

JUN 2 2016

CERTIFICATION

FILED

June 2, 2016

I, Bruce R. Ramage, Director of Insurance of the State of Nebraska, do hereby certify that the attached is a full and correct copy of the

Financial Examination Report of

PREFERRED PROFESSIONAL INSURANCE COMPANY

as of

December 31, 2014

The report is now on file and forming a part of the records of this Department.

I hereto subscribe my name under the seal of my office at Lincoln, Nebraska.



Bruce R. Ramage
DIRECTOR OF INSURANCE

CERTIFICATE OF ADOPTION

Take notice that the proposed report of the financial examination of

PREFERRED PROFESSIONAL INSURANCE COMPANY

dated as of December 31, 2014, verified under oath by the examiner-in-charge on April 13, 2016, and received by the company on April 27, 2016, has been adopted without modification as the final report pursuant to Neb. Rev. Stat. § 44-5906(3)(a).

Dated this 27 day of April, 2016.

STATE OF NEBRASKA
DEPARTMENT OF INSURANCE



Justin Schrader
Chief Financial Examiner

STATE OF NEBRASKA

Department of Insurance

EXAMINATION REPORT

OF

PREFERRED PROFESSIONAL INSURANCE COMPANY

as of

December 31, 2014



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Omaha, Nebraska
March 15, 2016

Honorable Bruce R. Ramage
Director of Insurance
Nebraska Department of Insurance
941 "O" Street, Suite 400
Lincoln, Nebraska 68508

Dear Sir:

Pursuant to your instruction and authorizations, and in accordance with statutory requirements, an examination has been conducted of the financial condition and business affairs of:

**PREFERRED PROFESSIONAL INSURANCE COMPANY
11605 Miracle Hills Drive, Suite 200
Omaha, Nebraska 68154**

(hereinafter also referred to as the "Company") and the report of such examination is respectfully presented herein.

INTRODUCTION

The Company was last examined as of December 31, 2010 by the State of Nebraska. The current financial condition examination covers the intervening period to, and including, the close of business on December 31, 2014, and includes such subsequent events and transactions as were considered pertinent to this report. The State of Nebraska participated in this examination and assisted in the preparation of this report.

SCOPE OF EXAMINATION

This examination was conducted pursuant to and in accordance with both the NAIC Financial Condition Examiners Handbook (Handbook) and Section §44-5904(1) of the Nebraska Insurance Statutes. The Handbook requires that examiners plan and perform the examination to evaluate the financial condition and identify prospective risks of the Company by obtaining

information about the Company including, but not limited to: corporate governance, identifying and assessing inherent risks within the Company, and evaluating system controls and procedures used to mitigate those risks. The examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation and management's compliance with Statutory Accounting Principles and Annual Statement Instructions, when applicable to domestic state regulations.

A general review was made of the Company's operations and the manner in which its business has been conducted in order to determine compliance with statutory and charter provisions. The Company's history was traced and has been set out in this report under the caption "Description of Company." All items pertaining to management and control were reviewed, including provisions for disclosure of conflicts of interest to the Board of Directors and the departmental organization of the Company. The Articles of Incorporation and By-Laws were reviewed, including appropriate filings of any changes or amendments thereto. The minutes of the meetings of the shareholder, Board of Directors and committees, held during the examination period, were read and noted. Attendance at meetings, proxy information, election of Directors and Officers, and approval of investment transactions were also noted.

The fidelity bond and other insurance coverages protecting the Company's property and interests were reviewed, as were plans for employee welfare and pension. Certificates of Authority to conduct the business of insurance in the various states were inspected and a survey was made of the Company's general plan of operation.

Data reflecting the Company's growth during the period under review, as developed from the Company's filed annual statements, is reflected in the financial section of this report under the caption "Body of Report."

