REPORT OF THE
ASSOCIATION FINANCIAL EXAMINATION OF

PHYSICIANS PROFESSIONAL INDEMNITY ASSOCIATION

AS OF
DECEMBER 31, 2008

(Adopted by the Director with Modifications or Corrections)

STATE OF MISSOURI

DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS
AND PROFESSIONAL REGISTRATION

JEFFERSON CITY, MISSOURI

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Jefferson City, Missouri
October 26, 2010

Honorable Alfred W. Gross, Commissioner
Virginia Bureau of Insurance
Chairman, Financial Condition (E) Committee

Honorable Mary Jo Hudson, Director
Ohio Department of Insurance
Secretary, Midwestern Zone, NAIC

Honorable John M. Huff, Director
Missouri Department of Insurance, Financial Institutions
and Professional Registration
301 West High Street, Room 530
Jefferson City, Missouri 65101

Ladies and Gentlemen:

In accordance with your financial examination warrant, a full scope association financial examination has been made of the records, affairs and financial condition of

Physicians Professional Indemnity Association

hereinafter referred to as such, as PPIA, or as the Company. Its administrative office is located at 3218 Emerald Lane, Suite B, Jefferson City, Missouri, 65109, telephone number (573) 634-7742. This examination began on June 8, 2009, and concluded on the above date.

SCOPE OF EXAMINATION

Period Covered

The prior full scope association financial examination of PPIA was made as of December 31, 2005, and was conducted by examiners from the State of Missouri representing the Midwestern Zone of the National Association of Insurance Commissioners (NAIC), with no other zones participating.

The current full scope association financial examination covered the period from January 1, 2006, through December 31, 2008, and was conducted by examiners from the State of Missouri, representing the Midwestern Zone of the NAIC, with no other zones participating.

This examination also included the material transactions and/or events occurring subsequent to the examination date, which are noted in this report.

Procedures

This examination was conducted in accordance with the NAIC Financial Condition Examiners Handbook, except where practices, procedures and applicable regulations of the Missouri Department of Insurance, Financial Institutions and Professional Registration (DIFP) and statutes of the State of Missouri prevailed. The Handbook requires that we plan and perform the examination to evaluate the financial condition and identify prospective risks of the Company by obtaining information about corporate governance, identifying and assessing inherent risks, and evaluating the Company's 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, management's compliance with Statutory Accounting Principles and annual statement instructions.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. The key activities identified in our examination of PPIA, were as follows:

- Investments
- Premiums
- Underwriting
- Claims Handling
- Reserving
- Taxes
- Related Party Transactions
- Reinsurance

The examiners relied upon information supplied by the Company's independent auditor, Seaver & Forck, CPA's, of Jefferson City, Missouri, for its audit covering the period from January 1, 2008, through December 31, 2008. Information relied upon mostly included the CPA workpapers for substantive testing of account balances.

Comments - Previous Examination

The previous financial examination of PPIA was conducted by the Missouri DIFP for the period ending December 31, 2005. Listed below are the comments, recommendations, and notes from the previous examination report, the Company's response, and the findings in the current examination.

Assessments

Comment: It was recommended that the Company establish a requirement for membership to allow for the assessment, if necessary, of ex-members. Such assessments would only be necessary to increase capital and surplus from losses and premium deficiencies that may have occurred during prior years.

Company's Response: The Company stated that the Chapter 383 (Medical Malpractice) statutes do not require an Association to assess ex-members or require the assessment of ex-members to be a requirement or condition of membership.

Current Findings: PPIA amended its Articles of Association in 2007 to specifically prohibit assessments of ex-members. This provision complies with Section 383.016(3)(e) (Articles of Association and Bylaws), which only requires the Articles of Association to specify how assessments shall apply to current members and former members.

Board of Directors

Comment: The Company was directed to elect more members to the Board of Directors to achieve the required twelve members that are required by the Articles of Association and Bylaws.

Company's Response: The Company stated that it would fill the vacant Board positions as PPIA expands in membership throughout the State of Missouri.

Current Findings: There were twelve members elected to the Board of Directors, as of December 31, 2008, in accordance with the provisions of the Articles of Association and Bylaws.

Conflict of Interest

Comment: The Company was directed to have its officers and directors sign a conflict of interest disclosure statement on an annual basis.

Company's Response: The Company stated that it believed its policy for the completion of the conflict of interest disclosure statement was satisfactory and in compliance with Missouri law and prudent business practices.

Current Findings: Directors and officers completed a conflict of interest statement during each year of the current examination period. However, omissions were noted in some of the statements that were completed. Refer to the Conflict of Interest section of this report for further information.

Fidelity Bond

Comment: The Company was directed to increase its fidelity bond insurance coverage to $150,000 to comply with the minimum coverage recommended by the guidelines of the NAIC Financial Condition Examiner's Handbook.

Company's Response: The Company stated that it was unaware of any specific statute, rule or NAIC guideline that requires PPIA to maintain a fidelity bond with a minimum liability limit of $150,000.

Current Findings: The Company's current fidelity bond policy has a liability limit of $175,000, which exceeds the amount recommended in the prior examination and complies with the recommended coverage by the NAIC.

Agency Agreement

Comment: The Company was directed to revise its amended agreement with the Missouri State Medical Association Insurance Agency, Inc. (MSMAIA) to specify what functions MSMAIA must perform in order to earn the two percent (2%) over-write commission.

Company's Response: The Company stated it would review the two percent (2%) universal commission and determine whether it should be phased out and terminated. If the commission continued, the contract would be modified to include the duties and responsibilities of the MSMAIA.

Current Findings: The Company amended the agency agreement with MSMAIA to eliminate the 2% over-write commission.

Reporting of Payments to Third Parties

Comment: The Company was directed to report the yearly amounts paid pursuant to its agreements with third parties in the "Notes to the Financial Statements" section of the Annual Statement. The specific Note in which to report the payments would be the one titled "Information Concerning Parent, Subsidiaries and Affiliates."

Company's Response: The Company stated that it would comply with the directive in future Annual Statements.

Current Findings: The Company did not disclose the amount of payments made to any third parties in the Notes to the Financial Statements section of the 2006, 2007 or 2008 Annual Statements. It was determined that three of the third parties described in the prior exam report meet the definition of a related party, per SSAP No. 25 (Accounting for and Disclosures about Transactions with Affiliates and Other Related Parties). Refer to the Affiliated Companies and

Related Party Transactions section of this report for a description of all related parties and a recommendation for disclosures in the Annual Statement.

Money Market Reporting

Comment: The Company was directed to properly report its investment in a Charles Schwab and Company money market fund on the Common Stocks line instead of the Cash and Short-Term Investments line of the Annual Statement, in accordance with the guidelines of the Securities Valuation Office of the NAIC.

Company's Response: The Company stated that it would properly report the Charles Schwab and Company money market fund on the Common Stocks line of future Annual Statements.

Current Findings: The Company fully disposed of its investment in the Charles Schwab money market fund during 2007.

Reserves for Losses and Loss Adjustment Expenses

Comment: The Missouri DIFP's consulting actuary determined that PPIA's reserves for losses and loss adjustment expenses (LAE) were deficient by $2,918,180, as of December 31, 2005. This deficiency was comprised of five components. The Company was directed to work with its actuary to develop and implement procedures that would address the underlying issues of each of the components. These procedures should result in adequate reserve levels in the future.

Company's Response: The Company stated the data and information created and relied upon by the Missouri DIFP consulting actuary in the review of PPIA's reserves was inaccurate, not based upon adequate data, and provided limited credible inferences. The Company also stated the claim review utilized by the Missouri DIFP consulting actuary was unreliable and formed a defective basis for the results and findings that the reserves were deficient. In summary, PPIA stated that it strongly disagreed with the examination findings and it was the Company's opinion, based upon the complete information available to PPIA, as well as the certified actuarial statement completed by its own actuary, that the case reserves were adequate and no deficiency existed.

