

REPORT ON EXAMINATION

OF

PHYSICIANS' RECIPROCAL INSURERS

AS OF

DECEMBER 31, 2019

DATE OF REPORT

MAY 3, 2021

EXAMINER

TEENA JOSEPH, PIR

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## Department of Financial Services

**KATHY HOCHUL**  
Governor

**ADRIENNE A. HARRIS**  
Acting Superintendent

October 1, 2021

Honorable Adrienne A. Harris  
Acting Superintendent  
New York State Department of Financial Services  
Albany, New York 12257

Madam:

Pursuant to the requirements of the New York Insurance Law, and in compliance with the instructions contained in Appointment Number 32100 dated June 18, 2020, attached hereto, I have made an examination into the condition and affairs of Physicians' Reciprocal Insurers as of December 31, 2019, and submit the following report thereon.

Wherever the designation "the Reciprocal" or "PRI" appears herein without qualification, it should be understood to indicate Physicians' Reciprocal Insurers.

Wherever the term "Department" appears herein without qualification, it should be understood to mean the New York State Department of Financial Services.

Due to the Governor's Executive Order of New York State on PAUSE regarding the COVID-19 pandemic, the examination was conducted remotely.

This examination has determined that as of December 31, 2019, the Reciprocal was insolvent in the amount of \$149,804,669. Additionally, the Reciprocal's minimum required to be maintained surplus of \$650,000 was impaired in the amount of \$150,454,669.

## 1. SCOPE OF EXAMINATION

The Department has performed an examination of the Reciprocal, a single-state insurer. The previous examination was conducted as of December 31, 2014. This examination covered the 5-year period from January 1, 2015 through December 31, 2019. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

This examination was conducted in accordance with the National Association of Insurance Commissioners (“NAIC”) Financial Condition Examiners Handbook, which requires that we plan and perform the examination to evaluate the financial condition and identify current and prospective risks of the Reciprocal by obtaining information about the Reciprocal including corporate governance, identifying and assessing inherent risks within the Reciprocal and evaluating system controls and procedures used to mitigate those risks. This 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 New York laws, statutory accounting principles, and annual statement instructions.

This examination report includes, but is not limited to, the following:

- Reciprocal history
- Management and control
- Territory and plan of operation
- Reinsurance
- Holding company description
- Financial statement presentation
- Loss review and analysis
- Significant subsequent events
- Summary of recommendations

A review was also made to ascertain what action was taken by the Reciprocal with regard to the recommendations contained in the prior report on examination.

This report on examination is confined to financial statements and comments on those matters that involve departures from laws, regulations or rules, or that are deemed to require explanation or description.

## 2. DESCRIPTION OF RECIPROCAL

Physicians' Reciprocal Insurer is a reciprocal insurer, as defined in the New York Insurance Law ("NYIL") Section 107(a)(37) and was organized pursuant to the provisions of Article 61 of the NYIL. As promulgated by Section 6102(b) of the NYIL, the Superintendent approved the declaration creating the Reciprocal on November 6, 1981. The Reciprocal was incorporated under the laws of the State of New York on June 1, 1982. It became licensed and commenced business on June 22, 1982. The Reciprocal provides medical malpractice insurance, on both a claims-made and an occurrence basis, for physicians, chiropractors, dentists, other medical professionals, hospitals and healthcare facilities in New York State. Effective July 1, 1994, the Reciprocal began writing excess professional liability policies providing coverage of \$1 million over the limit of the underlying policy.

As PRI is a reciprocal insurer, its policyholders engage in the business of inter-insurance on the reciprocal plan. It has no employees and is owned by its subscribers. The Reciprocal's business and affairs are managed by an attorney-in-fact. The policyholders are, and may only be, subscribers. To provide surplus for the Reciprocal, the subscribers were required, as prerequisite to the initial purchase of their insurance policies, to contribute to the Reciprocal's surplus in varying amounts. Effective January 1, 1998, the Reciprocal eliminated the requirement that new subscribers contribute to surplus.

In 2017, the Reciprocal formed PRIMMA, LLC ("PRIMMA") as a wholly-owned subsidiary. Effective July 6, 2017, PRIMMA serves as PRI's attorney-in-fact.

### A. Corporate Governance

Pursuant to a declaration, which was executed and approved in accordance with Section 6102 of the NYIL, an advisory committee/board of governors was elected to act on behalf of the subscribers with the power to supervise and control the attorney-in-fact and to control the investment activities of the Reciprocal, as well as such other powers as may be conferred by the subscribers' agreement.

