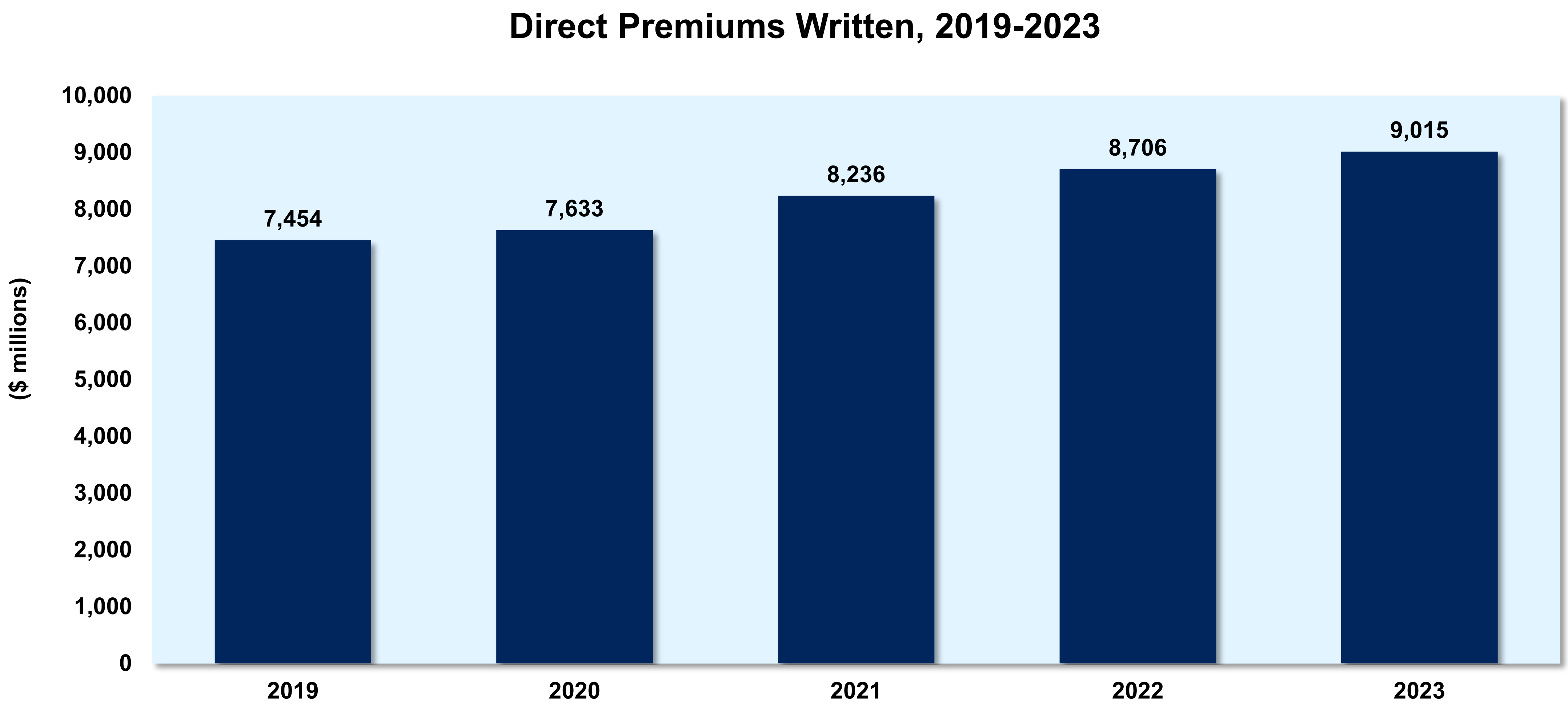
US MPL Composite Underwriting Results

2023 Results:

- Premium growth moderated. Improved direct written premium for the composite was up 3.6% to approximately $9. billion, after rising 5.7% in 22 and 7.9% in 2021. Rising rates began to wane and less top line growth coupled with increasing loss costs and expenses, and the increase in frequency of higher severity claims resulted in an increase in the combined ratio year over year.

- Loss and LAE ratio increased to about 79%, while underwriting expenses increased 1.3% to 24%, likely impacted by economic inflation. The segment's loss and LAE ratio rose slightly but remained below its five-year average. Loss experience reflected a reduction in reported favorable prior year loss reserve development.
- In addition, there was a slight increase in the policyholder dividend ratio (up for the first time in five years), resulting in a combined ratio of 105.3.
- The deterioration in the CR year-over-year was minimal, and certainly not at the composite's high-water mark of approximately 114 that we saw in 2019.