Current Findings: PPIA's reported net incurred losses and LAE, as of December 31, 2005, were compared to the development during the four years ending December 31, 2009. There was a deficiency of $1,656,000 in the development of the December 31, 2005 net incurred losses and LAE during these subsequent years. However, the Missouri DIFP's consulting actuary determined that PPIA's reserves for losses and LAE were reasonable, as of December 31, 2008.

Unearned Premiums

Comment: The Company was directed to calculate ceded unearned premiums based upon the correct ceding rate, as specified in its reinsurance agreement.

Company's Response: The Company stated that it utilized a conservative approach in the application of the cession rate. The Company stated it would utilize the ceding rate set forth in the reinsurance agreement in the future calculation of ceded unearned premiums.

Current Findings: There were no ceded unearned premiums, as of December 31, 2008. The premiums ceded to the only reinsurer are based upon a percentage of PPIA's earned premiums.

Reinsurance Arrangement with PIPCO

Comment: It was recommended that PPIA should disclose the related party nature of the reinsurance agreement with PIPCO, SPC (PIPCO) and all other related features in future Annual Statements. It was recommended that the Company continue to evaluate the relationships under the agreement to be certain that it is beneficial for the entire membership of PPIA. It was also recommended that PPIA ensure that an adequate security, acceptable to the Missouri DIFP, is in place before reserve credits for cessions to PIPCO are reported on the Quarterly and Annual Statements.

Company's Response: The Company stated that the reinsurance agreement with PIPCO is beneficial to the PPIA membership in that the cost of reinsurance was significantly reduced, the duration of the reinsurance contract was increased, and the terms of the agreement were more beneficial to PPIA. It was also stated that PIPCO established the necessary trust account and has funded the account. The Company did not address the related party disclosure in the Annual Statement that was recommended.

Current Findings: Refer to the Affiliated Companies and Related Party Transactions section of this report for an explanation of the affiliation between PPIA and PIPCO. Refer to the Reinsurance section of this report for an explanation of the terms of the reinsurance agreement with PIPCO. A trust account that names PPIA as the beneficiary was established by PIPCO as collateral for ceded reserves.

HISTORY

General

PPIA was incorporated on April 21, 2003 under the laws of the State of Missouri and commenced business on July 1, 2003. The Company operates as an association medical malpractice insurer under the insurance laws of Chapter 383 RSMo (Malpractice Insurance).

Capital Stock

The Company does not have any stock issued due to its formation as an association. Each member physician that is insured by PPIA has equal voting rights during membership meetings.

Dividends

There are no provisions in the Articles of Association or Bylaws for the payment of dividends.

Management

The management of the Company is vested in a Board of Directors, which is appointed by the member policyholders. The Company's Bylaws specify that the Board of Directors shall consist of twelve members. The Board of Directors elected and serving, as of December 31, 2008, were as follows:

Name	Address	Principal Occupation and Business Affiliation
Carrie L. Carda, MD	Poplar Bluff, Missouri	Physician, Owner of Women's Health Specialists
Robert L. Hall, MD	Poplar Bluff, Missouri	Surgeon, Owner of Surgery Clinic of Poplar Bluff
William F. Marr	Bolivar, Missouri	Administrator, Bolivar Family Care Center
Warren K. Miller	Millersville, Missouri	Administrator, Cape Radiology Group
Randall E. Mueller, MD	Rocheport, Missouri	President, Emergency Physicians of Mid Missouri
Carl F. Patty, MD	Poplar Bluff, Missouri	Physician, Owner of Carl F. Patty, MD, LLC
John R. Patty, DO	Poplar Bluff, Missouri	Physician, Owner of John R. Patty, DO, LLC
Karl R. Stark, MD	Parkville, Missouri	Surgeon, President of Kansas City Vascular Surgery
Benny E. Thomas, DO	Lake Ozark, Missouri	Physician, Private Practice
Kevin L. Threlkeld, MD	Washington, Missouri	Physician, Self Employed
Mark S. Vincent, JD	Union, Missouri	Attorney, Vincent, Hoven & Purschke, P.C.
Robert C. Young, MD*	Poplar Bluff, Missouri	Physician, Self Employed

* Dr. Young resigned, effective September 23, 2009

Committees

The Articles of Association and Bylaws do not require any committees, but the Bylaws do allow for committees to be appointed by the Board of Directors. The members appointed and serving on active committees, as of December 31, 2008, were as follows:

Executive Committee	Budget Committee	Claims and Settlement Committee
Carrie L. Carda, MD	Carrie L. Carda, MD	Carrie L. Carda, MD
Jonathan L. Downard, JD	Jonathan L. Downard, JD	Jonathan L. Downard, JD
Robert L. Hall, MD	Robert L. Hall, MD	Robert L. Hall, MD
Carl F. Patty, MD	Warren K. Miller	Randall E. Mueller, MD
Benny E. Thomas, DO	Carl F. Patty, MD	Karl R. Stark, MD
	Kevin L. Threlkeld, MD	Benny E. Thomas, DO
	Robert C. Young, MD	Mark S. Vincent, JD
		Robert C. Young, MD

Investment Committee	Political Action Committee
Jonathan L. Downard, JD	Jonathan L. Downard, JD
William F. Marr	Robert L. Hall, MD
Randall E. Mueller, MD	Warren K. Miller
Carl F. Patty, MD	Carl F. Patty, MD

Officers

The officers elected by the Board of Directors and serving as of December 31, 2008, were as follows:

Officer	Position
Carrie L. Carda, MD	Chairperson and President
Jonathan L. Downard, JD	Executive Vice President and General Counsel
Robert L. Hall, MD	Secretary
Carl F. Patty, MD	Treasurer
Benny E. Thomas, DO	Vice President

Conflict of Interest

The Company has a policy that requires all officers, directors, and key employees to complete a conflict of interest statement each year. Several omissions were noted in the conflict of interest statements that were completed for 2008, as follows:

- Several directors own stock in the reinsurer, PIPCO, that was not disclosed.
- Mark Vincent did not disclose his representation of a policyholder, Patients First Health Care, LLC.

- Jonathan Downard did not disclose (1) the full extent of his ownership of Corporate Insurance Services, LLC (CIS), which provides administrative services for PPIA; (2) the Company's agreement with Med Pro, which is an agency for which he is an officer and director and is owned by his father, Lloyd Downard; (3) the full extent of his involvement as a partner in the law firm, Hansen, Stierberger, Downard, Melenbrink & Schroeder (HSDMS), which provides legal services for PPIA; or (4) the nature of the transactions between PPIA, CIS, MedPro, and HSDMS.

The Company has a high level of related party transactions that potentially present conflict of interest situations. Refer to the Affiliated Companies and Related Party Transactions section of this report for a complete description.

Corporate Records

A review was made of the Articles of Association and Bylaws. The Articles of Association were amended on August 18, 2007 for two purposes. A sentence was added to Article VII to state that former members of PPIA are not subject to assessments. Requirements were added to Article IX for the type of individuals that serve on the Board of Directors. A minimum of seven directors must be physicians insured by PPIA, two directors may by physicians that are not insured by PPIA, and three directors may be non-physicians. The Bylaws were amended on February 28, 2008 to change the date of the annual meeting of the members / policyholders.

The minutes of the Board of Directors' meetings, committee meetings, and member meetings were reviewed for proper approval of corporate transactions. In general, the minutes appear to properly reflect and approve the Company's major transactions and events for the period under examination.

Acquisitions, Mergers and Major Corporate Events

None.