Pursuant to Section 6105(h) of the NYIL and to the subscribers' agreement, the advisory committee/board of governors shall consist of at least nine individuals elected by the subscribers. The board meets once a month during each calendar year. At December 31, 2019, the advisory committee/board of governors was comprised of the following six members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Thomas Chan, M.D. Great Neck, NY	Physician, Private Practice Physician
Barry Fisher, M.D. Old Brookville, NY	Physician, Private Practice Physician
Brian Nolan Wallingford, CT	Executive Vice President, PRIMMA, LLC
Craig Rosenberg, M.D. Glen Cove, NY	Physician, Glen Cove Hospital and South Side Hospital
Bruce C. Shulan Warren, NJ	President and Chief Executive Officer, PRIMMA, LLC
John Zaso, D.O. East Meadow, NY	Physician, Private Practice Physician

Section 6105(h) of the NYIL states, in part:

“The advisory committee shall meet at least annually and shall consist of at least nine individuals elected by the subscribers...”

The Reciprocal failed to have nine members of the advisory committee/board of governors as required by Section 6105(h) of the NYIL and the subscribers’ agreement. As of December 31, 2020, the Reciprocal had seven board members.

It is recommended that the Reciprocal comply at all times with Section 6105(h) of the NYIL and with the subscribers’ agreement with regard to the minimum number of advisory committee/board of governors.

As of December 31, 2019, the principal officers of the Reciprocal were as follows:

<u>Name</u>	<u>Title</u>
Bruce Shulan	President, Chief Executive Officer, Chief Restructuring Officer and Vice Chairman
Barry Fisher, M.D.	Chairman
Craig Rosenberg, M.D.	Secretary
John Zaso, D.O.	Treasurer

### Audit Committee Meetings

The audit committee charter states, in part:

“ . . . The audit committee shall meet at such times and from time to time as it deems to be appropriate, but not less than four times a year . . . ”

In reviewing the audit committee meeting minutes, the examiner noted that the audit committee failed to meet four times annually in 2018 and 2019, as required in the audit committee charter.

It is recommended that the Reciprocal ensure that the audit committee comply with its charter by having at least four meetings annually.

### Audit Committee Members

Department Regulation 118, Part 89.12(e) states:

“The Company shall provide written notification to the superintendent of the selection of its audit committee within 30 days of the effective date of this Part and within 30 days of any change in membership of the audit committee. The notice shall include a description of the reason for the change.”

Since February 8, 2018, the audit committee has been comprised of the entire PRI board of governors. In reviewing the audit committee minutes, it was noted that new members were elected to the PRI board in 2018 and 2019, in addition to resignations of multiple members from the PRI board during 2018 and 2019. The Reciprocal did not give written notice to the Superintendent within 30 days of change in the audit committee membership.

It is recommended that the Reciprocal notify the Department within 30 days of any change in membership of the audit committee, as required by Department Regulation 118, Part 89.12(e).

### Attorney-in-fact

As noted above, in 2017, the Reciprocal formed a wholly-owned subsidiary, PRIMMA. Pursuant to a management agreement dated July 6, 2017, PRIMMA was appointed as the Reciprocal’s attorney-in-fact and manager. Prior to the appointment of PRIMMA, Administrators for the Professions, Inc. (“AFP”), an unaffiliated entity, served as PRI’s attorney-in-fact and manager.

The Reciprocal entered into an amended management agreement with PRIMMA on April 13, 2018, which terminated and superseded the management agreement dated July 6, 2017. Pursuant to the terms of

the management agreement, PRIMMA manages the insurance operations of the Reciprocal, including, but not limited to, solicitation of subscribers, investigation of applicants, underwriting services, issuance of policy forms, cancellation of policies, claims reporting and processing, reinsurance, risk management, education, data processing, investment and accounting services. PRIMMA's compensation for its services under the management agreement shall be an amount equal to the total amount of all costs and expenses actually and reasonably incurred by PRIMMA for such year in the performance of its obligation as attorney-in-fact and manager of the Reciprocal plus \$1.00. In 2019, the Reciprocal reported approximately \$31.1 million in expenses under this agreement.

The Reciprocal notified the Department regarding the amended management agreement on April 13, 2018. The amendment was approved by the Department on May 23, 2018.

Section 6111(f) of the New York Insurance Law states, in part:

“...all material transactions between or among the reciprocal, its subscribers, the attorney-in-fact and any affiliate of the attorney-in-fact shall not be entered into, unless they have been filed with the superintendent at least thirty days prior thereto and the superintendent has not disapproved them...”

It is recommended that, in the future, the Reciprocal comply with Section 6111(f) of the New York Insurance Law.

B. Territory and Plan of Operation

As of December 31, 2019, the Reciprocal was licensed to write business in New York only.

As of the examination date, the Reciprocal was authorized to transact the kinds of insurance as defined in the following numbered paragraphs of Section 1113(a) of the New York Insurance Law:

<u>Paragraph</u>	<u>Line of Business</u>
3	Accident & health
13	Personal injury liability
14	Property damage liability
15	Workers' compensation and employers' liability
19	Motor vehicle and aircraft physical damage
29	Legal services

Based upon the lines of business for which the Reciprocal is licensed, and pursuant to the requirements of Articles 13, 41 and 61 of the New York Insurance Law, the Reciprocal is required to maintain a minimum surplus to policyholders in the amount of \$650,000.