The Company's reinsurance facilities were ascertained and noted, and have been commented upon in this report under the caption "Reinsurance." Accounting records and procedures were tested to the extent deemed necessary through the risk-focused examination process. The Company's method of claims handling and procedures pertaining to the adjustment and payment of incurred losses were also noted.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This included a review of workpapers prepared by PricewaterhouseCoopers, LLP, the Company's external auditors, during their audit of the Company's accounts for the year ended December 31, 2014. Portions of the auditor's workpapers have been incorporated into the workpapers of the examiners and have been utilized in determining the scope and areas of emphasis in conducting the examination. This utilization was performed pursuant to Title 210 (Rules of the Nebraska Department of Insurance), Chapter 56, Section 013.

Any failure of items to add to the totals shown in schedules and exhibits appearing throughout this report is due to rounding.

DESCRIPTION OF COMPANY

HISTORY

The Company was incorporated under the laws of the State of Nebraska on June 30, 1976, and commenced business on July 1 of that same year as a mutual insurance association under the provisions of LB 809, Second Session, 84th Legislature, with its offices located in Omaha, Nebraska. The Articles of Incorporation were amended on July 9, 1976 to provide for perpetual existence as a mutual company. The Articles were again amended on July 11, 1979 to allow for the Company to operate as a not-for-profit corporation by limiting its membership to hospitals which

were organized exclusively for religious, charitable, educational, or scientific purposes. It then became qualified as a Federal Income Tax exempt corporation.

Effective February 22, 1985, the Articles of Incorporation were amended to expand the membership to include “for profit” hospitals, this effectively removed the Company's tax-exempt status. The Articles of Incorporation were restated effective March 26, 1986, to convert the Company's operations to that of a non-assessable mutual insurance company, whereby no member would be liable for any debt obligations of the Company. In a subsequent restatement of its Articles of Incorporation, effective December 11, 1987, the Company's name was changed from Hospital Mutual Insurance Company to Preferred Physicians Insurance Company, and its corporate structure was changed to that of a stock insurance company.

The shareholders of Preferred Physicians Insurance Company (PPIC) and Consolidated Catholic Casualty Risk Retention Group (CCCRRG) approved a business combination effective October 1, 1998. Simultaneous to the business combination, CCCRRG assumed a run-off position for its existing liability portfolio. At the same time, by way of dividends from both companies, an eleven-owner system became shareholders of the continuing PPIC. PPIC assumed the excess liability insurance business previously written by CCCRRG upon renewal. The name of the Company was then changed from Preferred Physicians Insurance Company to Preferred Professional Insurance Company.

Effective August 1, 2014, the Company restated its Articles of Incorporation in connection with its Agreement and Plan of Merger with ProMutual Group, Inc. (ProMutual). As a result of the restatement, the number of shares the Company is authorized to issue was changed to 100 shares, all of which are of a par value of \$1.00 each. This was further amended on December 19, 2014 to

change the number of shares the Company is authorized to issue to 100,000 shares, all of which are of a par value of \$50.00 each and are of the same class and are common shares.

The Company is authorized by its Articles of Incorporation to transact and write all types of insurance and reinsurance authorized by the Nebraska Insurance Code, with the exception of life insurance, title insurance, and variable annuities. The Company’s current Certificate of Authority authorizes the Company to write the lines of insurance as provided under Section 44-201 Paragraphs 4, 5, 7, 8, 9, 10, 11, 12, and 18 of the Nebraska Insurance Laws.

MANAGEMENT AND CONTROL

Holding Company

The Company is a member of an insurance holding company system as defined by Nebraska Statute. An organizational listing flowing from the “Ultimate Controlling Person,” as reported in the 2014 Annual Statement, is represented by the following (subsidiaries are denoted through the use of indentations, and unless otherwise indicated, all subsidiaries are 100% owned):

- Medical Professional Mutual Insurance Company
- ProMutual Group, Inc.
- Coverys Specialty Insurance Company
- Preferred Professional Insurance Company
- Physicians Consultants, Inc.
- ProMutual Insurance Agency, Inc.
- ProSelect Insurance Company
- ProSelect National Insurance Company, Inc.