Surplus Debentures

PPIA had no surplus notes issued and outstanding, as of December 31, 2008.

AFFILIATED COMPANIES AND RELATED PARTY TRANSACTIONS

Holding Company, Subsidiaries and Affiliates

PPIA and other medical malpractice insurers organized under Section 383 RSMo are not subject to the holding company statutes of Section 382 RSMo (Insurance Holding Companies). The Company is an association and therefore, there is no parent company. PPIA also does not have any subsidiaries.

Although the Company has no affiliates in terms of ownership, there are entities that are related to PPIA. Paragraph 2 of SSAP No. 25 (Accounting for and Disclosures about Transactions with Affiliates and Other Related Parties) states that "related parties are defined as entities that have common interests as a result of ownership, control, affiliation or by contract." PPIA has numerous relationships and transactions with entities that meet the definition of a related party, pursuant to paragraph 2 of SSAP No. 25. These entities and a description of the extent of the related party relationships are described in the following sections.

Related Party - PIPCO

PIPCO, SPC has been the Company's only reinsurer for direct policies issued since April 2006. PIPCO was incorporated as a Segregated Portfolio Company (SPC) in April 2006 under the laws of the Cayman Islands. An SPC entity is structured so that premiums and losses are to be kept in separate accounts for each company that is reinsured by the SPC. PPIA paid PIPCO $200,000 in February 2006 to acquire 20 shares of voting stock, which currently represents 8.1% of the total voting shares of PIPCO. Management stated that PIPCO was established to provide reinsurance coverage at a lower cost that will ultimately translate to an overall lower cost of medical malpractice insurance for Missouri physicians. PIPCO is a licensed reinsurer by the Cayman Islands Monetary Authority.

Since its formation in 2006, PIPCO has provided reinsurance coverage for PPIA only. [Note: Terms of the reinsurance agreement between PPIA and PIPCO are described in the Reinsurance section of this report.] PIPCO has no other source of premium income other than its business with PPIA.

Paragraph 2.f. of SSAP No. 25 states that a related party is an entity with "which the reporting entity may deal if either party directly or indirectly controls or can significantly influence the management or operating policies of the other to an extent that one of the transacting parties might be prevented from fully pursuing its own separate interest."

PPIA and PIPCO also have common management. Four of PPIA's directors (Dr. Hall, Dr. Thomas, Dr. Young and Mr. Vincent) are also current or past directors for PIPCO or are listed as current or past officers of PIPCO. Management stated that PIPCO's Bylaws require one director is to be selected by PPIA.

Related Party – Patients First

Patients First Health Care, LLC (Patients First) is the largest group insured by PPIA, accounting for approximately 10% of premiums in-force, as of December 31, 2008. Patients First is a multi-specialty group of 65 physicians based in Washington, Missouri. Patients First is a related party to PPIA through its ownership of the reinsurer, PIPCO. Patients First was identified by management as the entity that formed PIPCO in 2006.

PIPCO has voting and non-voting classes of stock. The percentage ownership of PIPCO voting stock held by Patients First and other entities could not be completely determined in our examination. Management of PPIA only provided a limited explanation that the ownership of PIPCO is comprised primarily of Missouri physicians. However, it was determined that thirteen individuals comprise the directors, officers, and alternate directors of PIPCO. Nine of these thirteen individuals are physicians or management employed by Patients First, including the Chairman of the Board, Chief Executive Officer, and Medical Director of Patients First.

Another entity, PFHC Medical Management, LLC (PFHC), was identified as owning 23.8% of the voting stock of PIPCO. PFHC is an affiliate of Patients First, but the extent of the affiliation is unknown. It appears that Patients First and PFHC collectively own the majority of PIPCO voting stock, since these two entities hold the majority of PIPCO's director and management positions.

Paragraph 2.h. of SSAP No. 25 describes a related party as an entity "which has an ownership interest in one of the transacting parties and can significantly influence the other to an extent that one or more of the transacting parties might be prevented from fully pursuing its own separate interests." Patients First has the ability to influence the directors and management of PPIA by virtue of the fact that four of PPIA's directors were as of December 31, 2008, in some manner affiliated with PIPCO. A potential conflict of interest is created between PPIA and Patients First on two levels. Patients First can influence the rates and terms of the reinsurance coverage provided by PIPCO for PPIA. The ownership of PIPCO could also affect the premium rates and insurance coverage provided by PPIA for Patients First.

Another connection between PPIA, Patients First, PFHC and PIPCO is Mark Vincent, a PPIA director. Mr. Vincent provides legal representation for Patients First and PFHC in addition to his management titles for PIPCO.

Patients First's ownership of PIPCO has created a dynamic in which Patients First may have effectively received free or greatly reduced cost of medical malpractice insurance for its 65 physicians for several years. This is accomplished from the profitability of PIPCO's reinsurance coverage provided for PPIA. PPIA paid premiums of $6.3 million to PIPCO from 2006 to 2008 while only recording incurred claims ceded to PIPCO of $2.7 million for the same period.

It should be noted that the Missouri DIFP was not able to obtain any financial statements for PIPCO during our examination. Thus, the financial condition or financial results for PIPCO are not known for the time period it has reinsured PPIA, beginning in 2006.

Related Parties Involving Jonathan Downard

Jonathan Downard is the Company's Executive Vice President and only full-time management employee. Paragraph 2.d. of SSAP No. 25 states that the management of an insurance company is a related party. There are three entities that are related parties to PPIA due to the ownership by Jonathan Downard or his family, which are described below:

- Corporate Insurance Services, LLC is an entity that performs most of the daily functions to operate the business of PPIA. An agreement between PPIA and CIS is described in the Related Party Agreements section of this report. CIS is a related party to PPIA from Jonathan Downard's dual role serving as executive management for PPIA and his ownership of CIS.
- Jonathan Downard is a partner in the law firm Hansen, Stierberger, Downard, Melenbrink & Schroeder. The Company has an agreement with HSDMS to receive legal services, which is described in the Related Party Agreements section. HSDMS is a related party to PPIA from Jonathan Downard's dual role serving as executive management for PPIA and his ownership / management of HSDMS.
- Administrative Management Corporation d.b.a. Med Pro (Med Pro) is owned 100% by Jonathan Downard's father, Lloyd Downard. Jonathan Downard is also an officer and director for Med Pro. The Company has an agency agreement with Med Pro to produce business for PPIA. This agreement is also described in the Related Party Agreements section. Paragraph 2.e. of SSAP No. 25 defines members of immediate families of management to be a related party. Med Pro is a related party to PPIA since it is owned by Jonathan Downard's father.

Related Party Disclosures

All material related party transactions are required to be disclosed in the Annual Statement filed by PPIA with the Missouri DIFP. Specifically, these disclosures are to be made in Note 10 (Information Concerning Parent, Subsidiaries and Affiliates) of the Notes to the Financial Statements section of the Annual Statement. PPIA is required by 20 CSR 200-1.020(1) and NAIC Annual Statement Instructions for Note 10 to disclose its relationship, agreements and transactions with PIPCO, Patients First, PFHC, CIS, HSDMS, and Med Pro in Note 10 of future Annual Statements.

Transactions with Related Parties

Transactions and agreements between related parties are reviewed in our financial examinations to determine if the transactions and agreements were made on an "arms-length" basis. Our examination reviewed the "arms-length" nature of the transactions and agreements between PPIA and PIPCO.

There are potential conflicts of interest between PPIA and PIPCO. These conflicts include PPIA's ownership of PIPCO stock, Patients First's majority ownership of PIPCO stock, and the four individuals that serve jointly as directors and officers of PPIA and PIPCO. Because of these factors, it would appear that any other potential reinsurers of PPIA's business could be at a competitive disadvantage because of the related party relationship between PPIA and PIPCO.