The Reciprocal writes medical professional liability insurance for physicians, chiropractors, dentists, other medical professionals, hospitals, and healthcare facilities in New York State as well as excess coverage provided through participation in the New York State Hospital Excess Liability Pool (“the Pool”). The Reciprocal also offers general liability coverage to its insured hospitals, healthcare facilities, and nursing homes. Professional liability policies are issued on a claims-made and occurrence basis, while general liability and excess policies are issued on an occurrence basis only. The maximum physician limits that the Reciprocal writes are \$1.3 million per claim and \$3.9 million annual aggregate primary coverage. The Reciprocal provides an additional layer of excess insurance protection of \$1 million / \$3 million annual aggregate to eligible individual physicians who meet certain requirements through the Pool at no additional cost. The premiums for this excess coverage are paid through the Pool, a program funded by New York State. The Reciprocal also offers direct pay excess to physicians who are not eligible for excess coverage through the Pool.

The Reciprocal participates in the Medical Malpractice Insurance Pool (“MMIP”) based on its proportionate market share of the New York medical professional liability insurance market. As a writer of medical professional liability insurance in New York, the Reciprocal is required to share in the business of the MMIP. This entity is a state-created insurance pool designed to provide insurance to all physicians and medical professionals who cannot obtain medical professional liability insurance through the voluntary market.

The following schedule shows the direct premiums written by the Reciprocal for the period under examination:

<u>Calendar Year</u>	<u>Direct Premiums Written</u>
2015	\$301,540,822
2016	\$292,871,663
2017	\$186,931,906
2018	\$175,310,686
2019	\$171,194,337

The Reciprocal did not assume business during the period under examination. The decline in premium volume from 2015 to 2019 was primarily due to the entrance of risk retention groups into the

medical malpractice market starting in the 2014 and 2015 timeframe, which resulted in the Reciprocal losing some of its business to these new writers. Additionally, in 2017, the Reciprocal's management team was replaced with a new senior management team. This new team implemented a restructuring of the Reciprocal, including its underwriting strategy, which resulted in the Reciprocal non-renewing some business.

Effective October 1, 2014, the Reciprocal entered into an Adverse Loss Development Reinsurance Contract ("ALD Cover") with Pennsylvania Physicians Reciprocal Insurers ("PaPRI"). The ALD Cover provides that the Reciprocal assumes \$11,500,000 of losses in excess of PaPRI's \$4,800,000 retention for a deposit premium of \$4,500,000 to be paid by PaPRI to the Reciprocal. Up to \$6,500,000 of the \$11,500,000 coverage can be used by PaPRI to pay for uncollectible reinsurance from its other reinsurance contracts.

In addition, Article VII of the ALD Cover states that the Reciprocal will maintain an Experience Refund Account ("ERA") of the operating expenses (including daily expenses) of the PaPRI that will be initially credited with \$1,400,000. The total operating expenses paid from the ERA account as of December 31, 2019 was \$719,029. The remaining ERA balance as of December 31, 2019 was \$680,971. The transaction was approved by the Department and by the Pennsylvania Insurance Department.

#### C. Reinsurance Ceded

During the examination period, the Reciprocal entered into a health care liability per loss occurrence excess reinsurance contract with one authorized reinsurer. The reinsurance coverage provided a coverage of \$5,000,000 excess of \$5,000,000 per loss occurrence subject to a limit of \$15,000,000 ultimate net loss with respect to all loss occurrences. The Reciprocal placed 50% of the coverage. The agreement covered the Reciprocal's business classified as medical malpractice for physicians and hospitals and/or related medical facilities.

The Reciprocal entered into a professional liability reinsurance agreement with Futuro Insurance Company, Ltd. ("Futuro") with respect to its Separate Account – Neurological Surgery, P.C., effective June 30, 2014 and subsequently amended on numerous occasions. Futuro is an unauthorized Bermuda-domiciled captive company and a wholly-owned subsidiary of the Reciprocal. The Reciprocal cedes the first \$750,000 of each loss occurrence for professional liability claims with an aggregate limit of \$5,000,000 per policy year. The transaction was approved by the Department.

It is the Reciprocal's policy to obtain the appropriate collateral for its cessions to unauthorized reinsurers. Letters of credit and trust accounts obtained by the Reciprocal to take credit for cessions to unauthorized reinsurers were reviewed for compliance with Department Regulations 133 and 114, respectively. No exceptions were noted.

All significant ceded reinsurance agreements in effect as of the examination date were reviewed and found to contain the required clauses, including an insolvency clause meeting the requirements of Section 1308 of the New York Insurance Law.