US MPL Composite – Direct Premiums Written



Source: Best link

MPL Composite – Financial Ratios

Financial Ratios, 2019-2023					
	2019	**2020**	**2021**	**2022**	**2023**
Loss & LAE Ratios	85.0	85.1	83.2	78.4	79.0
Underwriting Expense Ratios	25.2	24.5	24.2	22.7	24.0
Policyholder Dividend Ratio	3.8	3.2	2.6	2.2	2.3
Combined Ratio After Dividends	114.0	112.8	110.0	103.2	105.3

Note: Results shown are for the companies in the MPL special composite whose financials were received by AM Best as of April 9, 2024. Results of companies whose financials have not yet been received are excluded from prior and current years' results.
Source: AM Best Data and Research

US MPL Composite Underwriting Results

Additionally, if you look at the US MPL Composite original AY combined ratio and the original CY combined ratio over the last ten-year period, we can see we are getting to the point where the AY and CYs are getting closer to intercepting even though this has leveled off since 2019.

The difference the composite enjoyed in prior years is declining because the segment is not releasing as much favorable development into earnings.

Loss cost inflation and waning favorable reserve development forced many MPL insurers to adjust their pricing the past several years with pricing actions more pronounced in the hospital and senior care segments, which have higher loss ratios.

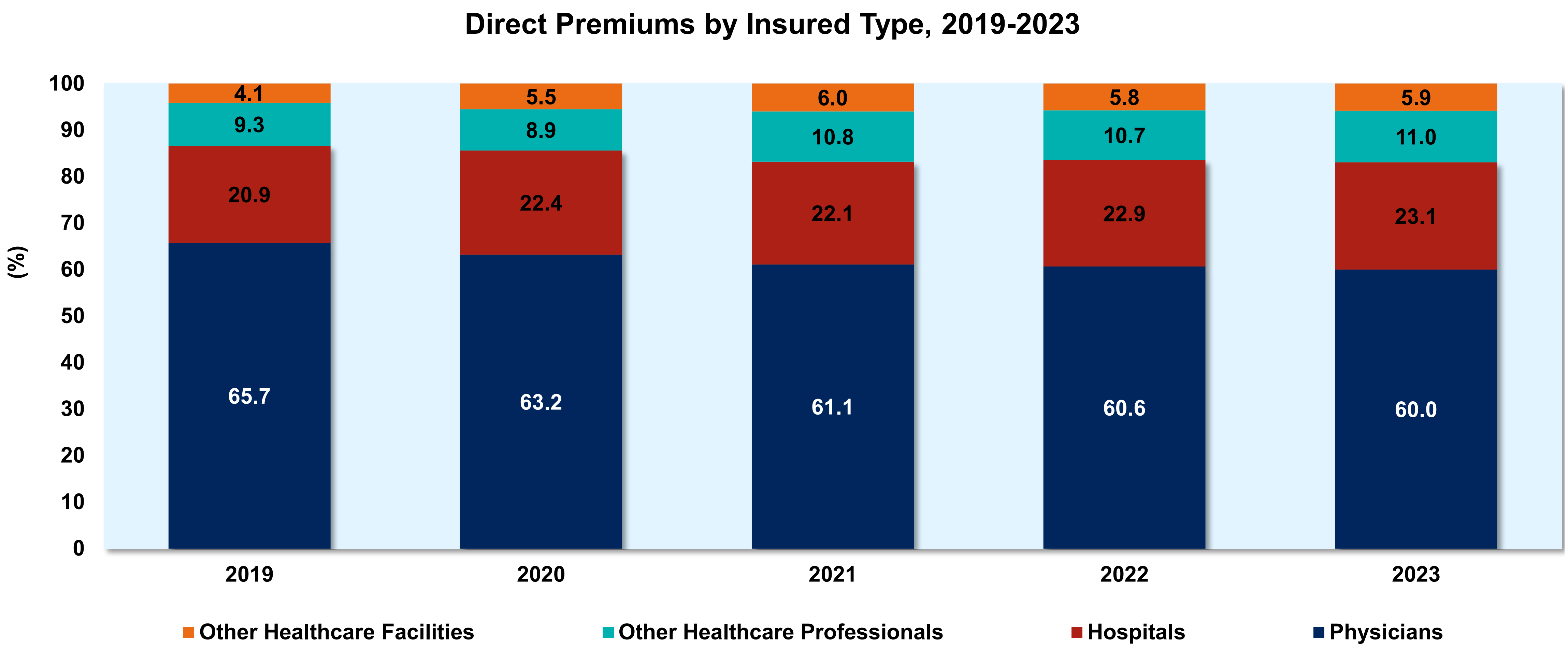
MPL Industry – Incurred Loss & DCC Ratios