The reinsurance agreement with PIPCO was effective April 1, 2006. We requested copies of any proposals for reinsurance coverage that were obtained from other reinsurers at the time the agreement with PIPCO was being considered in 2006. The Company did not provide any documentation to demonstrate that a reasonable effort was made to obtain competitive bids in comparison to the rates and coverage that were being offered by PIPCO. Management cited the attorney-client privilege as the basis for denying our request for this underwriting documentation. Management did not document the receipt of other proposals for reinsurance from the direct or brokerage market in the United States over the last three years.

We further requested copies of any proposals for reinsurance coverage that were obtained from other reinsurers or brokers in 2007, 2008 or 2009. Due to the cancellation provisions of the PIPCO agreement, PPIA would be able to terminate the PIPCO agreement and execute a reinsurance agreement with another reinsurer if more favorable rates and terms were found. Management stated that it only had conversations with a Lloyds of London representative, and discussions with other reinsurers at meetings or forums, to determine reinsurance rates and coverages that were available in the 2007 to 2009 timeframe. Management did not document the receipt of other proposals for reinsurance from the direct or brokerage market in the United States over the last three years.

The Company's reinsurance underwriting efforts have been deficient from the time that the PIPCO agreement was negotiated and the subsequent years since the PIPCO agreement has been in effect. Management has not performed the same level of due diligence in reviewing reinsurance options that is typically demonstrated by other insurance companies. This lack of effort and due diligence could result in PPIA paying higher than necessary premium rates for the reinsurance coverage that is provided by PIPCO. Ultimately, excessive reinsurance premium rates are not in the best interest of the members of PPIA in that the overall level of surplus available to pay claims is reduced.

Our examination could not conclude that reinsurance coverage provided by PIPCO and the reinsurance premium rates paid to PIPCO were the result of "arms-length" negotiations. This is due to the lack of documentation for reinsurance proposals from other reinsurers at comparable coverage to the terms and rates in the PIPCO reinsurance agreement.

Related Party Agreements

The Company's agreements with related parties that were in effect, as of December 31, 2008 and subsequent periods, are outlined below. A reinsurance agreement and a trust agreement with PIPCO are described in the Reinsurance section of this report.

1. **Type:** Administration Agreement

   Entity: Corporate Insurance Services, LLC

   Effective: May 6, 2005

   Terms: CIS will provide the following administrative services for the Company: business management, administration, investments, underwriting, issuance of policies, compliance with the Missouri DIFP, coordination of actuarial and auditing services, personnel, and accounting services. The fees paid by PPIA to CIS are dependent upon the gross written premiums each year. CIS receives 10% of the first $3,000,000 of premiums; 8% of premiums between $3,000,000 and $5,000,000; and 6% of premiums in excess of $5,000,000.

2. **Type:** Agreement (Legal Counsel)

   Entity: Hansen, Stierberger, Downard, Melenbrink & Schroeder

   Effective: May 10, 2006 (replaced prior agreement effective since May 26, 2005)

   Terms: HSDMS will provide the following legal services for the Company: legal compliance with the Missouri Secretary of State and Missouri DIFP, legal consultation on day-to-day operations, review of litigation and assignment and oversight of all claims against members, participation in the settlement committee, attendance at Board of Directors meetings and membership meetings, review of legal documents and contracts, and the preparation of any necessary legal documents or forms. PPIA will pay HSDMS $6,666 per month for the services provided.

3. **Type:** Producer-Company Agreement

   Entity: Administrative Management Corporation d.b.a. Med Pro

   Effective: August 27, 2008 (replaced prior agreement effective since July 1, 2003)

   Terms: Med Pro is authorized to solicit applications for, and to service insurance policies issued by PPIA. Med Pro cannot act as an agent for any other medical malpractice insurer licensed pursuant to Chapter 383 RSMo. Med Pro is also authorized to collect premiums on behalf of PPIA. However, PPIA bills and collects premiums directly from its policyholders in most instances. PPIA will pay commissions equal to 10% of the collected premium for business produced by Med Pro.

4. **Type:** Professional Liability Insurance Policy

   Entity: Patients First Health Care, LLC

   Effective: January 1, 2008 to January 1, 2009
   January 1, 2009 to January 1, 2010 (renews January 1 of each year)

   Terms: The Company provides insurance coverage for any liability claims made against medical services that were provided by Patients First and its group of physicians. The policy limit is $1,000,000 per claim for each physician with an annual aggregate coverage of $3,000,000 for each physician. In addition to the policy limits, the policy will cover the costs incurred to defend Patients First and its physicians in any lawsuit. Patients First will pay monthly installment premiums that include finance charges at an annual rate of 4.5%. The total premium for a policy period varies depending on physicians added to or deleted from the policy throughout the year. The beginning annual premium was $703,023 at the beginning of 2008 and $741,451 at the beginning of 2009.

Payments

Fees and other payments to related parties, pursuant to the above agreements, are listed in the following table:

		Net Paid / (Received)		
Related Party	Agreement	**2006**	**2007**	**2008**
CIS	Administration	$675,999	$831,089	$675,642
HSDMS	Legal Counsel	73,328	79,992	79,992
Med Pro	Producer-Company	97,011	95,382	75,499
Patients First	Insurance Policy	(572,653)	(669,708)	(726,903)
TOTAL		$273,685	$336,755	$104,230

FIDELITY BOND AND OTHER INSURANCE

The Company is a named insured on a commercial crime policy that covers losses resulting from dishonest or fraudulent acts of employees. The policy has a liability limit of $175,000 with a $250 deductible, which meets the minimum coverage that is recommended by the NAIC. The Company also has an insurance policy that provides coverage for the following risks: business personal property, loss of income, business liability and medical payments. The Company does not have a worker's compensation policy or a directors' and officers' liability policy. These coverages are standard for most insurance companies and it is recommended that the Company consider purchasing policies for these risks.

PENSION, STOCK OWNERSHIP AND INSURANCE PLANS

PPIA only has two direct employees – Executive Vice President, Jonathan Downard, and an individual that manages the Company's office in Jefferson City, Missouri. The Company does not provide any benefits for these two employees.

Most of the Company's daily business operations are performed by the employees of Corporate Insurance Services, LLC, an entity owned by Jonathan Downard and based in Union, Missouri. PPIA has an Administration Agreement with CIS, which is described in the Affiliated Companies and Related Party Transactions section of this report. CIS has a staff of six employees. Any benefits provided to CIS employees are indirectly paid by PPIA through the payment of fees, pursuant to the Administration Agreement.

STATUTORY DEPOSITS

Deposits with the State of Missouri

There is no law requiring funds to be placed on deposit with the Missouri DIFP for medical malpractice insurers licensed pursuant to Section 383 RSMo.

Deposits with Other States

Since PPIA is only licensed in Missouri, the Company has no funds on deposit with any other states.

INSURANCE PRODUCTS AND RELATED PRACTICES

Territory and Plan of Operation

The Company is licensed as a medical malpractice insurer by the Missouri DIFP under Chapter 383 RSMo (Malpractice Insurance). PPIA is not licensed in any other states. The Company's only line of business is medical malpractice written on a claims-made reporting basis. During 2008, PPIA was the fifth largest writer of physician medical malpractice insurance in the State of Missouri. As of December 31, 2008, the Company had 256 policies in-force that insured 680 physicians.

The Company has several options for policy limits that members may choose, which range from as low as \$100,000 of coverage per claim up to a maximum coverage of \$1,000,000 per claim. Other policy options are available including extended reporting endorsements. A physician may purchase extended reporting coverage that will cover claims reported after the expiration, termination, or cancellation of a policy. Any physician insured by PPIA for a minimum of three years automatically receives extended reporting coverage in the event that the physician becomes disabled, dies, or retires.