Examination review found that the Schedule F data reported by the Reciprocal in its filed annual statement accurately reflected its reinsurance transactions. Additionally, management has represented that all material ceded reinsurance agreements transfer both underwriting and timing risk as set forth in the NAIC Accounting Practices and Procedures Manual, Statement of Statutory Accounting Principles ("SSAP") No. 62R. Representations were supported by appropriate risk transfer analyses and an attestation from PRIMMA's President and Chief Executive Officer and from PRIMMA's Executive Vice President. Additionally, examination review indicated that the Reciprocal was not a party to any finite reinsurance agreements. All ceded reinsurance agreements were accounted for utilizing reinsurance accounting as set forth in SSAP No. 62R.

D. Holding Company System

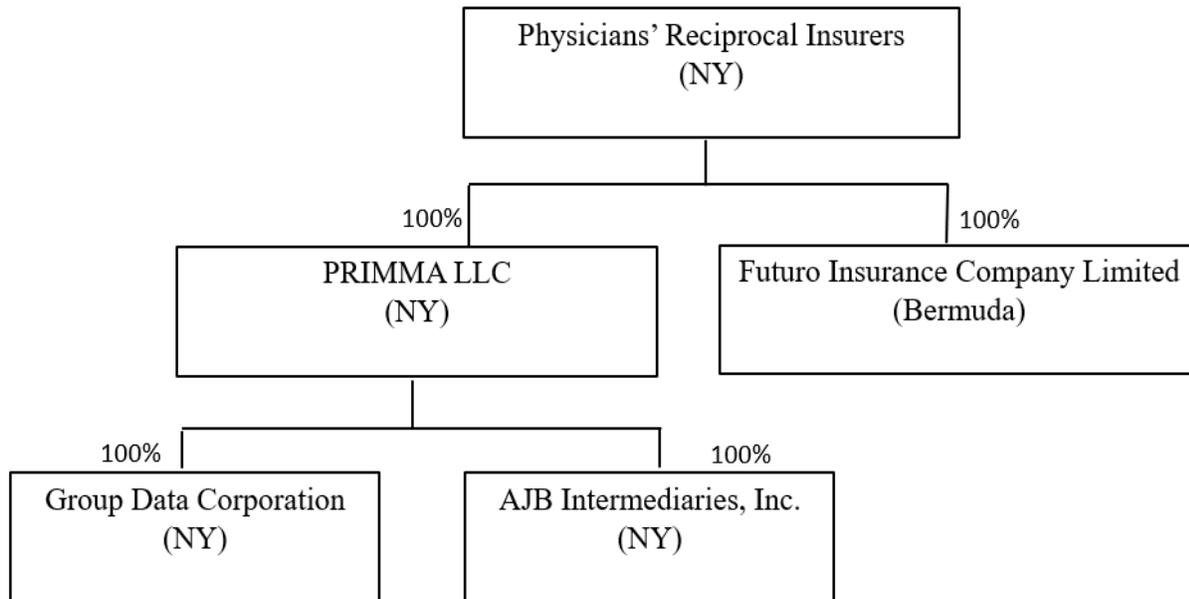
Effective June 3, 1999, the Reciprocal's wholly-owned subsidiary, Futuro, became licensed under the laws of Bermuda and was registered as a Class 3 Insurer under the Bermuda Insurance Act, 1978, with an initial capital contribution of \$1 million. This transaction was approved by the Department. As of December 31, 2019, the total capital contribution to the subsidiary was \$3,100,000.

On March 2, 2017, the Reciprocal formed a wholly-owned subsidiary, PRIMMA, which was authorized by the Department to serve as the attorney-in-fact and manager for the Reciprocal. Refer to section 2A of this report for further details regarding the management agreement between the Reciprocal and PRIMMA.

On December 20, 2017, PRIMMA acquired Group Data Corporation ("GDC"), a structured settlement corporation, which is currently dormant/inactive. When GDC was active, it placed structured annuities with various life insurance companies through its sub-licensee brokers from PRI's former attorney-in-fact, AFP.

On December 20, 2017, PRIMMA acquired AJB Intermediaries, Inc. (“AJB”), a reinsurance intermediary, which is currently dormant/inactive. When AJB was active, it placed reinsurance contracts for PRI, from PRI’s former attorney-in-fact, AFP.

The following is an unabridged of the holding company system at December 31, 2019:



#### E. Significant Ratios

The Reciprocal’s adjusted liabilities to liquid assets ratio of 152%, computed as of December 31, 2019, falls outside the benchmark range (which is not greater than 100%) as set forth in the Insurance Regulatory Information System of the NAIC.

The underwriting ratios presented below are on an earned/incurred basis and encompass the five-year period covered by this examination:

	<u>Amount</u>	<u>Ratio</u>
Losses and loss adjustment expenses incurred	\$869,107,258	73.17%
Other underwriting expenses incurred	249,306,742	20.99%
Net underwriting gain (loss)	<u>(69,349,740)</u>	<u>(5.84)%</u>
Premiums earned	<u>\$1,187,763,740</u>	<u>100.00%</u>

F. Accounts and Records

The Reciprocal did not obtain awareness letters from the Reciprocal's CPA firm for all years under examination.