US MPL Composite – Combined Ratios, 2013-2023

Accident Year	Original Accident Year Combined Ratios	Original Calendar Year Combined Ratio	Difference
2013	114.9	92.7	22.2
2014	116.1	93.2	22.9
2015	118.2	98.3	19.9
2016	118.1	102.8	15.3
2017	117.2	101.2	16.0
2018	117.8	102.3	15.5
2019	120.2	114.1	6.1
2020	118.3	112.5	5.8
2021	116.0	110.1	5.9
2022	110.1	103.5	6.6
2023	111.6	105.4	6.2

Note: The 2012-2013 and 2016-2022 data reflects the results of all companies in the MPL composite for those years. 2014 data excludes MedPro; 2015 data excludes Medpro, MCICVermont, and TX JUA; 2018 data excludes the effects of MLMIC's LPT that year; and 2022 data includes companies whose statements have been received by AM Best as of April 9, 2024.

MPL Composite – DPW By Insured Type



Source: Best link

US MPL Composite Investment Returns

- Essentially, while overall MPL premium was relatively flat in 2023, financial results were bolstered by favorable net investment income. Net investment income rose for the second year, with particularly strong growth of 41.6% in 2023 as yields rose to 3%.

- The MPL composite's net income grew by 6.9% to $827 million driven by the significant increase in net investment income following the repositioning of many companies' investment portfolios to take advantage of higher interest rates. MPL Insurers have historically maintained conservative investment portfolios, with most holdings consisting of fixed-income securities.

- Gains in investment results offset larger underwriting losses and declines in realized capital gains.

- The 6.2% return in invested assets in 2023 reflected a $1.1 billion unrealized capital gain driven by the rebound in the equity markets

- Overall, the segment generated approximately $2.9 billion in pretax operating income and $3.9 billion in net income from 2019 to 2023 due to investment results.

US MPL Composite – Key Income Statement Data

Key Income Statement Data ($ millions)					
	2019	2020	2021	2022	2023
Premiums Earned	5,575	5,635	6,138	6,516	6,571
Loss & LAE Incurred	4,741	4,798	5,107	5,107	5,332
Other Underwriting Expense	1,432	1,387	1,513	1,512	1,644
Policyholder Dividends	214	179	157	141	157
Underwriting Income	-812	-729	-639	-244	-382
Investment Income Earned	1,007	897	828	899	1,273
Other Income	55	70	71	80	95
Pre-Tax Income/Loss	251	238	260	735	986
Realized Gains/Loss	478	418	711	82	6
Income Tax	46	-32	48	44	164
After-Tax Income	682	687	923	773	827

US MPL Composite Capital and Surplus

- Net investment income and substantial unrealized capital gains were the primary driver for the 9.2% growth in policyholders' surplus in 2023 to $21.8 billion.
- In 2023, growth in surplus more than offset the 2.7% growth in net premiums written and 1.8% growth in loss and LAE reserves.
- The 1.5 underwriting leverage ratio remained in line with the prior year, indicating the MPL composite's solid capital position.
- Shareholder dividends, contributed capital, premium rebates, discounts, and credits during the five-year period, were funded in part by the release of redundant reserves for prior accident year claims and did not have much of an impact on the increase in surplus.
- AM Best's analysis considers the strong capital position of most of the rated MPL insurers as well as positive cashflows, additional sources of liquidity, sound risk management, and the ability to hold fixed-income assets to maturity, the primary drivers of significant balance sheet strength.

MPL Composite – Key Balance Sheet Data

Key Balance Sheet Data, 2020-2023 ($ millions)				
	2020	2021	2022	2023
Cash & Short-Term Investments	4,678	4,836	4,034	5,235
Bonds	23,404	24,927	25,252	26,273
Common Stocks	7,923	9,591	8,588	8,548
Other Invested Assets	2,342	3,531	4,210	3,802
Other Assets	5,468	5,022	5,197	4,670
Total Assets	43,815	47,523	45,845	48,528
Loss & LAE Reserves	17,246	18,677	19,220	19,558
Other Liabilities	6,871	7,039	6,593	7,121
Total Liabilities	24,117	25,745	25,864	26,704
Policyholder's Surplus	19,698	21,778	19,981	21,824
Total Liabilities and Surplus	43,815	47,523	45,845	48,528

US MPL Composite Evolving Risks

Identified Risks Include:

- Rising claims costs due not only to economic inflation but also social inflation.
- Tort reform challenges as reforms have been weakened or loosely enforced in more jurisdictions every year. Could result in runaway verdicts and excessive life care plans.
- Cyber, as healthcare is one of the most vulnerable industries to cyber attacks.
- Political trends in certain states following the US Supreme Court's Dobbs decision and the threat to criminalize long-standing standard of care practices. Market uncertainty in the upcoming elections and government funding considerations.
- Staffing and supply shortages, overloaded hospitals, caregiver burnout, early retirement, scope creep.
- Third-Party litigation financing, not as pronounced in the MPL industry, but growing, and controversial, as the risk is largely unregulated, owing to transparency of funding arrangements and attention drawn to interest rates.
- AI and the clarity needed to where the liability lies in the event of a diagnosis or treatment error.