Shareholder

Article II, Section 2 of the Company’s First Amendment to the By-Laws provides that, “annual meetings of the shareholders, commencing with the year 2015, shall be held before June 30, at such place and time as the Board of Directors may determine, at which they shall elect by

majority vote a Board of Directors, receive the report of the Officers and Directors, and transact such other business as may properly be brought before the meeting.”

On August 1, 2014 the Company was acquired by ProMutual which is a wholly owned subsidiary of Medical Professional Mutual Insurance Company (MPMIC), a property and casualty insurance company domiciled in Massachusetts. Prior to the purchase, the Company had 5,305,944 shares of outstanding common stock that were issued among eighteen ownership companies. In connection to the acquisition, the number of outstanding shares was amended. Article II of the Company’s Amended and Restated Articles of Incorporation state that, “the number of shares the Company is authorized to issue is 100 shares, all of which are of a par value of \$1.00 each and are of the same class and are common shares.” Article II was further amended December 19, 2014 to state that, “the number of shares of the Company is authorized to issue is 100,000 shares, all of which are of a par value of \$50.00 each and are of the same class and are common shares.” ProMutual owns all of the shares of the Company.

In connection with the August 1, 2014 acquisition by ProMutual, the Company issued an extraordinary dividend to its former shareholders. The Company was authorized by the Nebraska Department of Insurance to pay an extraordinary dividend in an amount up to \$99,963,984.96 to its shareholders of record as of July 28, 2014. The actual amount paid to the former shareholders through the extraordinary dividend was \$80,013,636.

Board of Directors

Article V, Section 1 of the Company's Amended By-Laws provides that, “the number of Directors shall be fixed by resolution of the Board of Directors, but shall not be less than five. At all times, at least one Director shall be a resident of the state of Nebraska and at least one-fifth of all Directors shall be persons who are not Officers or employees of the Company.” Article V,

Section 2 of the Company's Amended By-Laws provides that, "the Directors, other than the first Board of Directors, shall be elected at the annual meeting of the shareholders, and each Director elected shall serve until the next succeeding annual meeting and until his successor shall have been elected and qualified."

The following persons were serving as Directors at December 31, 2014:

<u>Name and Residence</u>	<u>Principal Occupation</u>
Gregg L. Hanson North Attleboro, Massachusetts	President and Chief Executive Officer, MPMIC
Richard G. Hayes Beverly, Massachusetts	Senior Vice President and Chief Financial Officer, MPMIC
Lynnette M. Matza Omaha, Nebraska	President and Chief Executive Officer of the Company
Donna Miele-Cesario Winthrop, Massachusetts	Chief Information Officer and Chief Claims Officer, MPMIC
Mary L. Ursul Grand Rapids, Michigan	Executive Vice President, MPMIC

Officers

Article VIII, Section 1, of the Company's Amended By-Laws provides that, "the Officers of the Company shall be a chosen by the Board of Directors and shall be a President, a Vice President, a Secretary and a Treasurer, none of whom need be a member of the Board. The Board of Directors may also choose additional Vice Presidents, one or more Assistant Secretaries and Assistant Treasurers, and such other Officers and agents as it shall deem necessary."

The following is a listing of Officers elected and serving the Company at December 31, 2014:

<u>Name</u>	<u>Office</u>
Lynnette M. Matza	President and Chief Executive Officer
Anders G. Backlund	Senior Vice President, Claims and Chief Risk Officer
Denise A. Hill	Senior Vice President, General Counsel and Chief Compliance Officer
James T. McCoy	Senior Vice President, Insurance Operations, Chief Underwriting Office and Assistant Secretary
Karen A. Riley	Senior Vice President, Finance, Chief Financial Officer and Assistant Treasurer
James O. Walters	Senior Vice President, Information Systems and Chief Information Officer
Ann R. Wozny	Vice President, Business Development
Donna Miele-Cesario	Secretary
Richard G. Hayes	Treasurer

TRANSACTIONS WITH AFFILIATES

Employee Leasing Agreement

The Company has an Employee Leasing Agreement with its wholly owned subsidiary, Physicians Consultants, Inc. (PCI). Services rendered to PCI include 1) soliciting, writing, and servicing insurance accounts sold by PCI issued through the Company, 2) general administrative support of PCI, and 3) clerical support as necessary. The Company is responsible for all licensing and documentation of hours spent on services performed.