Department Regulation 118, Part 89.4 states:

“The company shall obtain a letter from the CPA, and file a copy with the superintendent, stating that the CPA is aware of the provisions of the insurance law and the regulations thereunder of the state of domicile that relate to accounting and financial matters and affirming that the CPA will express his or her opinion on the financial statements in terms of their conformity to the statutory accounting practices prescribed or otherwise permitted by that insurance department, specifying such exceptions as the CPA may believe appropriate.”

It is recommended that the Reciprocal require the independent certified public accountant to provide an awareness letter on an annual basis pursuant to Department Regulation 118, Part 89.4.

### 3. FINANCIAL STATEMENTS

#### A. Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2019, as reported by the Reciprocal:

#### Assets

	<u>Assets</u>	<u>Nonadmitted</u> <u>Assets</u>	Net Admitted <u>Assets</u>
Bonds	\$614,948,708	\$ 0	\$614,948,708
Common stocks (stocks)	29,214,946	191,079	29,023,867
Cash, cash equivalents and short-term investments	49,118,165	0	49,118,165
Other invested assets	36,422,790	4,655,924	31,766,866
Receivables for securities	494,098	0	494,098
Investment income due and accrued	3,750,760	78,077	3,672,683
Uncollected premiums and agents' balances in the course of collection	25,170,912	704,489	24,466,423
Deferred premiums, agents' balances and installments booked but deferred and not yet due	35,731,285	0	35,731,285
Amounts recoverable from reinsurers	262,996	0	262,996
Current federal and foreign income tax recoverable and interest thereon	848,402	0	848,402
Receivables from parent, subsidiaries and affiliates	45,582	0	45,582
Deductible receivable	7,404,741	250,000	7,154,741
Admitted assets - Medical Malpractice Insurance Pool of New York State	148,180,639	10,592	148,170,047
Prepaid New York State income taxes	473,193	0	473,193
Notes receivable	333,459	333,459	0
Miscellaneous receivable	<u>36,374</u>	<u>8,175</u>	<u>28,199</u>
Total assets	<u>\$952,437,050</u>	<u>\$6,231,795</u>	<u>\$946,205,255</u>

Liabilities, Surplus and Other FundsLiabilities

Losses and loss adjustment expenses	\$1,023,762,818
Other expenses (excluding taxes, licenses and fees)	1,456,328
Unearned premiums	103,009,513
Advance premium	2,156,201
Ceded reinsurance premiums payable (net of ceding commissions)	3,069,154
Remittances and items not allocated	1,029,573
Payable for securities	1,045,474
Credit for discount on losses and lae reserves	(97,212,388)
Reinsurance deposit liability – adverse loss development cover	479,025
Miscellaneous liabilities	3,431,704
Premium deficiency reserve	453,418
Investment payable – MMIP	(4)
Funds held adverse loss development cover	<u>354,538</u>
Total liabilities	\$1,043,035,354

Surplus and Other Funds

Gross paid in and contributed surplus	\$ 25,131,767
Unassigned funds (surplus)	<u>(121,961,866)</u>
Surplus as regards policyholders	<u>(96,830,099)</u>
Total liabilities, surplus and other funds	\$ <u>946,205,255</u>

Note: The Internal Revenue Service has not audited tax returns covering tax years 2015 through 2019. The examiner is unaware of any potential exposure of the Reciprocal to any tax assessment and no liability has been established herein relative to such contingency.

B. Statement of Income

The net income for the examination period as reported by the Reciprocal was \$15,727,645, as detailed below:

Underwriting Income

Premiums earned		\$1,187,763,740
Deductions:		
Losses and loss adjustment expenses incurred	\$975,132,688	
Other underwriting expenses incurred	<u>249,306,742</u>	
Total underwriting deductions		<u>1,224,439,430</u>
Net underwriting gain or (loss)		\$ (36,675,690)

Investment Income

Net investment income earned	\$122,916,601	
Net realized capital gain	<u>11,492,293</u>	
Net investment gain or (loss)		134,408,894

Other Income

Net gain or (loss) from agents' or premium balances charged off	\$ (933,053)	
Finance and service charges not included in premiums	395,755	
Discount on loss and lae reserves	(92,179,607)	
Miscellaneous income – MMIP	12,230,633	
Miscellaneous expense	(2,850,720)	
Adverse loss development cover – amortization loss	<u>(259,063)</u>	
Total other income		<u>(83,596,055)</u>
Net income before dividends to policyholders but before federal and foreign income taxes		\$ 14,137,149
Dividends to policyholders		<u>0</u>
Net income after dividends to policyholders but before federal and foreign income taxes		\$ 14,137,149
Federal and foreign income taxes incurred		<u>(1,590,496)</u>
Net income		\$ <u>15,727,645</u>

