

REPORT ON EXAMINATION
OF
PHYSICIANS INSURANCE COMPANY
DEERFIELD BEACH, FLORIDA
AS OF
DECEMBER 31, 2011

BY THE
FLORIDA OFFICE OF INSURANCE REGULATION

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January 4, 2013

Kevin M. McCarty
Commissioner
Office of Insurance Regulation
State of Florida
Tallahassee, Florida 32399-0326

Dear Sir:

Pursuant to your instructions, in compliance with Section 624.316, Florida Statutes, Rule 690-138.005, Florida Administrative Code, and in accordance with the practices and procedures promulgated by the National Association of Insurance Commissioners (NAIC), we have conducted an examination as of December 31, 2011, of the financial condition and corporate affairs of:

**PHYSICIANS INSURANCE COMPANY
361 E. HILLSBORO BLVD
DEERFIELD BEACH, FLORIDA 33441**

Hereinafter referred to as, the "Company". Such report of examination is herewith respectfully submitted.

SCOPE OF EXAMINATION

This examination covered the period of January 1, 2007, through December 31, 2011. The Company was last examined by representatives of the Florida Office of Insurance Regulation (Office) as of December 31, 2006. This examination commenced with planning at the Office on September 24, 2012, to September 28, 2012. The fieldwork commenced on October 1, 2012, and concluded as of January 4, 2013.

This financial examination was a statutory financial examination in accordance with the Financial Condition Examiners Handbook, Accounting Practices and Procedures Manual and annual statement instructions promulgated by the NAIC as adopted by Rules 69O-137.001(4) and 69O-138.001, Florida Administrative Code, with due regard to the statutory requirements of the insurance laws and rules of the State of Florida.

The Financial Condition Examiners Handbook requires that the examination be planned and performed to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company including corporate governance, identifying and assessing inherent risks within the Company, and evaluating system controls and procedures used to mitigate those risks. An examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation and management's compliance with Statutory Accounting Principles and annual statement instructions when applicable to domestic state regulations.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process.

This report of examination is confined to significant adverse findings, a material change in the financial statements or other information of regulatory significance or requiring regulatory action. The report comments on matters that involved departures from laws, regulations or rules, or which were deemed to require special explanation or description.

SUMMARY OF SIGNIFICANT FINDINGS

Current Exam Findings

There were no material findings or exceptions noted during the examination as of December 31, 2011.

Prior Exam Findings

There were no findings, exceptions or corrective action to be taken by the Company for the examination as of December 31, 2006.

SUBSEQUENT EVENTS

Subsequent to the examination date, on May 2, 2012, the Office approved the indirect acquisition of the Company by Texas Medical Liability Trust (Texas Medical), a Texas healthcare liability claims trust, pursuant to the terms and conditions of Consent Order No. 125138-12-CO. As a result, Texas Medical owns 100% of the Company's common stock. The following changes have been made to the management of the Company subsequent to the examination date.

Directors

Name and Location	Principal Occupation
Charles R. Ott, Jr. Austin, Texas	Chief Executive Officer Texas Medical Liability Trust
Daniel R. O'Neal Deerfield Beach, Florida	President Physicians Insurance Company
Pamela N. Browning Deerfield Beach, Florida	Chief Operating Officer Physicians Insurance Company
Vincent L. Kasch Austin, Texas	Treasurer Texas Medical Liability Trust
Robert D. Donohoe Austin, Texas	Senior Vice President and Secretary Texas Medical Liability Trust

On May 1, 2012, the Company's bylaws were restated and amended. Pursuant to the amended bylaws, the Board appointed the following senior officers:

Senior Officers

Name	Title
Charles R. Ott, Jr.	Chief Executive Officer
Daniel R. O'Neal	President
Pamela N. Browning	Chief Operating Officer
Walter T. Brysh	Chief Financial Officer
Vincent L. Kasch	Treasurer
Robert D. Donohoe	Senior Vice President and Secretary

Since its acquisition by Texas Medical Liability Trust, no internal committees have been established by the Company's Board of Directors.

