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July 11, 2004

Commissioner Jose Montemayor
Chair, NAIC Property Casualty C Committee

Re: Discussion of Investment Income in Med Mal Report

Dear Jose:

I will try one last time to demonstrate that reduced investment income was a significant factor – along with other factors, most notably increased claim costs – that caused a dramatic increase in med mal rates in 2001 and 2002.

The latest version of the investment income section of the med mal report relies upon an analysis of a subset of the med mal market to support the report's conclusion that decreased investment income was not a significant factor driving med mal rate increases. It is unclear why the report relies on this subset when there are ready sources of data describing the entire med mal market.

The first source is the Insurance Expense Exhibit which breaks out medical professional liability as a separate line of insurance and which includes investment income from operations and investment income from surplus. These values result from an allocation – loss reserves and premiums – that was thoroughly tested by David Eley and has been used for profitability analyses in Texas since the early 1980's. The IEE represents the entire admitted med mal market and is the best description of med mal experience. These data show that incurred losses grew substantially more than investment income declined, but the decline in investment income was significant – almost $1.3 billion. Certainly a decline of $1.3 billion must be considered a significant factor in this line of insurance. The figures below are in millions.

	2000	2002	Change
Incurred Losses	$7,234	$10,805	$3,570.2
Total Inv. Income	$3,903	$2,627	-$1,275.8

Another source is the NAIC Profitability Report by State by Line which also provides premium, loss and investment income experience for the med mal line by year. We have already provided you these data which show that med mal insurers received about 48 cents of investment income per dollar of earned premium through the 1990's and this figure declined to 20 cents for 2002. Again, a reduction of 28 cent of revenue per dollar of earned premium is reasonably considered a significant factor.

A third source is *Best's Aggregates and Averages*, which includes an analysis of *Medical Malpractice Predominating Organizations.* I include this source because a copy of one of these pages was distributed prior to the last phone call. From 2000 (63 organizations) to 2002 (55 organizations), incurred losses increases by $66 million or 2%, while investment income decreases by $840 million or 50%. Based on these data, any reasonable person would conclude that the decrease in investment income was a significant factor driving up med mal rates in 2002. The figures below are in millions.

	2000	2002	Change
Incurred Losses	$4,191.0	$4,257.0	$66.0
Total Inv. Income	$1,669.3	$830.5	-$838.8
Net Inv. Income	*$1,288.8*	*$1,051.6*	
Realized Cap Gain	*$380.5*	*-$221.1*	

Sincerely,

Birny Birnbaum
Executive Director