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US MPL Segment Innovation

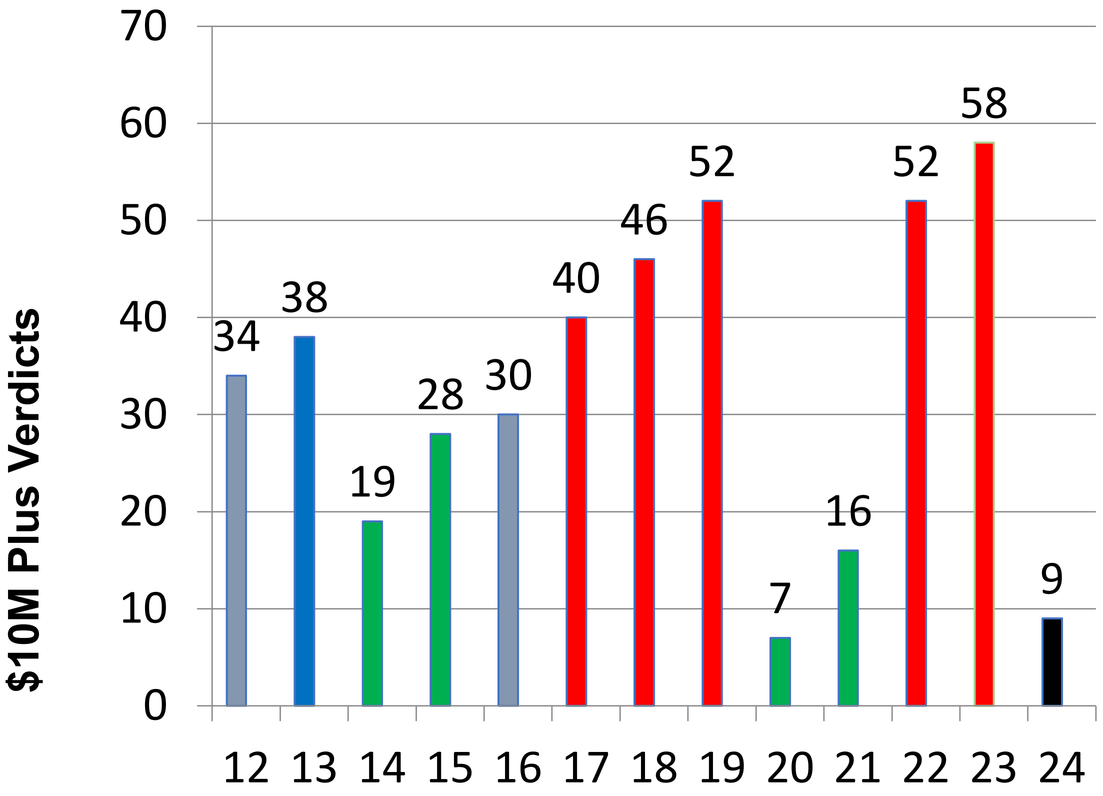
- Cultural shift towards innovative transformation