HISTORY

General

The Company was incorporated as a stock property and casualty company in the State of Florida on January 31, 2003, and commenced business on March 7, 2003, as Physicians Insurance Company upon approval from the Office, the Company expanded its business into the State of Texas in 2005.

The Company was authorized to transact one line of business, Medical Malpractice, in Florida on February 26, 2003 and continued to be authorized to transact this line of business as of December 31, 2011.

The Articles of Incorporation and the Bylaws were not amended during the period covered by this examination.

Dividends to Stockholders

The Company did not declare or pay any dividends during the period of this examination.

Capital Stock and Capital Contributions

As of December 31, 2011, the Company's capitalization was as follows:

Number of authorized common capital shares	500,000
Number of shares issued and outstanding	400,000
Total common capital stock	\$1,000,000
Par value per share	\$2.50

As of December 31, 2011, 100% of the Company's issued and outstanding shares of common stock were owned by PIC Group, LLC, a Florida limited liability corporation. Daniel R. O'Neal, Chief Executive Officer, indirectly owned approximately 87% of PIC Group, LLC.

Surplus Notes

The Company did not have any surplus notes during the period of this examination.

Acquisitions, Mergers, Disposals, Dissolutions, and Purchase or Sales Through Reinsurance

On December 7, 2007, the Office approved the acquisition by PIC Group, LLC with 100 percent of the issued and outstanding shares of the Company.

The Company had no other acquisitions, mergers, disposals, and purchase or sales through reinsurance during the period of this examination.

CORPORATE RECORDS

The recorded minutes of the Board of Directors (Board) and certain internal committees were reviewed for the period under examination. The recorded minutes of the Board adequately documented its meetings and approval of Company transactions and events, in compliance with the NAIC Financial Condition Examiners Handbook adopted by Rule 69O-138.001, Florida Administrative Code and including the authorization of investments as required by Section 625.304, Florida Statutes.

Conflict of Interest

The Company's conflict of interest statements were reviewed.

MANAGEMENT AND CONTROL

Management

The directors were appointed annually in accordance with Section 628.231, Florida Statutes.

Directors serving as of December 31, 2011, were:

Directors

Name and Location	Principal Occupation
Daniel R. O'Neal Deerfield Beach, Florida	Chief Executive Officer Physicians Insurance Company
Pamela N. Browning Deerfield Beach, Florida	Chief Operating Officer Physicians Insurance Company
Walter T. Brysh Deerfield Beach, Florida	Chief Financial Officer Physicians Insurance Company
Christopher J. Waterson St. Johns, Michigan	Director Physicians Insurance Company
Cristy B. Delahaye Heck Baton Rouge, Louisiana	Financial Consultant Heck Industries

The Board in accordance with the Company's bylaws appointed the following senior officers:

Senior Officers

Name	Title
Daniel R. O'Neal	Chief Executive Officer
Pamela N. Browning	Chief Operating Officer
Walter T. Brysh	Chief Financial Officer

See officers and directors serving as of the date of this examination in the Subsequent Events section of this report.

The Company's Board appointed two internal committees. Following were the principal internal board committees and their members as of December 31, 2011:

Audit Committee

Walter T. Brysh
Christopher Waterson
Daniel O'Neal

Investment Committee

Walter T. Brysh
Christopher Waterson
Daniel R. O'Neal

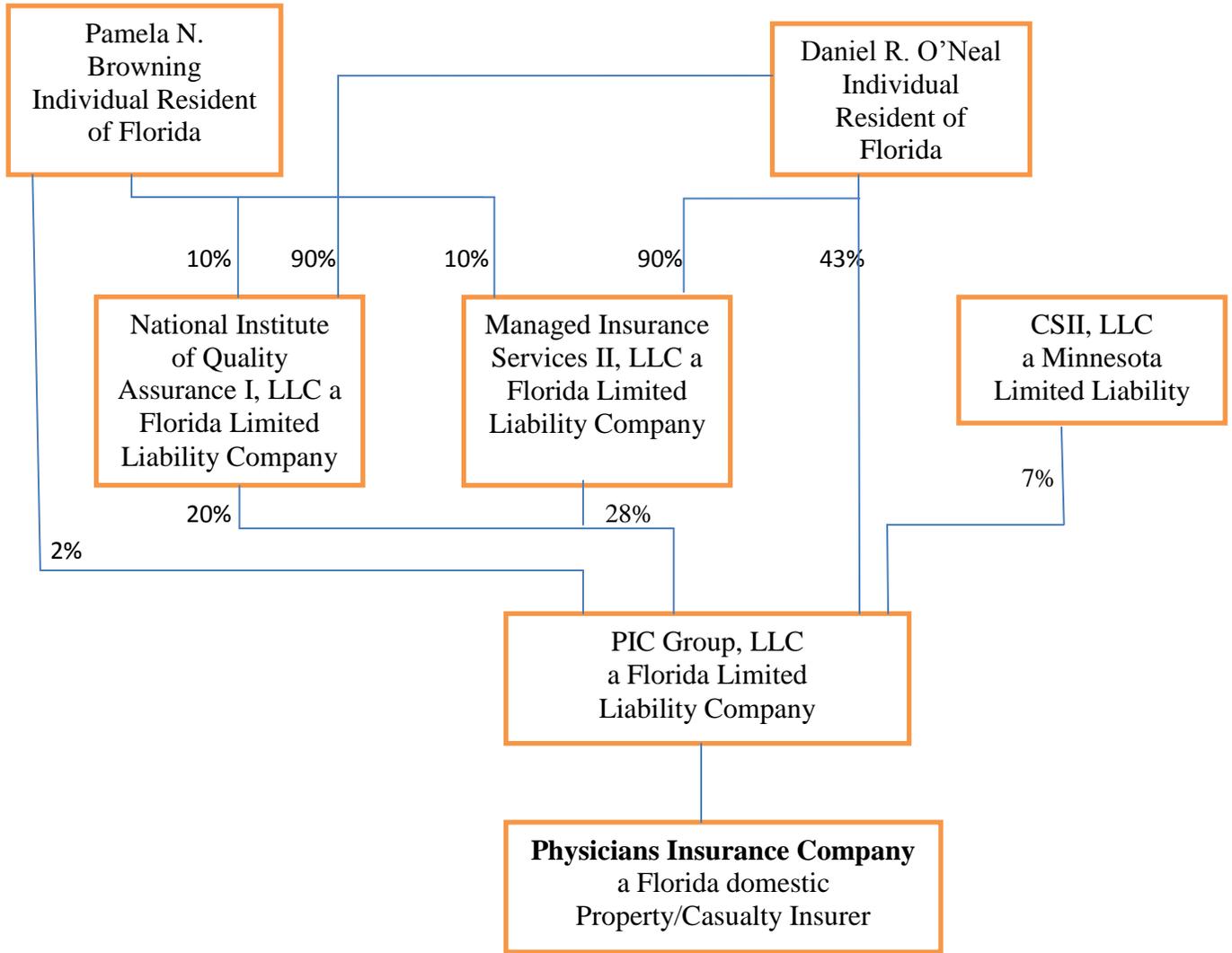
Affiliated Companies

The Company was a member of PIC Group, LLC, an insurance holding company system as defined by Rule 69O-143.045(3), Florida Administrative Code. The latest holding company registration statement was filed with the State of Florida on March 8, 2012, as required by Section 628.801, Florida Statutes, and Rule 69O-143.046, Florida Administrative Code.

An organizational chart as of December 31, 2011, reflecting the holding company system, is shown on the following page:

**PHYSICIANS INSURANCE COMPANY
ORGANIZATIONAL CHART**

DECEMBER 31, 2011



Schedule Y of the Company's 2011 annual statement provided a list of all related companies of the holding company group.

The following agreements were in effect between the Company and its affiliates:

Managing General Underwriting Agreement

During the period under examination, services were provided to the Company pursuant to a Managing General Underwriting Agreement (MGU), with its affiliate, Managed Insurance Service, LLC (Managed Insurance). The agreement became effective September 14, 2007, for a time period not to exceed five years, after which the Agreement became renewable annually; unless otherwise terminated within the guidelines of the Agreement. Pursuant to its agreement, Managed Insurance provided the following: solicitation of business; all usual and customary services to sub-producers, insureds and policyholders; binding risks in accordance with underwriting guidelines and pricing established by the Company; and policy issuance.