The Company's business increased during the first year (2006) of the examination period, while decreasing the following two years, as shown in the table below:

Year	Direct Premiums Written	Net Premiums Written	Surplus as Regards Policyholders	Ratio of Net Premiums to Surplus
2005	\$ 8,466,959	\$5,991,959	\$ 311,615	19.23
2006	10,468,408	8,819,424	291,754	30.23
2007	9,415,129	6,998,749	963,385	7.26
2008	7,650,968	7,158,964	1,756,717	4.08

The decrease in direct writings in 2008 was due to a combination of the termination of an agreement with the Company's largest agency in March 2008 and a 14% reduction in premium rates, e ffective January 1, 2008. The large growth in surplus during 2007 and 2008 was attributable to a combination of net income and reinsurance transactions. The most significant item was the commutation of a reinsurance agreement at the end of 2008 that resulted in a net increase to surplus of approximately \$900,000.

The Company utilized seven agencies to produce its business in 2008, which was an increase from four agencies in 2006 and 2007. The largest agency is the Missouri State Medical Association Insurance Agency (MSMAIA), which accounted for 76%, 79%, and 61% of the total commissions paid by PPIA for 2006, 2007, and 2008, respectively. The Company's relationship with MSMAIA had been terminated in March 2008, but was renewed in April 2009 with a new agency agreement.

Policy Forms & Underwriting
Advertising & Sales Materials
Treatment of Policyholders

The Missouri DIFP has a market conduct staff that performs a review of these issues and generates a market conduct report. However, the Missouri DIFP has never conducted a market conduct examination of PPIA.

REINSURANCE

General

The Company's premium activity on a direct written, assumed and ceded basis, for the period under examination, is detailed below:

	2006	2007	2008
Direct Business	\$10,468,408	\$9,415,129	\$7,650,968
Reinsurance Assumed	0	0	0
Reinsurance Ceded:			
Lloyd's of London	(825,000)	0	1,531,617
PIPCO	(823,984)	(2,416,380)	(2,024,021)
Net Premiums Written	**\$ 8,819,424**	**\$6,998,749**	**\$7,158,564**

Assumed

The Company does not assume any business.

Ceded

The Company had one reinsurance agreement in effect, as of December 31, 2008, with PIPCO, SPC that remained in effect until cancelled on March 31, 2010. This agreement is herein referred to as the "2006 agreement" or the "2006 reinsurance agreement." The 2006 reinsurance agreement with PIPCO had a ten year term, effective April 1, 2006 and ending April 1, 2016. PPIA cedes 100% of losses in excess of a retention of \$500,000 per claim. PIPCO's limit of liability is \$500,000 per claim. The retention of \$500,000 plus the excess reinsurance coverage of \$500,000 per claim equals the maximum \$1,000,000 limit of insurance for any policy issued by PPIA. The 2006 agreement also has an aggregate limit of liability for PIPCO that cannot exceed 200% of total premiums ceded by PPIA during the duration of the agreement.

The reinsurance premium rates under the 2006 agreement with PIPCO were negotiated on a yearly basis and were structured as a percentage of the Company's earned premiums. The actual premium rate was 25% of PPIA's total earned premiums for the first two agreement years from April 1, 2006 through March 31, 2008. The premium rate for each of the next two agreement years from April 1, 2008 through March 31, 2010 will be 24% for PPIA's first $9 million of earned premiums; 23% for earned premiums between $9 million and $10 million; and 22% for earned premiums between $10 million and $11 million.

PIPCO is an unauthorized reinsurer for PPIA because it is not a licensed, accredited or approved reinsurer in the State of Missouri. An insurance company may not take credit for any reinsurance recoverables (mostly ceded loss and LAE reserves) from unauthorized reinsurers on its financial statements, unless an acceptable form of collateral is established. PPIA is the beneficiary in a trust agreement, effective April 1, 2006, that includes PIPCO, as the grantor, and the Bank of Washington serving as the trustee. There were funds totaling $2.5 million, as of December 31, 2008, in the PIPCO trust account that would be available for PPIA to withdraw in the event that PIPCO could not meet its obligations under the 2006 reinsurance agreement.

The only other reinsurance agreement in effect during the examination period was an agreement with various syndicates of Lloyd's of London, effective from April 1, 2005 to March 31, 2006. This agreement provided reinsurance coverage of $500,000 per claim in excess of a retention of $500,000, which is the same coverage as the current agreement with PIPCO. The agreement was commuted, effective April 1, 2008. A large receivable was recorded, as of December 31, 2008, as a result of the commutation of the agreement that is described in Note 2 of the Notes to the Financial Statements section of this report.

The Company is contingently liable for all reinsurance losses ceded to others. This contingent liability would become an actual liability in the event that an assuming reinsurer fails to perform its obligations under the reinsurance agreement.

ACCOUNTS AND RECORDS

The CPA firm, Seaver & Forck, CPA's, of Jefferson City, Missouri issued audited statutory financial statements of the Company for all years in the examination period.

The actuarial opinion regarding the Company's reserves for losses and loss adjustment expenses (LAE) was issued by Steven J. Regnier, ACAS, MAAA, of Regnier Consulting Group, Inc. in Stevens Point, Wisconsin for all years in the examination period.

J. Randy Snodgrass, CPA, of Jefferson City, Missouri provides accounting services and prepares the Quarterly and Annual Statements for PPIA. Mr. Snodgrass is the designated contact person for PPIA in its correspondence with the Missouri DIFP and also managed the gathering of information to respond to the Missouri DIFP's requests for this financial examination.

FINANCIAL STATEMENTS

The following financial statements, with supporting exhibits, present the financial condition of Physicians Professional Indemnity Association for the period ending December 31, 2008. Any examination adjustments to the amounts reported in the financial statements and/or comments regarding such are made in the "Notes to the Financial Statements." The failure of any column of numbers to add to its respective total is due to rounding or truncation.

There may have been additional differences found in the course of this examination, which are not shown in the "Notes to the Financial Statements." These differences were determined to be immaterial concerning their effect on the financial statements, and therefore, were only communicated to the Company and/or noted in the workpapers for each individual Annual Statement item.

Assets
as of December 31, 2008

	Assets	Non-Admitted Assets	Net Admitted Assets
Bonds	$ 9,255,558	$ 0	$ 9,255,558
Common Stocks	1	1	0
Cash and Short-Term Investments	2,996,268	0	2,996,268
Investment Income Due and Accrued	106,920	0	106,920
Uncollected Premiums and Agents' Balances (**Note 1**)	20,479	1,603	18,876
Deferred Premiums (**Note 1**)	2,283,957	0	2,283,957
Other Amounts Receivable Under Reinsurance Contracts (**Note 2, 3**)	2,758,836	1,035,745	1,723,091
Net Deferred Tax Asset (**Note 4**)	605,465	239,215	366,250
Electronic Data Processing Equipment	1,564	1,564	0
Furniture and Equipment	6,697	6,697	0
Aggregate Write-In Assets:			
Deposit Account – PIPCO (**Note 5**)	5,850,130	3,343,639	2,506,491
Leasehold Improvements	6,321	6,321	0
TOTAL ASSETS	**$23,892,196**	**$4,634,785**	**$19,257,411**