Service Agreement

The Company and PCI have also entered into a Service Agreement whereby the Company appoints PCI as its agent representative. PCI shall pay the Company for the actual cost for assets, supplies, and services rendered to PCI not covered by any other agreement and the Company will pay a commission for insurance services rendered on the Company's behalf.

Tax Sharing Agreement

The Company entered into a Tax Sharing Agreement with PCI that was executed on June 6, 2003. Through July 31, 2014, the Company was a separate federal taxpayer and filed a consolidated

income tax return with its subsidiary PCI. Effective August 1, 2014 the Company and PCI became part of the MPMIC tax group and will be included in MPMIC's federal income tax filings.

Management and Service Agreement

Effective January 1, 2013, the Company entered into a Management and Service Agreement with PPRRG, a risk retention group domiciled in the District of Columbia. Under the agreement the Company provides underwriting, claims, financial and general management services to PPRRG.

TERRITORY AND PLAN OF OPERATION

As evidenced by current or continuous Certificates of Authority, the Company is licensed to transact business in all states and the District of Columbia.

The Company has been and continues to be a direct writer of insurance coverages, with all underwriting and marketing performed by employees of the Company or through an agreement with PCI, a wholly-owned subsidiary. The Company's plan of operation for its legacy business is to support the Catholic healthcare ministry of its former shareholders by providing a wide array of insurance products and related services to preferred physicians and other healthcare providers. Physicians and healthcare providers who are unaffiliated with the former shareholders, but who maintain a business relationship with the former shareholders are also provided these products and services.

All claims, other than most of the fronted programs, the auto programs, and the workers compensation programs, are handled by the home office claims department in Omaha, Nebraska. Procedures and guidelines are established and monitored by the claims department. Contracts are in place with qualified third party administrators for the fronted programs, the auto programs, and the workers compensation programs insured by the Company but not handled by the home office claims department.

Through the acquisition of the Company, new agency affiliations have been made available within the new holding company structure. The Company has expanded its marketing distribution to include agencies already identified within the holding company structure, owned by MPMIC. Also, as part of MPMIC's strategy, the Company is tasked with expanding its footprint in specific states. The Company selects and utilizes agencies within these states, where prospective opportunity is identified.

REINSURANCE

Assumed

The Company assumes Healthcare Provider Professional Liability insurance from Catholic Relief Insurance Company of America (CRIC) covering healthcare providers and employed attorneys for Catholic Mutual Relief Society of America (CMRS). The Company provides coverage of \$800,000 excess of \$200,000 of ultimate net loss each insured with one or two exceptions where limits of \$1,800,000 excess of \$200,000 were provided, each loss of Not-For-Profit Professional Liability and related General Liability business. In all cases the limits provided are retroceded under the physician and surgeon treaty in place at that time with the current coverages noted in this report under the "Reinsurance – Ceded; Non-Fronted Physician and Surgeon" section below.

The Company assumes Physician Professional, Umbrella Liability, and Long Term Care Professional and General Liability risk from Covenant Health System Insurance, Ltd. (CHSIL), a wholly-owned Cayman captive insurer of Covenant Health System, a former shareholder of the Company. This business is assumed under facultative contracts and retroceded under excess facultative agreements.

Multiple facultative contracts are issued for the Physician Professional Liability assumed from CHSIL. These risks are retroceded as described under “Reinsurance-Ceded; Non-Fronted Physician and Surgeon” section below.