C. Capital and Surplus

Surplus as regards policyholders decreased \$10,811,435 during the five-year examination period January 1, 2015 through December 31, 2019, as reported by the Reciprocal, detailed as follows:

Surplus as regards policyholders as reported by the Reciprocal as of December 31, 2014			\$(86,018,664)
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income	\$15,727,645		
Net unrealized capital gains or (losses)	0	\$18,311,510	
Change in net deferred income tax	24,672,234		
Change in nonadmitted assets	0	25,649,864	
Change in subscriber balance	<u>0</u>	<u>7,249,940</u>	
Total gains and losses	\$40,399,879	\$51,211,314	
Net increase (decrease) in surplus			<u>(10,811,435)</u>
Surplus as regards policyholders as reported by the Reciprocal as of December 31, 2019			<u>\$(96,830,099)</u>

Gross paid in and contributed surplus is \$25,131,767. Gross paid in and contributed surplus has not changed during the examination period.

D. Analysis of Changes to Surplus

Surplus as regards policyholders as reported by the Reciprocal as of December 31, 2019	\$(96,830,099)
Increase (decrease) in surplus due to examination adjustment to loss and loss adjustment expenses	(46,180,182)
Increase (decrease) in surplus due to examination adjustment on discount to loss and loss adjustment expenses	<u>(6,794,388)</u>
Surplus as regards policyholders as of December 31, 2019, after examination adjustments	<u>\$(149,804,669)</u>

This examination has determined that as of December 31, 2019, the Reciprocal was insolvent in the amount of \$149,804,669. Additionally, the Reciprocal's minimum required to be maintained surplus of \$650,000 was impaired in the amount of \$150,454,669.

E. Analysis of Changes to Income

Net income for the examination period, as reported by the Reciprocal	\$ 15,727,645
Increase (decrease) in income due to reversal of prior examination adjustment to loss and loss adjustment expenses	131,000,000
Increase (decrease) in income due to reversal of prior examination adjustment to discount on loss and loss adjustment expenses	28,000,000
Increase (decrease) in income due to examination adjustment to loss and loss adjustment expenses	(46,180,182)
Increase (decrease) in income due to examination adjustment to discount on loss and loss adjustment expenses	<u>(6,794,388)</u>
Net gain (loss) for the examination period, after examination adjustments	<u>\$121,753,075</u>

#### 4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination net undiscounted liability for the captioned items of \$1,069,943,000 is \$46,180,182 more than the \$1,023,762,818 reported by the Reciprocal in its filed annual statement as of December 31, 2019. The examination analysis of the loss and loss adjustment expense reserves was conducted in accordance with generally accepted actuarial principles and statutory accounting principles, including SSAP No. 55.

Section 1303 of the New York Insurance Law states, in part:

“Every insurer shall . . . maintain reserves in an amount estimated in the aggregate to provide for the payment of all losses or claims incurred on or prior to the date of statement, whether reported or unreported, which are unpaid as of such date and for which such insurer may be liable, and also reserves in an amount estimated to provide for the expenses of adjustment or settlement of such losses or claims.”

Further, Paragraph 10 of SSAP No. 55 states, in part:

“The liability for claim reserves and claim liabilities, unpaid losses, and loss/claim adjustment expenses shall be based upon the estimated ultimate cost of settling the claims (including the effects of inflation and other societal and economic factors), using past experience adjusted for current trends, and any other factors that would modify past experience . . .”

The Reciprocal’s carried gross and net reserves fall within the Department’s range of reasonable reserves. The Reciprocal’s prior years’ unfavorable loss and loss adjustment expense runoff trend has been mitigated under the new management team, which has been in place since 2017. The Department also observed that the Reciprocal’s loss ratios for the most recent years have improved under the new management team.

By virtue of the Reciprocal’s 15-month loss and loss adjustment expense adverse runoff for accident years 2019 and prior, as reported by the Reciprocal in its filed March 31, 2021 quarterly statement, the Reciprocal has already acknowledged an undiscounted loss and loss adjustment expense reserve deficiency of \$7.744 million, representing 16.8% of the Department’s indicated deficiency of \$46.18 million.

It is recommended that the Reciprocal continue its efforts to strengthen the loss and loss adjustment expense reserves and book adequate reserves, pursuant to the provisions of Section 1303 of the New York Insurance Law and SSAP No. 55.

## **5. CREDIT FOR DISCOUNT LOSSES AND LOSS ADJUSTMENT EXPENSE RESERVES**

The examination liability for the captioned item of \$(90,418,000) is \$6,794,388 less than the \$(97,212,388) reported by the Reciprocal in its filed annual statement as of December 31, 2019.

The examination adjustment was due to selection of a lower interest rate for certain years to discount examination loss and loss adjustment expenses reserves. Pursuant to Section 4117(e) of the New York Insurance Law, the Department has allowed the Reciprocal to discount its loss and loss adjustment expense reserves.