Liabilities, Surplus and Other Funds
as of December 31, 2008

Losses (**Note 6**)	$ 9,501,000
Loss Adjustment Expenses (**Note 6**)	3,822,479
Commissions Payable	12,483
Other Expenses	34,482
Taxes, Licenses and Fees	145
Federal Income Taxes Payable (**Note 7**)	1,278,486
Unearned Premiums (**Note 8**)	4,092,337
Advance Premium (**Note 9**)	225,934
Amounts Withheld or Retained	1,280
Ceded Reinsurance Premiums Payable	0
Aggregate Write-In Liabilities:	
Unearned Finance Charges	127,739
TOTAL LIABILITIES	**$19,096,365**
Common Capital Stock	0
Gross Paid In and Contributed Surplus	0
Unassigned Funds (Surplus)	161,046
Capital and Surplus	**$ 161,046**
TOTAL LIABILITIES AND SURPLUS	**$19,257,411**

Statement of Income
For the Year Ended December 31, 2008

Premium Earned	**$8,015,174**
DEDUCTIONS:	
Losses Incurred	2,753,466
Loss Expenses Incurred	2,597,073
Other Underwriting Expenses Incurred	2,021,411
Total Underwriting Deductions	**$7,371,950**
Net Underwriting Gain	**$ 643,224**
Net Investment Income Earned	435,730
Net Realized Capital Gains	4,919
Net Investment Gain	**$ 440,649**
Other Income	311,957
Dividends to Policyholders	0
Federal Income Taxes Incurred	456,842
Net Income	**$ 938,988**
CAPITAL AND SURPLUS ACCOUNT:	
Surplus as Regards Policyholders, December 31, 2007	$ 963,385
Net Income	938,988
Change in Net Deferred Income Tax	(80,881)
Change in Non-Admitted Assets	(64,775)
Examination Changes	(1,595,671)
Surplus as Regards Policyholders, December 31, 2008	**$ 161,046**

Notes to the Financial Statements

Note 1 – Uncollected Premiums and Agents Balances **$ 18,876**
Deferred Premiums **$2,283,957**

The Company reported premium receivables of $2,302,833 on the Uncollected Premiums line and $0 on the Deferred Premiums line. During our examination, it was determined that most of the premium receivables, as of December 31, 2008, were actually installments that would not be billed until 2009. The NAIC Annual Statement Instructions require any premium receivables that have not been billed to be reported on the Deferred Premiums line. An examination change was made to reclassify $2,283,957 of receivables to the Deferred Premiums line, which left a remaining balance of $18,876 for the Uncollected Premiums line.

The Company should properly separate its premium receivables into billed and unbilled categories in the future. Any portion of the premiums receivable that are installments that have not been billed to the policyholder should be reported on the Deferred Premiums line. Only the portion of premium receivables that has been billed and uncollected should be reported on the Uncollected Premiums line.

Note 2 – Other Amounts Receivable Under Reinsurance Contracts **$1,723,091**

The Company reported a receivable of $1,035,745 in the Other Amounts Receivable Under Reinsurance Contracts line that was referred to as a "deposit" with its reinsurer, PIPCO. This asset resulted from estimated reinsurance premium payments made by PPIA that were in excess of the actual premiums that were due to PIPCO. The Company pays quarterly estimated reinsurance premiums to PIPCO based upon a projection of earned premiums for the year. Actual reinsurance premiums can either be greater or lesser than the estimated amounts paid to PIPCO. A "true-up" settlement is supposed to be made for the balance either due to or due from PIPCO.

The deposits receivable from PIPCO accumulated since the inception of the reinsurance agreement on April 1, 2006, through December 31, 2008, but most of the asset balance was created during 2006. The portion of the receivable attributable to the 2006 coverage period was $849,189 or 82% of the cumulative balance, as of December 31, 2008.

The 2006 reinsurance agreement with PIPCO is vague in addressing the true-up between estimated premium payments and actual premium due. A specific number of days is not stated in the agreement for the true-up settlements. The 2006 agreement states that premiums shall be adjusted "as soon as possible" based upon actual gross net earned premium income at the end of each calendar year. This would indicate that it is a contractual obligation for PIPCO to refund any differences between PPIA's estimated premium payments and actual premiums due, shortly after the end of each calendar year. However, PIPCO did not make any payments to the Company in 2007, 2008, and most of 2009 for the deposit balances that had accumulated since April 1, 2006.

The Missouri DIFP examiners submitted a request to PPIA on September 24, 2009 to determine why PIPCO had not settled any portion of the deposit receivables since the balances began accumulating in 2006. The Company did not provide an explanation for the significant delay of well over two years in the collection of the receivables. However, the Company did explain that PPIA had received a payment from PIPCO on September 30, 2009 for the full amount of $1,035,745 that was due at December 31, 2008.

The deposit balances receivable from PIPCO at the end of 2006, 2007 and 2008 should have been collected well before September 30, 2009. The amounts receivable were very large and should not have been overlooked or allowed to remain stagnant on the balance sheet for over two years. Using PPIA's actual investment yields for 2007 (3.5%) and 2008 (3.6%), the Company could have earned approximately $85,000 of additional investment income during 2007 to 2009, if the PIPCO receivables would have been collected on a timely basis.

The Company should implement the following changes to prevent such large receivables from accumulating in the future:

- Any current or future reinsurance agreements should include terms to require the settlement of any balances due for the differences between estimated and actual reinsurance premiums to be made within 90 days after December 31 of each year.
- Management should implement monthly monitoring procedures to age the deposit amounts receivable from PIPCO. Immediate request for payment should be submitted to PIPCO for any amounts past due, in accordance with the amended terms of payment recommended above.
- Corrective action should be taken to avoid such large differences between the estimated and actual premiums, which occurred during 2006 to 2008 for the PIPCO reinsurance agreement. A faulty estimation methodology appears to have been used, especially for the 2006 estimated earned premiums. Improvements should be made in the estimation process to lower the risk of a large variance between estimated and actual earned premiums.

Note 3 – Other Amounts Receivable Under Reinsurance Contracts $1,723,091

An examination change was made to eliminate the $1,035,745 receivable from PIPCO that is described in Note 2. This adjustment was necessary to implement deposit accounting under the 2006 reinsurance agreement with PIPCO, which is explained in Note 5. The receivable would have been double counted under deposit accounting and therefore, was eliminated.

The Company also reported a receivable of $1,531,617 on the Other Amounts Receivable Under Reinsurance line for a commutation settlement receivable from Lloyd's of London. However, the actual cash received in 2009 was $191,474 greater than the receivable recorded at December 31, 2008. An examination change was made to increase the receivable to reflect the correct balance. Based on an actuarial report obtained by the Company from PIPCO the Company in good faith believed its reinsurance with PIPCO transferred risk and prepared its financial statements in accordance with this good faith belief. Upon subsequent examination, in fact the reinsurance does not transfer sufficient risk to qualify for the treatment given by PPIA.

Note 4 – Net Deferred Tax Asset **$366,250**

The net admitted Deferred Tax Asset (DTA) calculated by the Company was overstated due to an incorrect application of the provisions of SSAP No. 10 (Income Taxes). Paragraph 10.b of SSAP No. 10 allows for DTAs to be admitted at the lesser of temporary differences that will reverse in the next year or 10% of capital and surplus. PPIA determined that $126,406 of DTAs could be admitted pursuant to paragraph 10.b. However, any temporary tax timing differences used in the application of paragraph 10.a. for possible loss carrybacks cannot be used in the calculation of admitted DTAs in paragraph 10.b. Paragraph 4.6 in the Q&A section of SSAP No. 10 explains the following: *"If the reporting entity expects to realize an amount of gross DTAs under paragraph 10.b.i. that is equal to or less than the admitted gross DTAs calculated under paragraph 10.a., then the resulting admitted gross DTAs under paragraph 10.b.i. will be zero."* PPIA utilized all of the temporary timing differences for the admitted DTA determined from paragraph 10.a. and therefore, no additional DTAs from paragraph 10.b. can be admitted.