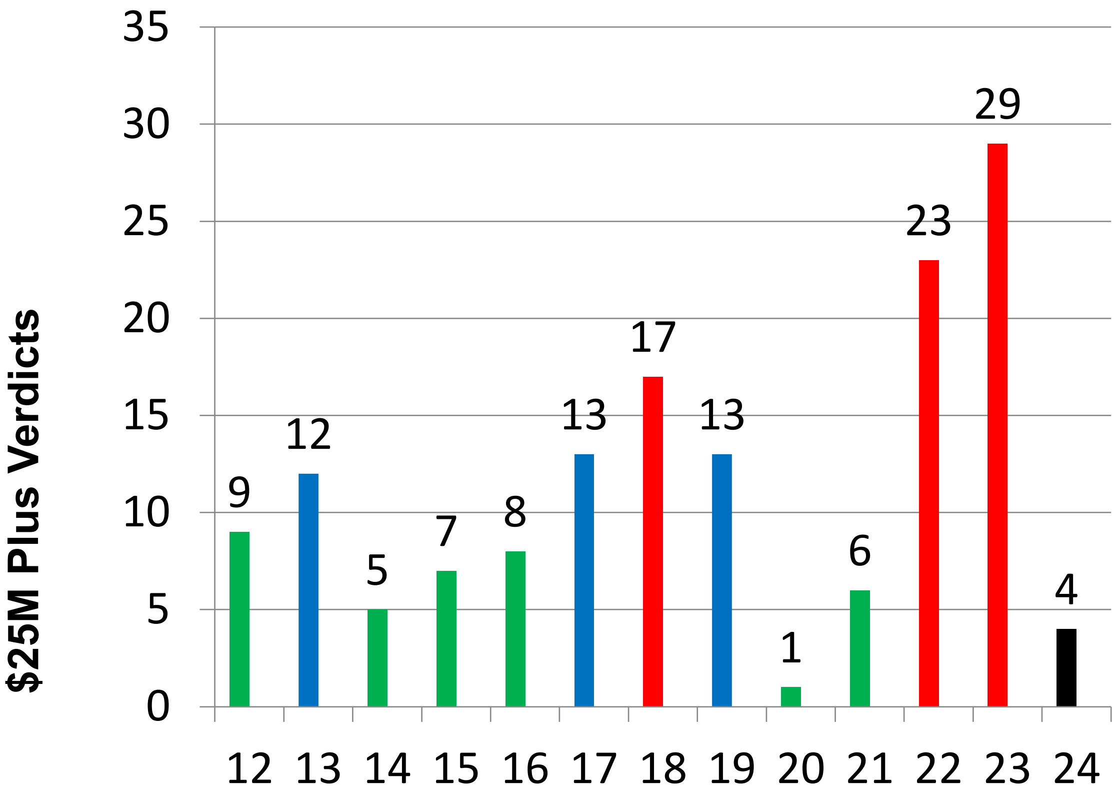
- Vast majority of MPL companies continue to score in the “moderate” assessment level but some companies breaking away form the pack

- Innovative solutions we are seeing (not across the board):
  - Machine learning & natural language processing to analyze vast amounts of healthcare data
  - Growing use of predictive analytics and models in underwriting and claims
  - Quick quoting with straight-through processing for select lower-risk segments
  - Partnerships with digital healthcare applications to provide advice/nudges at point of care
  - Leveraging AI-powered data analytic tools to manage legal spend

Med Mal Verdict Data > $10M and > $25M

Based on data known as of 2/29/2024





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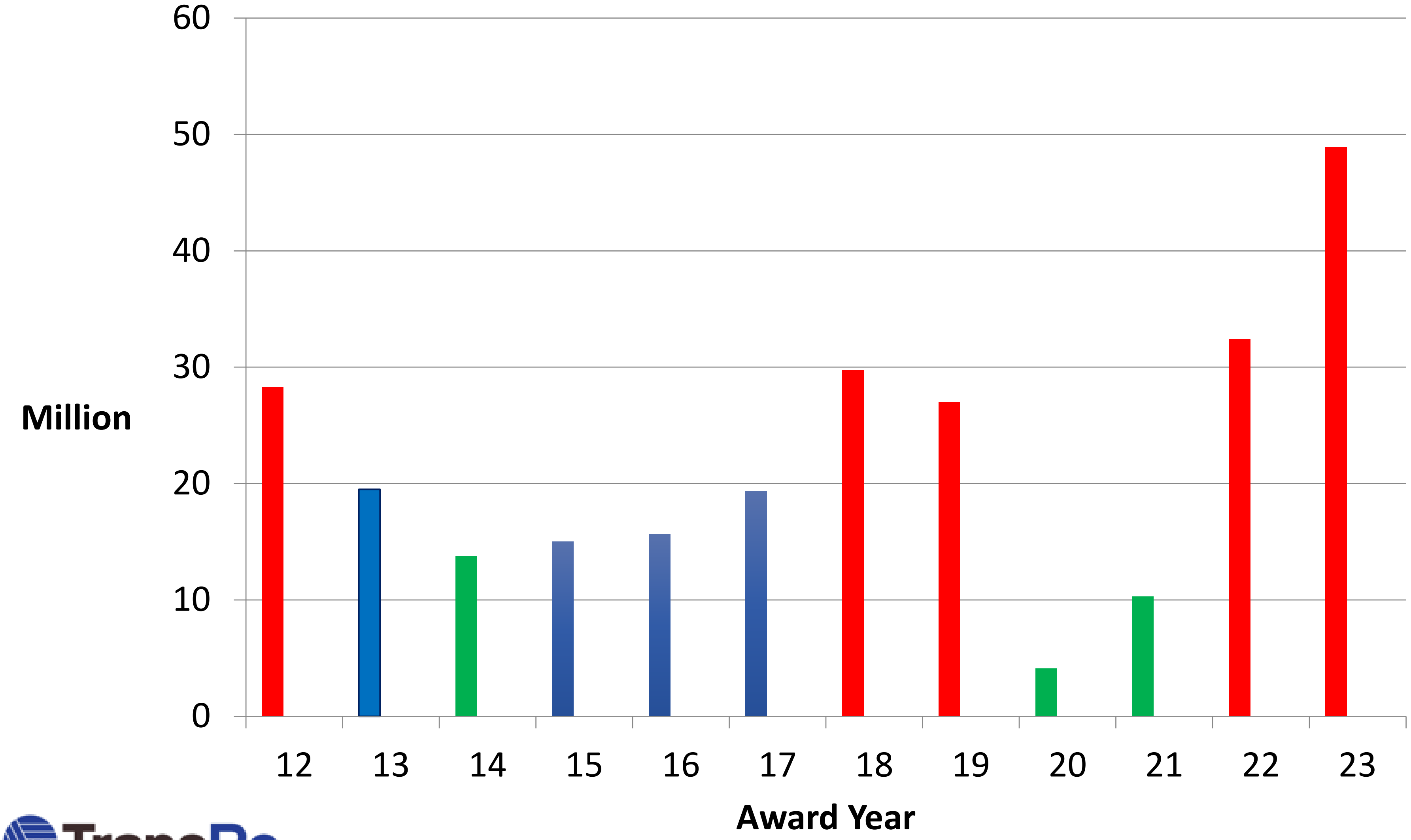
Average of Top 50 Med Mal Verdicts