## **6. SUBSEQUENT EVENTS**

On March 11, 2020, the World Health Organization declared an outbreak of a novel coronavirus (“COVID-19”) pandemic. The COVID-19 pandemic has continued to develop throughout 2020 and 2021, with significant uncertainty remaining regarding the full effect of COVID-19 on the U.S. and global insurance and reinsurance industry. At the time of releasing this report, the examination’s review noted that there has not been a significant impact to the Reciprocal’s current reserves. The Department has been in communication with the Reciprocal regarding the impact of COVID-19 on its business operations and financial position. The Department continues to closely monitor the impact of the pandemic on the Reciprocal and will take necessary action if a solvency concern arises.

On July 7, 2020, the Reciprocal acquired, from Sirius America Insurance Company, 19,515 shares of common stock representing all of the authorized, issued and outstanding common stock of Empire Insurance Company (“Empire”) for cash consideration \$11,488,152. This transaction was approved by the Department on June 26, 2020. On July 22, 2020, Empire was renamed EmPRO Insurance Company (“EmPRO”).

On July 27, 2020, the Reciprocal contributed funding to EmPRO through the purchase, in cash, of a \$100 million interest-bearing surplus note which is due in full on December 31, 2030. At September 30, 2020, there was an unaccrued interest on the surplus note of \$328,562. This amount was approved by the Department for payment.

Effective August 19, 2020, PRIMMA became the manager of EmPRO under the terms of the management and service agreement. On the same date, PRIMMA, EmPRO and the Reciprocal became parties to an intercompany services and cost allocation agreement. Effective August 26, 2020, the

Reciprocal and EmPRO entered into a tax allocation agreement. These agreements were approved by the Department on August 19, 2020.

## 7. CONCLUSION

This examination has determined that as of December 31, 2019, the Reciprocal was insolvent in the amount of \$149,804,669. Additionally, the Reciprocal's minimum required to be maintained surplus of \$650,000 was impaired in the amount of \$150,454,669.

## 8. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report on examination contained 24 recommendations as follows (page numbers refer to the prior report):

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Surplus Impairment</u>	
<p>This examination has determined that as of December 31, 2014, the Company was insolvent in the amount of \$295,705,493, and its capital of \$650,000 was impaired in the amount of \$296,355,493. Additionally, the Company's minimum required to be maintained surplus of \$650,000 was impaired in the amount of \$296,355,493.</p> <p>This report on examination contains a similar comment.</p>	20, 26
B. <u>Board Compensation</u>	
<p>i. It was recommended that the Company's board approve all compensation paid to its board members.</p> <p>The Reciprocal has complied with this recommendation.</p>	6
<p>ii. It was recommended that the Company and its manager re-evaluate the compensation of the board members to determine if it is reasonable given the Company's poor financial condition.</p> <p>The Reciprocal has complied with this recommendation.</p>	6
<p>iii. It was recommended that board members who engage in consulting services for the Company disclose any such services they perform in their conflict of interest statements completed annually.</p> <p>The Reciprocal has complied with this recommendation.</p>	6
C. <u>Executive Compensation</u>	
<p>i. It was recommended the Company's board discuss and approve its executive compensation and ensure that documentation of the board actions is maintained in the minutes.</p> <p>The Reciprocal has complied with this recommendation.</p>	7

- ii. It was recommended that the Company maintain documents for the bases of allocating salaries of its executive officers between itself and its manager, as required by Department Regulation No. 30, Part 109.2 (b)(2). 7
- The Reciprocal has complied with this recommendation.
- iii. It was recommended that the Company, as well as its manager, maintain the basis of determining bonuses paid to employees. 7
- The Reciprocal has complied with this recommendation.
- iv. It was also recommended that the board approve employee bonuses and document such approvals in the minutes of the board. 7
- The Reciprocal has complied with this recommendation.
- D. Conflict of Interest Transactions
- i. It was recommended that the Company ensure that AFP file its lease extension with Department in accordance with NYIL Section 6111(f). 8
- This recommendation is no longer applicable.
- ii. It was recommended that the Company ensure that its board member disclose the transaction in the conflict of interest statement completed annually. 8
- This recommendation is no longer applicable.
- iii. It was recommended that the Company ensure its manager's owner disclose the transaction in his conflict of interest statements completed annually as a Company board member. 9
- This recommendation is no longer applicable.
- iv. It was recommended that the Company and its manager file the agreement with the Department as required by NYIL Section 6111(f). 9
- This recommendation is no longer applicable.
- E. Accounts and Records
- i. Custodian Agreement 14
- It was recommended that the Company ensure its custodial agreement meets all of the required provisions as set forth in the NAIC Financial Condition Examiners' Handbook.
- The Reciprocal has complied with this recommendation.