Managed Insurance was entitled to receive commissions at a rate of 25% based on Gross Written Premium due the Company on policies bound, written, renewed or continued. Fees incurred under this agreement during 2011 amounted to \$1,840,656.

Insurance Claim Risk Assessment Services Agreement

During the period under examination, the National Institute of Quality Assurance, LLC (National) assisted the Company by performing certain tests and analysis (collectively, "Services"), the results of which were utilized to assess physicians for future medical malpractice insurance claims, witness characteristics and preparation.

For services rendered, National assessed the Company an annual fee of \$450 per physician/insured. In addition, National received a commission of 1% to 5% of the prior year premium of the Company. Fees incurred under this agreement during 2011 amounted to \$760,691.

FIDELITY BOND AND OTHER INSURANCE

The Company maintained fidelity bond coverage up to \$500,000 with a deductible of \$25,000, which reached the suggested minimum as recommended by the NAIC.

In addition, as a member of the PIC Group, LLC, the Company was afforded the following insurance coverage: building, personal property, business income and errors and omissions coverage up to \$100,000 each claim; \$1,000,000 in the aggregate; employment practices, sub-limit \$100,000, with \$1,000,000 in the aggregate and commercial crime policy of \$500,000 per occurrence.

PENSION, STOCK OWNERSHIP AND INSURANCE PLANS

The Company offered an optional 401K plan to its employees. The Board of Directors made an annual decision to determine if the Company contributed to the 401K plan.

TERRITORY AND PLAN OF OPERATIONS

The Company was authorized to transact insurance in the states of Florida and Texas.

Treatment of Policyholders

The Company established procedures for handling written complaints in accordance with Section 626.9541(1) (j), Florida Statutes.

The Company maintained a claims procedure manual that included detailed procedures for handling each type of claim in accordance with Section 626.9541(1) (i) 3a, Florida Statutes.

COMPANY GROWTH

The Company's earned premiums remained relatively flat during the period under examination, an indication of increased competition. The decrease in underwriting and net income in 2011 was due to the increases in incurred losses and loss adjustment expenses. Surplus continued to grow despite declining net income.

Profitability of Company

The following table shows the profitability trend (in dollars) of the Company for the period of examination, as reported in the filed annual statements:

	2011	2010	2009	2008	2007
Premiums Earned	5,203,279	4,068,378	4,280,841	4,153,799	5,624,210
Net Underwriting Gain/(Loss)	268,667	503,435	90,202	170,906	1,019,311
Net Income	451,657	607,361	445,519	280,821	1,008,733
Total Assets	18,064,130	18,547,862	17,295,201	16,646,752	16,870,729
Total Liabilities	9,440,922	10,363,436	9,718,143	9,512,447	10,068,861
Surplus As Regards Policyholders	8,623,208	8,184,426	7,577,058	7,134,305	6,801,868

LOSS EXPERIENCE

As of December 31, 2011, net payments for incurred losses and loss adjustment expenses attributable to prior years insured events were \$2.2 million. Remaining reserves for prior years were \$3.5 million as a result of re-estimation of unpaid claims and claim adjustment expenses. Therefore, there was a \$1.0 million favorable prior year loss development trend. The Company had no significant one and two-year reserve development over the past five years.

REINSURANCE

The reinsurance agreements reviewed complied with NAIC standards with respect to the standard insolvency clause, arbitration clause, transfer of risk, reporting and settlement information deadlines.

Assumed

The Company did not assume any reinsurance during the period of this examination.

Ceded

The Company ceded risk on a Per Event Excess of Loss Reinsurance Contract dated March 1, 2007, which continued in effect during the period under examination. Risks were ceded to various authorized and unauthorized reinsurance companies. Letters of credit were obtained for all risks ceded to unauthorized reinsurers. All reinsurance contracts were negotiated and approved by the Company utilizing the services of Guy Carpenter as the reinsurance intermediary. The agreement provided a limit of \$1,800,000 excess of \$200,000 per event, with loss adjustment expenses covered as a part of the ultimate net loss.