Based on data known as of 2/29/24



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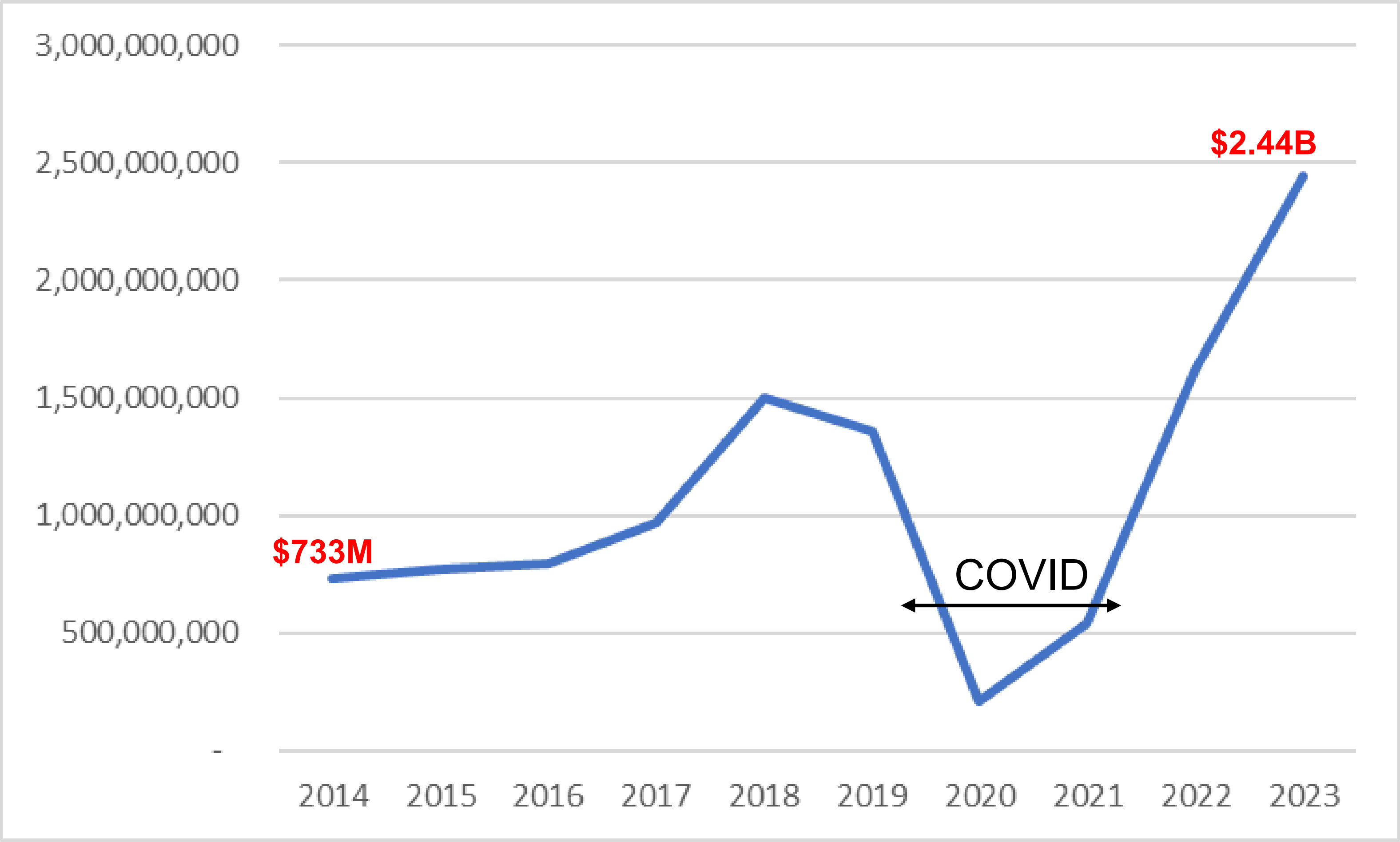
Sum of 50 Largest Verdicts