- ii. Investment Policy Statement  
It was recommended that the Company comply with Section IV of its investment policy statement regarding its investment limitation. 15
- The Reciprocal has complied with this recommendation.
- iii. Compliance with Management Agreement  
It was recommended that the Company comply with the requirements in Paragraph 5 of the Management Agreement. 15
- The Reciprocal has complied with this recommendation.
- iv. Management Fee Determination  
It was recommended that the Company calculate its management fees as prescribed by the agreement. 16
- The Reciprocal has complied with this recommendation.
- It was recommended that AFP reimburse PRI for its overpayment to AFP resulting from incorrectly including MMIP's premiums in calculating management fees. 17
- This recommendation is no longer applicable.
- F. Anticipated Future Investment Income on Losses and LAE Reserves
- It was recommended that the Company address its ongoing reserving inadequacies and increase its carried reserves to an appropriate level, pursuant to the provisions of NYIL Section 1303 and Paragraph 10 of SSAP No. 55. 23
- The Reciprocal has not complied with this recommendation. A similar recommendation is made in this report on examination.
- G. Bonds
- It was recommended that the Company value its bond investments in accordance with SSAP No. 26. 24
- The Reciprocal has complied with this recommendation.
- H. Other Invested Assets
- i. It was recommended that the Company value its investment in partnerships in accordance with SSAP Nos. 48 and 97. 25
- The Reciprocal has complied with this recommendation.

- ii. It was recommended that the Company limit its partnership investments to not more than one percent of its admitted assets, pursuant to the provisions of NYIL Section 1404 (8)(A)(i) and (B)(ii). 25

The Department no longer views this section of the law as applicable to the specific invested asset.

- iii. It was recommended that the Company report partnership asset of a doubtful value in accordance with NYIL Section 1302 (b). 25

The Reciprocal has complied with this recommendation.

- iv. It was recommended that the Company report any ineligible amount of partnership's investment in compliance with NYIL Section 1412 (b). 25

The Reciprocal has complied with this recommendation.

- v. It was recommended that the Company be guided by NYIL Section 6101(e) when investing its funds. 25

The Reciprocal has complied with this recommendation.

## 9. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Insolvency</u> This examination has determined that as of December 31, 2019, the Reciprocal was insolvent in the amount of \$149,804,669. Additionally, the Reciprocal's minimum required to be maintained surplus of \$650,000 was impaired in the amount of \$150,454,669.	16, 19
B. <u>Corporate Governance</u>	
i. It is recommended that the Reciprocal comply at all times with Section 6105(h) of the NYIL and the subscribers' agreement with regard to the minimum number of board of governors.	4
ii. It is recommended that the Reciprocal ensure that the audit committee complies with its charter by having at least four meetings annually.	5
iii. It is recommended that the Reciprocal notify the Department within 30 days of any change in membership of the audit committee as required by Department Regulation 118, Part 89.12(e).	5
iv. It is recommended that, in the future, the Reciprocal comply with Section 6111(f) of the New York Insurance Law.	6
C. <u>Accounts and Records</u> It is recommended that the Reciprocal require the independent certified public accountant to provide an awareness letter on an annual basis pursuant to Department Regulation 118, Part 89.4.	11
D. <u>Losses and loss adjustment expense reserves</u> It is recommended that the Reciprocal continue its efforts to strengthen the loss and loss adjustment expense reserves and book adequate reserves, pursuant to the provisions of Section 1303 of the New York Insurance Law and SSAP No. 55.	17

Respectfully submitted,

\_\_\_\_\_/S/\_\_\_\_\_  
Teena Joseph  
Senior Insurance Examiner

STATE OF NEW YORK     )  
  )ss:  
COUNTY OF NEW YORK    )

Teena Joseph, being duly sworn, deposes and says that the foregoing report, subscribed by her, is true to the best of her knowledge and belief.

\_\_\_\_\_/S/\_\_\_\_\_  
Teena Joseph

Subscribed and sworn to before me

this \_\_\_\_\_ day of \_\_\_\_\_, 2021.

*APPOINTMENT NO. 32100*

*NEW YORK STATE*

***DEPARTMENT OF FINANCIAL SERVICES***

*I, Linda A. Lacewell, Superintendent of Financial Services of the State of New York, pursuant to the provisions of the Financial Services Law and the Insurance Law, do hereby appoint:*

***Teena Joseph***

*as a proper person to examine the affairs of the*

***Physicians' Reciprocal Insurers***

*and to make a report to me in writing of the condition of said*

***COMPANY***

*with such other information as she shall deem requisite.*

*In Witness Whereof, I have hereunto subscribed by name  
and affixed the official Seal of the Department  
at the City of New York*

*this 18<sup>th</sup> day of June, 2020*

***LINDA A. LACEWELL***  
*Superintendent of Financial Services*

*By:*

*Joan L. Riddell*

\_\_\_\_\_  
*Joan Riddell*  
*Deputy Bureau Chief*