The Company assumes reinsurance from its affiliate, PPRRG effective April 26, 2013. This excess of loss contract covers policies issued by PPRRG providing professional liability to physicians and surgeons and related health care providers and medical facilities. PPRRG retains \$50,000 of any one loss and the Company is liable for all incurred losses in excess of \$50,000.

Effective January 1, 2014, the Company entered a reinsurance agreement with Healthspan Integrated Care (Healthspan) that terminated December 31, 2014. The Company assumed risks related to Individual Commercial HMO and Group Commercial HMO Members written by Healthspan that covered specific medical services. Healthspan retained the first \$500,000, as well as 10% of all covered services, with the exception of inpatient unscheduled transplant services, where Healthspan retained 50%. The Company retroceded the risks assumed from Healthspan as noted under the “Reinsurance-Ceded; Non-Fronted Other Lines” section below.

Non-Fronted Physician and Surgeon

Effective January 1, 2014, the Company entered into a 65% quota share agreement with various Lloyd’s of London Syndicates (#510, #609, #727, #1084, #1225, #1729, #2001, and #4020). The Company cedes 65% of its liability under policies classified as e-MD™/Medefense™ Plus Network Security and Privacy business for healthcare providers.

Effective from July 1, 2014 until June 30, 2015, the Company entered into an excess of loss reinsurance agreement providing coverage for Medical Professional Liability and related General Liability, Healthcare Provider Professional Liability, Miscellaneous Healthcare Facility

Liability, and Employed Attorneys and Healthcare Provider Professional Liability business assumed from CRIC. The Company has entered into similar agreements for the period of July 1 to June 30 for prior years.

Coverage is placed with reinsurers through an intermediary, Willis Re Inc., for the following:

- A. \$500,000 XS \$500,000 ultimate net loss each claim or occurrence, each insured.
- B. \$4,000,000 XS \$1,000,000 ultimate net loss each claim or occurrence, each insured. Recoveries under Coverage A shall be disregarded when determining retention for this coverage.
- C. \$5,000,000 XS \$1,000,000 ultimate net loss each claim or occurrence, each insured on excess of policy limits and extra contractual obligations. Recoveries under Coverage B shall inure to the benefit of this coverage.
- D. Excess of \$1,000,000 not to exceed 90% of \$5,000,000 of loss adjustment expenses arising out of each loss event. Recoveries for declaratory judgment expense under Coverage E shall inure to the benefit of this coverage.
- E. 80% in excess of \$75,000 not to exceed \$1,000,000 on any successful or settled declaratory judgment action regarding a claim.

Participants under this agreement, with their participation percentages, are; Hannover Ruck Se (25%), Munich Reinsurance America, Inc. (10%), Alterra Reinsurance USA, Inc. (15%), Odyssey Reinsurance Company (10%), Transatlantic Reinsurance Company (10%), Lloyd's London (Aspen Insurance UK Ltd and Syndicate #2003; 30%).

Non-Fronted Other Lines

Other lines of non-fronted insurance including Long Term Care Professional Liability, General Liability, and Umbrella Liability are reinsured under multiple facultative contracts individually negotiated.

Effective September 1, 2001, the Company entered into an agreement with CRIC to cede a 50% quota share on Workers' Compensation coverages to the Archdiocese of New York, and

any other entities that are related to the Archdiocese of New York. The Company is the beneficiary under a trust agreement providing pledged assets for liabilities held under this agreement.

Effective from October 10, 2013 to June 1, 2014, the Company entered into an agreement with American Excess Insurance Exchange, Risk Retention Group (AEIX) to cede 80% of \$5,000,000 each occurrence of losses stemming from Long Term Professional Liability. The Company is the beneficiary under a trust agreement providing pledged assets for liabilities held under this agreement.