based on data known as of 2/29/24



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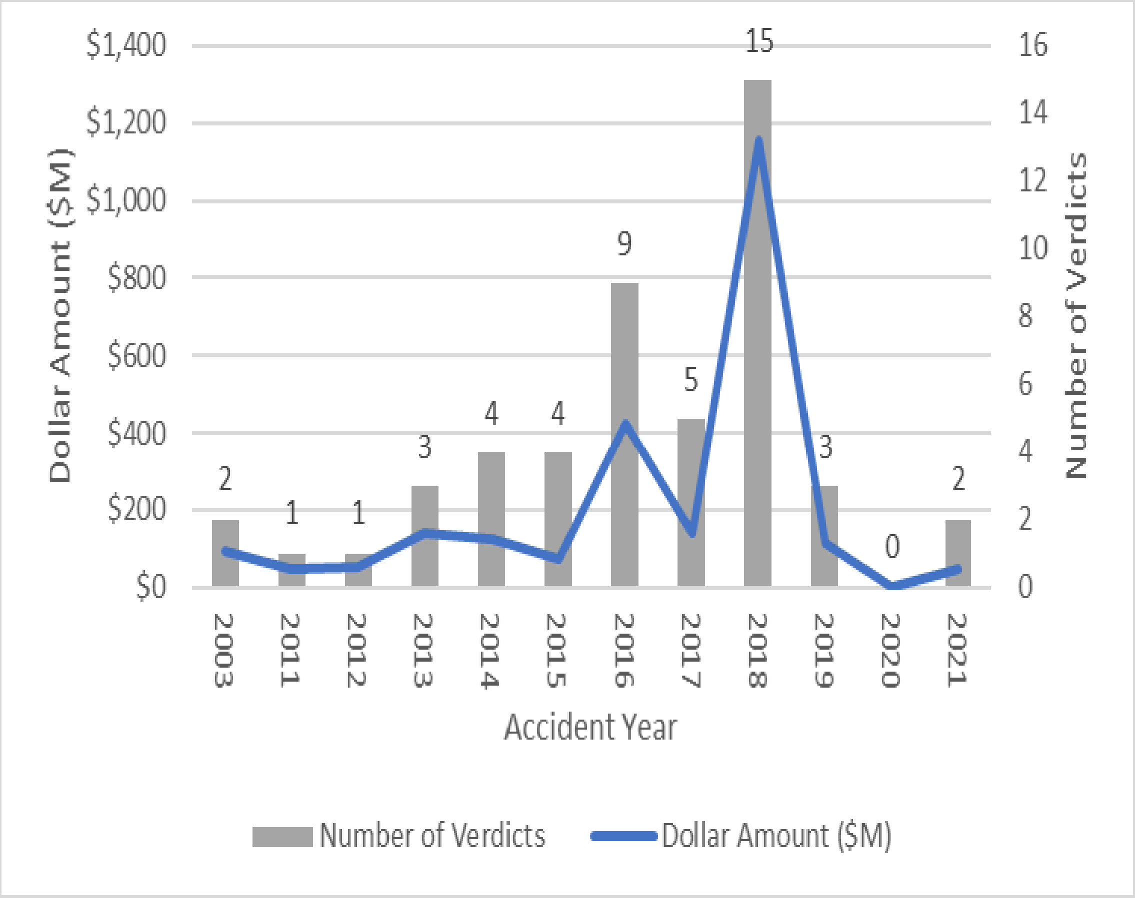
Sum of 50 Largest 2023 Verdicts – Recast by AY

based on data known as of 2/29/24



AY	# Verdicts	$Verdicts
2021	2	$45.6M
2020	0	$0
2019	3	$114.7M
2018	15	$1.15B
2017	5	$138.1M
2016	9	$424.8M
2015	4	$75.5M
2014	4	$125.5M
2013	3	$140.9M
2012	1	$52M
2011	1	$48M
2003	2	$95.5M

Undetermined: 1 verdict with AY unknown

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But These Are “Just” Verdicts….Right?