The reinsurance contracts were reviewed by the Company's appointed actuary and were utilized in determining the ultimate loss opinion.

ACCOUNTS AND RECORDS

The Company maintained its principal operational offices in Deerfield Beach, Florida.

The Company's accounting records were maintained on a computer system designed and implemented by the Company.

An independent CPA audited the Company's statutory basis financial statements annually for the years 2007, 2008, 2009, 2010 and 2011 in accordance with Section 624.424(8), Florida Statutes. Supporting work papers were prepared by the CPA as required by Rule 69O-137.002, Florida Administrative Code.

The Company and non-affiliates had the following agreements:

Custodial Agreement

The Company entered into a custodial agreement with Northern Trust Bank which was dated and executed March 25, 2003. The agreement was in compliance with Rule 69O-143.042, Florida Administrative Code.

Independent Auditor Agreement

The Company contracted with an external independent CPA firm to perform the annual audit of its financial statements as required by Rule 69O-137.002 (7) (c), Florida Administrative Code.

INFORMATION TECHNOLOGY REPORT

Denise Mainquist, CISA, QSA, IT Specialist, performed an evaluation of the information technology and computer systems of the Company. Results of the evaluation were noted in the Information Technology Report provided to the Company.

STATUTORY DEPOSITS

The Company had the following assets deposited with the State of Florida as required by Section 624.411, Florida Statutes:

STATE	Description	Par Value	Market Value
FL	Cash	\$1,450,000	\$1,450,000
FL	Cash Interest	<u>95,844</u>	<u>95,844</u>
TOTAL FLORIDA DEPOSITS		<u>\$1,545,844</u>	<u>\$1,545,844</u>

FINANCIAL STATEMENTS PER EXAMINATION

The following pages contain financial statements showing the Company's financial position as of December 31, 2011, and the results of its operations for the year then ended as determined by this examination. No adjustments were made as a result of the examination.

PHYSICIANS INSURANCE COMPANY
Assets

DECEMBER 31, 2011

	Per Company	Examination Adjustments	Per Examination
Bonds	\$6,131,835		\$6,131,835
Real Estate:			
Properties			
occupied by Company	1,600,000		1,600,000
Cash and Short-Term Investments	7,723,299		7,723,299
Investment income due and accrued	72,382		72,382
Agents' Balances:			
Uncollected premium	2,135,629		2,135,629
Reinsurance recoverable	4,560		4,560
Current federal and foreign income			
taxes recoverable and interes thereon	119,502		119,502
Net deferred tax asset	243,632		243,632
Aggregate write-in for			
other than invested assets	33,291		33,291
Totals	<u>\$18,064,130</u>	<u>\$0</u>	<u>\$18,064,130</u>

PHYSICIANS INSURANCE COMPANY
Liabilities, Surplus and Other Funds

DECEMBER 31, 2011

	Per Company	Examination	Per
		Adjustments	Examination
Losses	\$4,887,058		\$4,887,058
Loss adjustment expenses	1,766,349		1,766,349
Taxes, licenses and fees	38,876		38,876
Unearned premium	2,658,242		2,658,242
Advance premium	66,236		66,236
Ceded reinsurance premiums payable	24,161		24,161
Total Liabilities	\$9,440,922	\$0	\$9,440,922
Common capital stock	\$1,000,000		\$1,000,000
Gross paid in and contributed surplus	4,000,000		4,000,000
Unassigned funds (surplus)	3,623,208		3,623,208
Surplus as regards policyholders	\$8,623,208	\$0	\$8,623,208
Total liabilities, surplus and other funds	\$18,064,130	\$0	\$18,064,130

PHYSICIANS INSURANCE COMPANY
Statement of Income

DECEMBER 31, 2011

Underwriting Income

Premiums earned	\$5,203,279
	Deductions:
Losses incurred	\$953,741
Loss adjustment expenses incurred	1,525,867
Other underwriting expenses incurred	2,455,004
Total underwriting deductions	\$4,934,612
Net underwriting gain or (loss)	\$268,667