An examination change was made to non-admit $126,406 of DTAs from the incorrect application of SSAP No. 10. In the future, the Company should calculate the net admitted DTAs using the proper application of the instructions included in SSAP No. 10.

Note 5 – Aggregate Write-In Asset: Deposit Account – PIPCO **$2,506,491**

PPIA's 2006 reinsurance agreement with PIPCO was determined to not properly transfer risk, as explained in Note 6. SSAP No. 75 (Reinsurance Deposit Accounting) requires deposit accounting treatment for any reinsurance agreement that does not transfer risk. Deposit accounting requires a cumulative balance to be maintained for any cash transactions.

Our examination determined what the deposit balance would have been for the 2006 agreement with PIPCO, if deposit accounting had been applied to all transactions between PPIA and PIPCO from the inception of the agreement (April 1, 2006) until December 31, 2008. PPIA paid premiums of $6,330,130 to PIPCO and received loss and LAE recoveries of $480,000 during this time period. This would have resulted in a net deposit balance of $5,850,130, as of December 31, 2008.

PIPCO is domiciled in the Cayman Islands and thus, is an unauthorized reinsurer. The deposit balance from PIPCO may be admitted only to the extent that an acceptable form of collateral has been established. PPIA is the beneficiary in a trust account maintained by PIPCO, which had a balance of $2,506,491, as of December 31, 2008. Therefore, an examination change was made to establish the net admitted deposit balance of $2,506,491, which should have been reported under deposit accounting. Based on an actuarial report obtained by the Company from PIPCO the Company in good faith believed its reinsurance with PIPCO transferred risk and prepared its financial statements in accordance with this good faith belief. Upon subsequent examination, in fact the reinsurance does not transfer sufficient risk to qualify for the treatment given by PPIA.

Note 6 – Losses **$9,501,000**
Loss Adjustment Expenses **$3,822,479**

A consultant hired by the Missouri DIFP determined that the 2006 reinsurance agreement with PIPCO does not transfer risk, as defined in paragraphs 10 through 17 of SSAP No. 62 (Property and Casualty Reinsurance). The consultant's report stated that the reinsurance premiums paid to PIPCO are sufficiently high that it is only remotely possible that PIPCO would experience a significant loss under the 2006 agreement. The term of the 2006 agreement is another factor that lessens the transfer of risk since it is not reasonably possible for PIPCO to realize a significant loss over a ten-year period versus a typical one-year term.

An internal actuary of the Missouri DIFP also determined that the 2006 reinsurance agreement with PIPCO does not adequately transfer risk, as defined by SSAP No. 62. The Missouri DIFP actuary performed two tests to project the profits or losses of PIPCO under different scenarios of losses. It was determined that there was less than a 10% chance for PIPCO to experience a net loss under the terms of the 2006 agreement.

SSAP No. 75 (Reinsurance Deposit Accounting) explains the deposit accounting procedures that should be followed for reinsurance agreements that are determined to not properly transfer risk. No deductions to loss and LAE reserves are allowed for any reinsurance agreement that does not transfer risk. As a result, an examination change was made to disallow the reinsurance credits for reserves ceded to PIPCO, which were $1,600,000 for ceded losses and $594,000 for ceded LAE, as of December 31, 2008.

PPIA's 2006 reinsurance agreement with PIPCO was cancelled, effective March 31, 2010, and commuted on June 30, 2010. Therefore, deposit accounting treatment for reinsurance premiums and loss recoveries is no longer applicable, due to the commutation of the 2006 agreement. Based on an actuarial report obtained by the Company from PIPCO the Company in good faith believed its reinsurance with PIPCO transferred risk and prepared its financial statements in accordance with this good faith belief. Upon subsequent examination, in fact the reinsurance does not transfer sufficient risk to qualify for the treatment given by PPIA.

Note 7 – Federal Income Taxes Payable **$1,278,486**

The 2006, 2007 and 2008 financial statements were adjusted to implement deposit accounting for the 2006 reinsurance agreement with PIPCO, which is explained in Notes 5 and 6. PPIA would have reported $2,620,385 of additional underwriting gains for the period from 2006 to 2008, if deposit accounting would have been used for transactions with PIPCO. Additional income taxes of $890,931 would be payable on this additional income, after applying a 34% tax rate. An examination change was made to increase the Federal Income Taxes Payable by this amount. Based on an actuarial report obtained by the Company from PIPCO the Company in good faith believed its reinsurance with PIPCO transferred risk and prepared its financial statements in accordance with this good faith belief. Upon subsequent examination, in fact the reinsurance does not transfer sufficient risk to qualify for the treatment given by PPIA. While it is appropriate to modify the financial statement to reflect additional income taxes payable, the Report is not intended to and does not conclude that PPIA presently has any additional tax liabilities.

Note 8 – Unearned Premiums **$4,092,337**

The Company failed to record a portion of the unearned premiums for extended reporting policies. The total unearned premiums for extended reporting policies was $571,596, but the Company only recorded a liability of $342,980 for those policies issued in 2008. An exam change was made to increase the reserve for unearned premiums by $228,617 for the extended reporting policies issued prior to 2008. The Company should implement controls or crosscheck procedures to ensure that proper accounting entries are made in the future to fully record this component of unearned premiums.

Note 9 – Advance Premium **$ 225,934**

The reported liability of $407,997 for the Advance Premium line was overstated by $182,063 due to the inclusion of premium receipts for policies that were already in effect, as of December 31, 2008. An examination change was made to reduce the advance premium liability for the amount of the overstatement. It was determined that several reported advance premium amounts were actually early payments of installments due for existing policies. An advance premium is defined in paragraph 13 of SSAP No. 53 as premium that is received prior to the effective date of the policy. In the 2008 Annual Statement, an advance premium liability should have been recorded only for premiums received for policies with beginning effective dates in 2009. The Company should ensure to properly report the advance premium liability in the future.

Examination Changes

Capital and Surplus Per Company, December 31, 2008:	
Unassigned Funds (Surplus)	$1,756,717
Total Capital and Surplus Per Company	**$1,756,717**
Examination Changes:	
Eliminate Receivable from PIPCO (**Note 3**)	($1,035,745)
Increase Commutation Receivable (**Note 3**)	191,474
Non-Admit Net Deferred Tax Asset (**Note 4**)	(126,406)
Add Deposit Accounting Balance – PIPCO (**Note 5**)	2,506,491
Disallow Reserve Credits from PIPCO (**Note 6**)	(2,194,000)
Increase FIT Payable for Deposit Accounting (**Note 7**)	(890,931)
Increase Unearned Premiums (**Note 8**)	(228,617)
Decrease Advance Premium (**Note 9**)	182,063
Total Examination Changes	**($1,595,671)**
Capital and Surplus Per Examination, December 31, 2008:	
Unassigned Funds (Surplus)	161,046
Total Capital and Surplus Per Examination	**$ 161,046**

General Comments and/or Recommendations

Conflict of Interest Statements and Disclosures (pages 8 and 9)

The Company should take steps to ensure that conflicts of interest are properly disclosed in the conflict of interest statements in the future.

The Company has a high level of related party transactions that present potential conflict of interest situations. The Board of Directors should be cognizant of the potential conflicts of interest created by these related party relationships in its management of the business affairs of PPIA. The Board of Directors should continue to properly review any transactions or agreements, in which a conflict of interest exists, to verify that the terms and payments included in the transactions or agreements are "arms-length" in nature.

Related Parties and Required Disclosures (pages 10 to 12)

All material related party transactions should be disclosed in the Annual Statement filed by PPIA with the Missouri DIFP. Specifically, these disclosures are to be made in Note 10 (Information Concerning Parent, Subsidiaries and Affiliates) of the Notes to the Financial Statements section of the Annual Statement. PPIA should disclose its relationship, agreements and transactions with PIPCO, Patients First, CIS, HSDMS, and Med Pro in Note 10 of future Annual Statements.

