



FOURTH QUARTER 2013

Foresight: Interview with David Spiegler

BMS Group Executive Vice President & Chief Actuary, David Spiegler, provides some updates on key trends in the medical professional liability sector, and offers some insightful commentary on what's been happening.

IML: With redundant reserves nearly depleted, and fixed-income investments yielding meager returns, are MPL companies beginning to feel squeezed?

Spiegler: Yes. I would say that they are feeling somewhat squeezed—although probably not quite as much as you would expect. While reserves are less redundant than they were, certainly, it looks like there is still some room for them to release redundancies in the future. As they have released reserves on the older years, they have continued to put up conservative ultimates on the more recent years. So, our estimates show that there is still some room, barring a big increase in inflation, for them to release reserves going forward.

We saw reported losses during 2012 come in worse than what we had anticipated. There was more loss activity than expected, versus 2011, where losses came in much better than we had expected. This is something that PIAA [companies] should monitor closely to see if it's an aberration or a trend.

I think there are some red flags that managers have to look out for. But in general, the business still looks profitable—although much less profitable than a few years ago.

IML: Do you see ongoing keen competition in pricing?

Spiegler: We do see continued pricing pressure. But it hasn't really changed in the last couple years. It's been that way for two or three years now—perhaps even longer than that. The PIAA companies' results, while profitable, have decreased in profitability over the last five to six years. And their gross premiums have gone down quite a bit, from a peak of about \$6.6 billion, for all of the PIAA companies,

in 2006, to about \$5.3 billion in 2012. That has put pressure on their expense ratio, which has increased from less than 14% to more than 21% in that same time period.

So, there certainly have been warning signs. And the issue we continue to stress with our clients is: Will you correct these issues before they become a big problem, as they were in the late 1990s and early 2000s, where the corrections didn't start taking place until after the business was so unprofitable that there was significant stress on the whole industry?

IML: Why do companies resist changing their current course until it's late in the game?

Spiegler: This is opinion here, but I would say there are a couple of things. There's pressure from their client base, as their insured physicians increasingly shift to being employees of larger organizations, shrinking the potential universe of PIAA insureds. And then, they feel the need to keep up with their competitors, and to keep revenues up, and their expense ratio down. So they have to fight for business.

IML: Are companies continuing in the trend toward greater diversity in their investment portfolios?

Spiegler: We haven't seen a lot of companies straying too far from the fixed-income type of investment. Everyone is strapped in terms of investment yield, but no one has gone too crazy in terms of adding too much additional risk to their investment portfolio.

IML: Have there been any surprises in trends in frequency and severity?

Spiegler: No surprises. The frequency numbers are as we might have anticipated. We are watching it more closely this year because, as I said, 2012 came in worse than we were anticipating. We, like all of our clients, are monitoring it, to see if their string of reserve releases can continue.

IML: Have there been any recent advances in actuarial modeling?

Spiegler: There haven't really been any significant advances. But that being said, where modeling is right now, is very adequate to meet the demands in terms of analyzing the business.

IML: Has the increasing employment of physicians impacted what you are seeing in results, in any way?

Spiegler: The way it shows up in the results thus far is not as a change in loss trends, but as a change in exposure. Physicians that had been insured by PIAA companies are now part of hospitals' programs. And while part of the drop in premium over the last few years has been due to rate decreases, part of it has also been exposures moving out of the PIAA realm and into insured hospital programs.

IML: And you don't see any reason for that not to continue?

Spiegler: Not in the short term, barring some structural change in the industry. It looks like an ongoing trend. It hasn't gone as fast as some had expected, but it has been continual, and it has eroded the client base for our clients.

IML: And what about frequency and severity—staying the same as they were?

Spiegler: Yes. Severity is modest, and frequency has not increased. But, given that the exposure base is changing, that's something that has to be looked at closely.

IML: I have been reading that the influx of capital into the reinsurance market is distorting that market. Does this impact PIAA companies?

Spiegler: BMS does participate in the catastrophe market, where the impact is more direct. But among the reinsurers that support PIAA, it hasn't had a big impact, because the alternative capital has been almost exclusively catastrophe-driven.

IML: Are there any other developments in the MPL sector that you'd like to comment on?

Spiegler: I guess my main point here is that the results for these companies have been eroding over the last few years. Will companies react quickly enough, before it becomes a big problem?

IML: But what steps can they realistically take now—increase their prices?

Spiegler: That's the issue. Even if you want to increase your prices, if the market is not cooperating, you end up potentially losing business that you may want to retain. So it's not any easy thing.

The key is to determine which business is priced properly, and which is not. And to be able to say no, sometimes.

IML: And what about M&A, for some companies, that may be the main source of profits?

Spiegler: Well, I'd say that M&A is a source of profits only to the extent that the underlying business being acquired is priced and underwritten properly.

But there are certainly several companies in particular that have been very aggressive in M&A. I don't expect that will stop. They're always on the outlook for new opportunities. This is how companies have been growing recently, by acquisition, as opposed to growing organically. But at the end of the day, the underlying business has to be priced properly.