As noted in the “Reinsurance-Assumed” section above, the Company assumed risks related to healthcare services provided to HMO members, in excess of \$500,000 originally written by Healthspan during the exam period. Effective January 1, 2014, the Company entered into a 75% quota share agreement with CHP Insurance Ltd. (CHPIL) covering the business assumed from Healthspan up to \$2,500,000. This agreement requires the Company to retain 25% of the assumed Healthspan liabilities up to the \$2,500,000 threshold. Effective January 1, 2014, the Company also entered into an agreement with Westport Insurance Company (Westport), whereby the Company cedes all liabilities stemming from the assumed Healthspan business, in excess of \$2,500,000.

Fronted Auto and Workers Compensation Programs

Effective December 31, 2006, the Company fronts business for CRIC, a not-for-profit Vermont domiciled captive insurance company and wholly-owned subsidiary of CMRS. The Company has entered into a reinsurance contract with CRIC pertinent to Commercial Automobile Liability and Physical Damage and Workers’ Compensation and Employers Liability risks associated with members of the CMRS whereby the Company cedes \$500,000 of

each claim to CRIC. The remaining liability under the policies is commercially reinsured under two agreements arranged by Guy Carpenter as follows (for contract in effect for 2014):

Agreement 1:

The first layer provides coverage of \$500,000 XS of \$500,000, each occurrence, each coverage, each policy, for auto and each occurrence for workers' compensation business.

The second layer provides coverage of \$9,000,000 XS of \$1,000,000, each occurrence, for workers' compensation business only.

Agreement 2:

The agreement provides coverage of \$20,000,000 XS of \$10,000,000, each occurrence.

Effective December 1, 2005, the Company entered into an agreement with CRIC to front Professional Liability policies to long term care facilities in the state of Pennsylvania and Professional Liability and General Liability coverages to long term care facilities and other entities related to the facilities located in Kansas and other states as requested by CRIC.

Effective January 1, 2014, the Company entered into an agreement with Hills Insurance Company (Hills) to front Workers' Compensation Excess coverages for hospitals, physicians and surgeons, and related healthcare and other entities of the Franciscan Alliance System.

The Company is the beneficiary under trust agreements providing pledged assets for liabilities held under these fronting arrangements with CRIC and Hills.

Fronted Offshore Programs

The Company has entered into a number of fronting arrangements whereby risks written on physicians and other healthcare providers who maintain business relationships with former shareholders of the Company are 100% ceded to off-shore captives owned by the former shareholders.

The Company has issued a number of policies covering risks including Comprehensive General Liability, Medical Professional Liability, Employment Practices Liability, Workers'

Compensation, and Related Professional Liability policies to certain hospitals, physicians, and other healthcare providers owned by, or affiliated with, the Company's former shareholders.

Two of these agreements, Marillac Insurance Company Ltd. and Catholic Health Partners Insurance Ltd. are retroactive agreements and will be further discussed under the caption, "Retroactive Reinsurance" below. All of these policies are reinsured 100% by the former shareholders' wholly-owned off-shore captives, which are all domiciled in Grand Cayman, Cayman Islands as follows:

<u>Former Shareholder</u>	<u>Off-Shore Captive</u>
Ascension Health	Ascension Health Insurance Ltd.
Bon Secours Health System	Bon Secours Assurance Company Ltd.
Catholic Health Initiatives	First Initiatives Insurance Ltd.
Mercy Health	CHP Insurance Ltd.
CHRISTUS Health	Emerald Assurance Cayman Ltd.
Daughters of Charity Health System	Marillac Insurance Company Ltd.
Hospital Sisters Health System	Renaissance Quality Insurance Ltd.
Trinity Health Corporation	Venzke Insurance Company Ltd.
Wheaton Franciscan Services	Wheaton Franciscan Insurance Co.

The Company is the beneficiary of Letters of Credit to cover the liabilities ceded to Ascension Health Insurance Ltd., Bon Secours Assurance Company Ltd., Catholic Health Partners Insurance Ltd., Emerald Assurance Cayman Ltd., and Renaissance Quality Insurance Ltd.

