

THE MEDICAL PROTECTIVE COMPANY

TEXAS

PHYSICIANS AND SURGEONS

ACTUARIAL TORT REFORM MEMORANDUM

This memo explains our position in reducing our rates to reflect the potential impact of HB 4, effective on September 1, 2003, and Proposition 12, passed by the Texas Electorate on September 13, 2003. Exhibit I displays our rate need in the state of Texas of 27% for occurrence and 41% for claims made. These indications have been reduced by 6.5% to reflect potential savings from tort reform.

As outlined in a letter dated September 24, 2003, from Philip O. Presley, Chief Actuary, we quantified the impact that the three provisions in this letter would have on our rates.

- **Reduction in the interest rate to measure pre- and post-judgment interest (Article 6).**

We have no data to calculate the impact of this provision. We believe that adjustment of the interest rates in pre- and post-judgment constitute an insignificant effect on our overall book.

- **Limitations on non-economic damages (Article 10, Subchapter G).**

Non-economic damages are a small percentage of total losses paid. Capping non-economic damages will show loss savings of 1.0%. Please refer to Tort Reform Exhibit A.

- **Periodic payment of future damages in cases where the present value of future damages exceeds \$100,000 (Article 10, Subchapter K).**

This provision does not apply to damages already incurred and is a function of total damages paid and policy limits. Tort Reform Exhibit B illustrates that the estimated loss savings from this provision will be 1.1%.

Adding the three pieces gives us less than 3% in estimated savings in losses. When applied to premium rates, the savings will be even less. There are additional considerations as to why the potential impact of tort reform may be less than anticipated:

- 1 We write policy limits lower than some other companies. Therefore, our potential savings will be less.

Frequency has risen significantly this year. It will be at least a couple of years before we can tell how much can be attributed to filings to beat the September deadline and how much is a true increase in frequency.

3. The savings estimated by the 1996 Tort Reform did not materialize completely.
4. With big dollars at stake, plaintiff attorneys will find ways to shift costs from non-economic to economic damages.
5. It is unknown how the judicial system will react to the provisions. Medical malpractice victims with serious injuries who will be receiving less non-economic damages than before may be looked upon very favorably by juries and/or judges.
6. There may be "cap-busters." For example, in Jenkins v. Patel, Michigan Court of Appeals, 4/1/2003, it was ruled that the cap on non-economic damages does not apply to wrongful death cases.

The most significant reason for no further reduction is the uncertainty. Potential savings will not be seen for at least a couple of years. If these savings do not materialize we will have provided valuable services to physicians in Texas at inadequate rates. So we can continue our service we cannot reduce our rates more than 6.5%. In fact, because we are reducing our rates before savings can materialize we are putting ourselves at risk with possible inadequate rates. We view the 6.5% decrease in our indication as an act of faith with the Department and reflects a middle ground between the company's view of the impact of tort reform and the expected tort reform savings reflected in other estimates.

Each year we reevaluate our book, and fewer or greater savings will materialize in our data. We can then reflect any difference in future rate changes.

The Medical Protective Company

Tort Reform Exhibit A
\$250,000 Cap (Secure)

To estimate savings on a \$250,000 cap on non-economic damages for 2004, we stratified our losses into different layers. The losses are then projected to the year 2004. We then estimated what portion in each layer would be considered non-economic damages. The losses eliminated were calculated by subtracting \$250,000 from column (2) and dividing by the midpoint of the payment range.

<u>Payments</u>	<u>(1) % of Projected Losses in Layer</u>	<u>(2) Losses Estimated to be Non-Economic</u>	<u>(3) % Eliminated by \$250,000 Cap</u>	<u>(4) (1) x (3)</u>
1-\$100,000	10.0%	0	0.0%	0.0%
\$100,001-\$200,000	14.9%	0	0.0%	0.0%
\$200,001-\$500,000	36.6%	0	0.0%	0.0%
\$500,001-\$750,000	24.1%	100,000	0.0%	0.0%
\$750,001-\$1,000,000	8.4%	280,000	3.4%	0.3%
Over \$1,000,000	6.0%	400,000	12.5%	0.8%
Estimated Loss Savings				1.0%

The Medical Protective Company

Tort Reform Exhibit B
 Periodic Payments of Future Damages

To estimate savings on structured payments for 2004, we stratified our losses into different layers. The losses are trended to the year 2004. We then estimated the proportion of each layer would be paid in a lump sum. The remainder of each layer would be the part eligible for a structured payment.

<u>Payments</u>	(1) <u>% of Projected Losses in Layer</u>	(2) <u>% of Losses Paid as Cost to Date</u>	(3) <u>% of Losses Paid for Future Benefits 1.0 - (2)</u>	(4) <u>(1) x (3)</u>
1-\$100,000	10.0%	100%	0%	0.0%
\$100,001-\$200,000	14.9%	95%	5%	0.7%
\$200,001-\$500,000	36.6%	75%	25%	9.2%
\$500,001-\$750,000	24.1%	50%	50%	12.1%
\$750,001-\$1,000,000	8.4%	35%	65%	5.5%
Over \$1,000,000	6.0%	20%	80%	4.8%
Total				32.2%

Using a sample of our own data, 93% of our losses are paid outside of court verdicts. These amounts would not be subject to the law and would not be subject to the structured payments provision:

If we assume that the proportion of cases that resolve outside verdict decreases to 85%, the remainder subject to structured settlements would be approximately:

$$32.2\% \times (1.0 - 85\%) = 4.83\%$$

Discounting future payments at 5% over an average 10 year period, the savings on the future benefits is 22.8%. Therefore, the savings for losses for 2004 are estimated to be $4.83\% \times 22.8\% = 1.1\%$.