Reinsurance Underwriting (pages 13 and 14)

It is recommended that the management and Board of Directors of PPIA implement a policy to require at least two alternative proposals for reinsurance coverage be obtained each year. The Company should consult with brokers in the United States, such as Aon Benfield and Guy Carpenter, as well as its established contacts in the Lloyd's of London and Cayman Islands markets in the process of obtaining reinsurance proposals. The reinsurance proposals should be in writing and maintained in the Company's files for at least five years. The proposed terms, rates, and other conditions of the competitive reinsurance bids should be compared to the coverage and premium rates of reinsurance agreements currently in effect. This yearly process will allow management and the Board of Directors to properly evaluate its options for reinsurance coverage to best serve the interests of the member physicians of PPIA.

Insurance (page 16)

The Company does not have a worker's compensation policy or a directors' and officers' liability policy. These coverages are standard for most insurance companies and it is recommended that the Company consider purchasing policies for these risks.

Premium Receivable Reporting (page 24)

Most of the premium receivables that were reported on the Uncollected Premiums line should have been reported on the Deferred Premiums line, since most of the premium receivables, as of December 31, 2008, were actually installments that would not be billed until 2009. The Company should properly separate its premium receivables into billed and unbilled categories in the future. Any portion of the premiums receivable that are installments that have not been billed to the policyholder should be reported on the Deferred Premiums line. Only the portion of premium receivables that has been billed and uncollected should be reported on the Uncollected Premiums line.

Deposits Receivable from PIPCO (pages 24 and 25)

The Company reported a receivable of $1,035,745 that was referred to as a "deposit" with its reinsurer, PIPCO. This asset resulted from estimated reinsurance premium payments made by PPIA that were in excess of the actual premiums that were due to PIPCO. The deposits receivable from PIPCO accumulated since the inception of the reinsurance agreement on April 1, 2006, through December 31, 2008, but most of the asset balance was created during 2006.

The 2006 reinsurance agreement with PIPCO states that premiums shall be adjusted "as soon as possible" based upon actual gross net earned premium income at the end of each calendar year. This would indicate that it is a contractual obligation for PIPCO to refund any differences between PPIA's estimated premium payments and actual premiums due, shortly after the end of each calendar year. However, PIPCO did not make any payments to the Company in 2007, 2008, and most of 2009 for the "deposit" balances that had accumulated since April 1, 2006. Upon inquiry about the payment delay in our examination, PPIA received a payment from PIPCO on September 30, 2009 for the full amount of $1,035,745 that was due at December 31, 2008.

The "deposit" balances receivable from PIPCO at the end of 2006, 2007 and 2008 should have been collected well before September 30, 2009. PPIA could have earned an estimated $85,000 of additional investment income during 2007 to 2009, if the PIPCO receivables would have been collected on a timely basis.

The Company should implement the following changes to prevent such large receivables from accumulating in the future:

- Any current or future reinsurance agreements should include terms to require the settlement of any balances due for the differences between estimated and actual reinsurance premiums to be made within 90 days after December 31 of each year.
- Management should implement monthly monitoring procedures to age the "deposit" amounts receivable from PIPCO. Immediate request for payment should be submitted to PIPCO for any amounts past due, in accordance with the amended terms of payment recommended above.
- Corrective action should be taken to avoid such large differences between the estimated and actual premiums, which occurred during 2006 to 2008 for the PIPCO reinsurance agreement. A faulty estimation methodology appears to have been used, especially for the 2006 estimated earned premiums. Improvements should be made in the estimation process to lower the risk of a large variance between estimated and actual earned premiums.

Net Deferred Tax Asset Calculation (page 26)

The net admitted Deferred Tax Asset (DTA) calculated by the Company was overstated due to an incorrect application of the provisions of SSAP No. 10 (Income Taxes). An examination change was made to non-admit $126,406 of DTAs from the incorrect application of SSAP No. 10. In the future, the Company should calculate the net admitted DTAs using the proper application of the instructions included in SSAP No. 10.

Risk Transfer of PIPCO Agreement (page 27)

Due to the commutation of the 2006 agreement with PIPCO effective June 30, 2010, deposit accounting treatment is not required on a prospective basis for that agreement. The 2010 agreement and any future agreements with PIPCO should be evaluated for risk transfer, as defined in SSAP No. 62. If there is not sufficient transfer of risk for the 2010 agreement or any future reinsurance agreements, the Company should use deposit accounting pursuant to SSAP No. 75 and <u>not</u> reduce its reserves for losses and LAE reserves for balances ceded to PIPCO in any future Quarterly and Annual Statements.

Reporting of Unearned Premiums (page 28)

The Company should implement controls or crosscheck procedures to ensure that proper accounting entries are made in the future to fully record this component of unearned premiums.

Reporting of Advance Premium (page 28)

The Company should only report an advance premium liability for premiums received for a policy with a beginning effective date that is subsequent to the reporting date.

SUBSEQUENT EVENTS

PPIA's 2009 Annual Statement disclosed that the Company's Board of Directors voted to cancel the reinsurance agreement with PIPCO, effective March 31, 2010, in a meeting held on November 12, 2009. The Company executed an interim reinsurance agreement with PIPCO that was effective for the period from April 1, 2010 to June 30, 2010. Another reinsurance agreement was executed between PPIA and PIPCO that was effective for the period from July 1, 2010 to December 31, 2010. An evaluation of risk transfer, as defined in SSAP No. 62, for the two agreements executed in 2010 was not completed for the purposes of this examination.

PPIA's June 30, 2010 Quarterly Statement reported that the reinsurance agreements with PIPCO, which were effective from April 1, 2006 to June 30, 2010, were commuted on June 30, 2010. The premiums paid by PPIA to PIPCO over this period totaled $8.1 million. Ceded loss and LAE recoveries plus the commutation settlement received from PIPCO totaled $4.0 million during the same period. Therefore, in slightly over a four year period, PIPCO realized a gross profit of $4.1 million from its reinsurance transactions with PPIA.

ACKNOWLEDGMENT

The assistance and cooperation extended by the officers and the employees of Physicians Professional Indemnity Association during the course of this examination is hereby acknowledged and appreciated. In addition to the undersigned, Larry Kleffner, CFE and Timothy Carroll, examiners for the Missouri DIFP, and David Cox, actuary for the Missouri DIFP, participated in this examination. Jon Michelson, FCAS, MAAA, of Expert Actuarial Services, LLC, and Dale Ogden, ACAS, MAAA, of Dale F. Ogden & Associates, also participated as consulting actuaries.

VERIFICATION

State of Missouri)
)
County of)

I, Tim L. Tunks, on my oath swear that to the best of my knowledge and belief the above examination report is true and accurate and is comprised of only facts appearing upon the books, records or other documents of Physicians Professional Indemnity Association, its agents or other persons examined or as ascertained from the testimony of its officers or agents or other persons examined concerning its affairs and such conclusions and recommendations as the examiners find reasonably warranted from the facts.

____
Tim L. Tunks, CPA, CFE
Examiner-In-Charge
Missouri DIFP

Sworn to and subscribed before me this ______ day of _______, 2010.

My commission expires: ______________ ________________________
Notary Public

SUPERVISION

The examination process has been monitored and supervised by the undersigned. The examination report and supporting workpapers have been reviewed and approved. Compliance with NAIC procedures and guidelines as contained in the Financial Condition Examiners Handbook has been confirmed.

Mark A. Nance, CPA, CFE
Audit Manager
Missouri DIFP