Investment Income

Net investment income earned	\$220,808
Net realized capital gains or (losses)	25,627
Net investment gain or (loss)	\$246,435

Other Income

Finance and service charges not included in premiums	\$57,839
Aggregate write-ins for miscellaneous income	27,550
Total other income	\$85,389

Net income before dividends to policyholders and before federal & foreign income taxes	\$600,491
Dividends to policyholders	0
Net Income, after dividends to policyholders, but before federal & foreign income taxes	\$600,491
Federal & foreign income taxes	148,834
Net Income	\$451,657

Capital and Surplus Account

Surplus as regards policyholders, December 31 prior year	\$8,184,426
Net Income	\$451,657
Change in net deferred income tax	(74,315)
Change in non-admitted assets	61,440
Change in surplus as regards policyholders for the year	\$438,782
Surplus as regards policyholders, December 31 current year	\$8,623,208

A comparative analysis of changes in surplus is shown below.

PHYSICIANS INSURANCE COMPANY
Comparative Analysis of Changes in Surplus

DECEMBER 31, 2011

The following is a reconciliation of Surplus as regards policyholders between that reported by the Company and as determined by the examination.

Surplus as Regards Policyholders
December 31, 2011, per Annual Statement \$8,623,208

	<u>PER COMPANY</u>	<u>PER EXAM</u>	<u>INCREASE (DECREASE) IN SURPLUS</u>
ASSETS:			
No Adjustment			
LIABILITIES:			
No Adjustment			
Net Change in Surplus:			<u>0</u>
Surplus as Regards Policyholders December 31, 2011, Per Examination			<u><u>\$8,623,208</u></u>

COMMENTS ON FINANCIAL STATEMENTS

Liabilities

Losses and Loss Adjustment Expenses \$6,653,407

An outside actuarial firm appointed by the Board of Directors, rendered an opinion that the amounts carried in the balance sheet as of December 31, 2011, made a reasonable provision for all unpaid loss and loss expense obligations of the Company under the terms of its policies and agreements.

The Office consulting actuaries, Brent Sallay, FCAS, MAAA of Taylor-Walker & Associates, Inc., R. Glenn Taylor, ACAS, MAAA of Taylor-Walker & Associates, Inc. and Solomon Frazier, ASA, MAAA, Senior Actuarial Analyst, of Taylor-Walker & Associates, Inc., reviewed the loss and loss adjustment expense work papers provided by the Company and they were in concurrence with this opinion.

Capital and Surplus

The amount of capital and surplus reported by the Company of \$8,623,208, exceeded the minimum of \$4,000,000 required by Section 624.408, Florida Statutes.

CONCLUSION

The insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **Physicians Insurance Company** as of December 31, 2011, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's surplus as regards policyholders was \$8,623,208, which exceeded the minimum of \$4,000,000 required by Section 624.408, Florida Statutes.

In addition to the undersigned, Beverly A. Dale, CFE, CIE, FLMI, CPA, Examiner-In-Charge, Examination Resources, LLC, Rachelle Gowins, CFE, Supervising Examiner, Examination Resources, LLC and Sarah Lucibello, CPA, CFE, CIA, Examination Manager, Lewis & Ellis, Inc. participated in the examination. In addition, Brent Sallay, FCAS MAAA, consulting actuary of Taylor-Walker & Associates, Inc., R. Glenn Taylor, ACAS, MAAA, consulting actuary of Taylor-Walker & Associates, Inc. and Solomon L. Frazier, ASA MAAA of Taylor-Walker & Associates, Inc., Denise Mainquist, CISA, QSA, IT Specialist of Examination Resources, LLC, Steven Sigler, IT Manager of Examination Resources, LLC and Chibueze Alutu, CISA, Financial Examiner/Analyst II of the Office and Connie Hare, Financial Examiner/Analyst Supervisor of the Office also participated in the examination.

Respectfully submitted,

Mary M. James, CFE, CPM
Chief Examiner
Florida Office of Insurance Regulation