The Company is the beneficiary under several trust agreements providing pledged assets for liabilities held under these fronting agreements with First Initiatives Insurance Ltd., Marillac Insurance Company Ltd., Venzke Insurance Company Ltd., and Wheaton Franciscan Insurance Company.

Retroactive

On January 1, 2002, seven California healthcare facilities formerly in Catholic Health West separated to form the Daughters of Charity Health System (O'Connor Hospital, RFK Medical Center, Seton Coastside, Seton Medical Center, St. Francis Medical Center, St. Louise Regional Hospital, and St. Vincent Medical Center). Effective January 1, 2002, the Company entered into a workers' compensation insurance policy with Daughters of Charity Health System (DCHS) to cover certain hospitals, healthcare providers, and other entities which are owned by or affiliated with DCHS. Prior to this date, DCHS retained workers compensation' for its hospitals, physicians and surgeons, and related healthcare providers as part of a self-insurance program with a retention of \$250,000. This policy covered the retention on claims from July 1, 1978 through December 31, 2001 and 100% of claims after January 1, 2002.

Effective January 1, 2002, the Company entered into a reinsurance agreement with DCHS, S.P., a protected cell company in the Cayman Islands and affiliate of DCHS, who was substituted with Marillac Insurance Company, Ltd. (Marillac), a Cayman Islands company and wholly-owned subsidiary of DCHS, on December 30, 2003 covering the \$250,000 retention from July 1, 1978 to December 31, 2001. Sedgwick Claim Management Services, Inc. (Sedgwick) is assigned as the claims manager.

Effective August 1, 2009, the Company entered into a medical professional liability insurance policy with Catholic Health Partners (CHP) which provides coverage related to the following entities: Mercy Hospital of Scranton, PA; Mercy Special Care Hospital of Nanticoke; Mercy Hospital Wilkes Barre; Mercy Hospital Johnston; and Mercy Tyler Hospital during the periods which they were owned by CHP. This business was previously written through a CHP self-insured trust.

In connection with the above mentioned policy and effective August 1, 2009, the Company entered into a reinsurance agreement with CHPIL, a Cayman Islands company and wholly-owned subsidiary of CHP, covering 100% of the medical professional liability policy described above. The Company has assigned CHP as the claims manager for the business covered by this policy.

General

All contracts reviewed contained standard insolvency, arbitration, errors and omissions, and termination clauses where applicable. All contracts contained the clauses necessary to assure reinsurance credits could be taken.

BODY OF REPORT

GROWTH

The following comparative data reflects the growth of the Company during the period covered by this examination:

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>
Bonds	\$234,075,358	\$242,263,396	\$265,249,071	\$220,306,246
Admitted assets	368,865,245	402,712,991	408,932,635	311,384,981
Loss reserves	99,417,400	105,910,027	86,224,096	75,718,691
Total liabilities	205,815,244	225,497,012	202,841,098	160,693,835
Capital and surplus	163,050,001	177,215,979	206,091,537	150,691,145
Premiums earned	56,619,220	65,969,017	50,040,209	44,112,199
Net investment income	6,115,398	15,774,700	12,057,298	11,191,396
Losses incurred	28,804,943	30,040,415	5,789,625	14,605,693
Net income	14,513,812	16,093,381	34,167,786	17,478,784

FINANCIAL STATEMENTS

The following financial statements are based on the statutory financial statements filed by the Company with the State of Nebraska Department of Insurance and present the financial condition of the Company for the period ending December 31, 2014. The accompanying

comments on financial statements reflect any examination adjustments to the amounts reported in the annual statements and should be considered an integral part of the financial statements. A reconciliation of the capital and surplus account for the period under review is also included.

