PIAA Reserve and Profitability Update

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In our fourth annual review of the Physician Insurers Association of America ("PIAA") companies, BMS continues to look at:

1. how the profitability of member companies has changed over the past decade;
2. the profitability of their current business;
3. the level of redundancies in loss and loss adjustment expense reserves that has been released in recent years; and
4. how much redundancy remained as of December 31, 2013.

In our updated analysis of PIAA member company results as of year-end 2013, we will review how the reserve adequacy and profitability picture has changed since year-end 2012.

As with prior years' analyses, we have estimated the ultimate loss and defense cost containment ("DCC") expenses by report year (for claims-made business) and accident year (for occurrence business) for the PIAA member companies. So let us see how things look with the benefit of an additional year of history.

Market Share

The PIAA member companies account for about half of all MPL gross earned premium*:

Calendar Year	MPL Industry Total Gross EP ($000)	PIAA Total Gross EP ($000)	PIAA % of Total
2004	12,700,087	5,991,102	47.2%
2005	13,094,859	6,298,530	48.1%
2006	13,162,999	6,561,630	49.8%
2007	12,721,934	6,401,668	50.3%
2008	12,197,825	6,130,143	50.3%
2009	11,393,531	5,812,155	51.0%
2010	11,194,819	5,666,496	50.6%
2011	10,885,777	5,429,229	49.9%
2012	10,750,423	5,251,147	48.8%
2013	10,476,926	5,075,079	48.4%

*Note that this analysis includes only those companies that filed NAIC Annual Statements. There are several PIAA member companies that do not file Annual Statements, which could understate the PIAA market shares noted above.

The Current Picture

Estimated report year/accident year gross combined ratio for the PIAA member companies:

Calendar Year	Gross Earned Premium ($000)	Gross Ultimate Loss+DCC ($000)	Gross Ultimate Loss+DCC Ratio	Gross Other Expenses ($000)	Gross Other Expense Ratio	Estimated Gross Combined Ratio	Booked Gross Combined Ratio
2004	5,991,102	3,734,690	62.3%	777,561	13.0%	75.3%	74.0%
2005	6,298,530	3,743,507	59.4%	848,685	13.5%	72.9%	71.8%
2006	6,561,630	3,517,894	53.6%	864,940	13.2%	66.8%	66.3%
2007	6,401,668	3,663,512	57.2%	933,034	14.6%	71.8%	71.4%
2008	6,130,143	3,761,322	61.4%	961,449	15.7%	77.0%	77.3%
2009	5,812,155	3,671,539	63.2%	972,006	16.7%	79.9%	81.9%
2010	5,666,496	3,860,349	68.1%	1,087,851	19.2%	87.3%	92.1%
2011	5,429,229	3,943,525	72.6%	1,115,167	20.5%	93.2%	99.9%
2012	5,251,147	3,884,149	74.0%	1,105,305	21.0%	95.0%	105.2%
2013	5,075,079	4,147,800	81.7%	1,110,003	21.9%	103.6%	111.2%

From the table above, it can be concluded that PIAA member companies:

1. for the first time in ten years, have an estimated underwriting loss in 2013;
2. reached peak profitability in 2006;
3. have seen profitability decrease each year since 2006;
4. have seen gross premium drop by 23% since 2006;
5. have seen their expense ratio increase from 13.2% in 2006 to 21.9% in 2013; and
6. continue to carry relatively conservative reserves (as can be seen by comparing booked combined ratios to estimated combined ratios for 2008 through 2013).

Absent an increase in inflation not contemplated in the estimated ultimate losses, there appears to still be some cushion in carried reserves to allow for continued, though smaller, releases of reserves. However, the ability to improve future calendar year results, with the favorable development from prior years, may also have the impact of prolonging the current soft market.

And What About Those Reserve Redundancies?

The PIAA member companies have recognized net reserve redundancies in each calendar year from 2006 through 2013, totalling about $10.0 billion.

Calendar Year	Claims-Made ($000)	Occurrence ($000)	Total Net Redundancy Recognized ($000)
2006	408,669	77,318	485,987
2007	828,299	235,107	1,063,406
2008	1,179,683	220,694	1,400,377
2009	1,177,216	326,366	1,503,582
2010	1,076,617	375,146	1,451,763
2011	1,003,437	327,091	1,330,528
2012	1,039,187	541,232	1,580,419
2013	969,256	239,252	1,208,508
Total	7,682,364	2,342,206	**10,024,570**

As of 12/31/13, the PIAA member companies still maintain an estimated redundancy in gross reserves (about $1.5 billion) to cushion results in future calendar years, but much of total reserve redundancies have already been tapped. The trend of companies simultaneously releasing reserves on older years, while booking conservative reserve levels for the more recent years, continued in 2013.

Calendar Year	Estimated Gross Ultimate Loss+DCC ($000)	Gross Booked Loss+DCC @12/31/13 ($000)	Gross Implied Redundancy/ Deficiency ($000)
2004	3,734,690	3,657,960	(76,730)
2005	3,743,507	3,676,718	(66,789)
2006	3,517,894	3,486,108	(31,786)
2007	3,663,512	3,637,979	(25,533)
2008	3,761,322	3,776,720	15,398
2009	3,671,539	3,788,962	117,423
2010	3,860,349	4,128,986	268,637
2011	3,943,525	4,307,537	364,012
2012	3,884,149	4,416,512	532,363
2013	4,147,800	4,535,368	387,568
Total			**1,484,564**

In Conclusion

We have seen that 2013 continued the trend of significant reserve releases that began in 2005. Our analysis indicates that further reserve releases could materialize in the next couple of years. However, we estimate an underwriting loss for 2013, the first since 2003. As noted in our previous analyses, the challenge is whether the PIAA member companies can reverse the decreasing trend in profitability before the market returns to the highly unprofitable levels of the early 2000s. Furthermore, challenges such as the potential for unanticipated inflation in loss costs and the uncertain impact of the continued rollout of the Affordable Care Act on the MPL marketplace will confront the management teams of all MPL carriers.