- Verdicts comprise a minimal percentage of claim outcomes (5%?), but heavily influence settlement strategy on claims which are not tried, including high-low discussions
- Verdicts can easily be used by plaintiff counsel to anchor during mediation; concern mediators can be subtly influenced
- Verdicts play a role in desensitizing jurors to the value of money
- Ever-increasing verdicts impact the risk tolerance of C-Suite
- The question everyone wants to know…

How Much Is Actually Paid On Claims That Are Lost At Trial?

Using TransRe data of verdicts in 2023 which have since settled, and where cumulative verdicts totaled approx. $1***B***, approximately **42%** of the verdict has been paid in settlement. Is this a new level to expect?

In general, our experience is that somewhere in the mid 20% range is ultimately expended in global settlements once all claims are resolved.

So…let's assume 25%...

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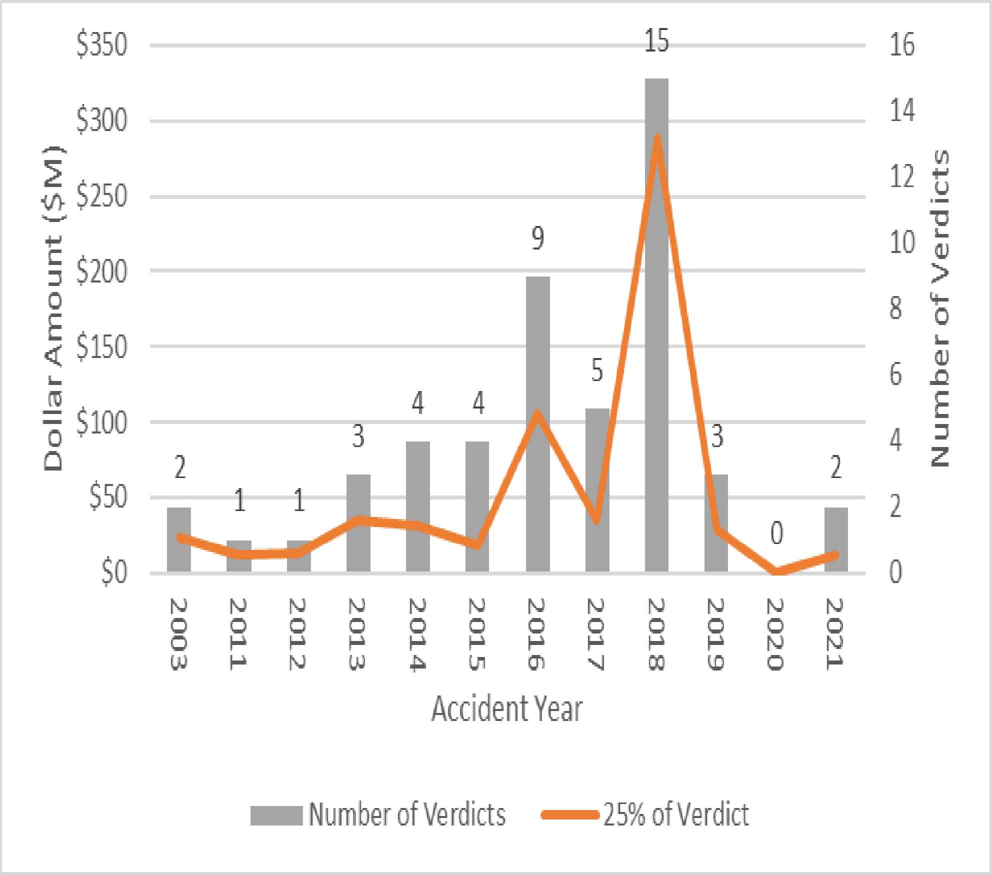
What if the 50 Top Verdicts in 2023 Settle at 25% of Verdict?

based on data known as of 2/29/24



AY	# Verdicts	$Verdicts
2021	2	$11.4M
2020	0	$0
2019	3	$28.7M
2018	15	$288.5M
2017	5	$34.5M
2016	9	$106.2M
2015	4	$18.9M
2014	4	$31.4M
2013	3	$35.2M
2012	1	$13M
2011	1	$12M
2003	2	$23.9M

Undetermined: 1 verdict with AY unknown

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