FINANCIAL STATEMENT
December 31, 2014

<u>Assets</u>	<u>Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>
Bonds	\$220,306,246		\$220,306,246
Common stock	47,102,639	\$1,233,507	45,869,132
Cash, cash equivalents, and short-term investments	28,194,343		28,194,343
Other invested assets	<u>750,000</u>	<u>750,000</u>	<u> </u>
Subtotal, cash and invested assets	\$296,353,228	\$1,983,507	\$294,369,721
Investment income due and accrued	1,723,689		1,723,689
Uncollected premiums and agents' balances in the course of collection	4,912,070	45,472	4,866,598
Deferred premiums	9,201,377		9,201,377
Amounts recoverable from reinsurers	121,945		121,945
Electronic data processing equipment	87,015	10,297	76,718
Furniture and equipment	6,599	6,599	
Miscellaneous receivable	1,415,001	590,132	824,869
Premium tax deposits	<u>200,064</u>	<u> </u>	<u>200,064</u>
Totals	<u>\$314,020,988</u>	<u>\$2,636,007</u>	<u>\$311,384,981</u>

Liabilities, Surplus, and Other Funds

Losses	\$ 75,718,691
Loss adjustment expenses	32,654,855
Other expenses	6,349,688
Taxes, licenses, and fees	303,362
Current federal and foreign income taxes	6,761,620
Net deferred tax liability	147,957
Unearned premiums	26,248,760
Advance premium	4,160,458
Ceded reinsurance premiums payable	10,433,929
Amounts withheld or retained by company for account of others	2,400
Payable to parent, subsidiaries, and affiliates	135,082
Reserves on retroactive reinsurance ceded	<u>(2,222,967)</u>
Total liabilities	<u>\$160,693,835</u>
Special surplus from retroactive reinsurance	\$ 2,222,967
Common capital stock	5,000,000
Gross paid in and contributed surplus	43,353,304
Unassigned funds (surplus)	<u>100,114,874</u>
Total capital and surplus	<u>\$150,691,145</u>
Totals	<u>\$311,384,980</u>

STATEMENT OF INCOME – 2014

Underwriting Income

Premiums earned	\$44,112,199
Losses incurred	\$14,605,693
Loss adjustment expenses incurred	9,280,811
Other underwriting expenses incurred	<u>8,103,094</u>
Total underwriting deductions	<u>\$31,989,598</u>
Net underwriting gain	<u>\$12,122,601</u>

Investment Income

Net investment income earned	\$ 6,777,146
Net realized capital gain	<u>4,414,250</u>
Net investment gain	<u>\$11,191,396</u>

Other Income

Management fee/education revenues	\$ 11,684
Change in incurred retroactive reinsurance	513,858
NCCI write-off	<u>451,571</u>
Total other income	<u>\$ 977,113</u>
Net income before dividends to policyholders and federal income taxes	\$24,291,110
Dividends to policyholders	240,117
Federal income taxes incurred	<u>6,572,209</u>
Net income	<u>\$17,478,784</u>

CAPITAL AND SURPLUS ACCOUNT

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>
Capital and surplus, beginning	\$163,163,656	\$163,050,001	\$177,215,979	\$206,091,545
Net income	\$ 14,513,812	\$ 16,093,381	\$ 34,167,786	\$ 17,478,784
Change in net unrealized capital gains	(2,238,735)	3,232,588	6,877,252	(2,186,491)
Change in net deferred income tax	(5,187,629)	19,842	(1,271,829)	(928,122)
Change in nonadmitted assets	2,189,253	(80,111)	(479,677)	(1,032,255)
Change in provision for reinsurance	4,624,000	(2,654,000)	(7,717,188)	10,691,188
Capital changes – paid in	(433,022)			(305,944)
Surplus adjustments – paid in	(13,404,153)			305,944
Dividends to stockholders	(2,447,440)	(2,445,722)	(2,700,778)	(80,013,636)
Increase in deferred tax asset value due to application of SSAP 10R	2,270,259			
Insurance guarantee association assessment recoverable	_____	_____	_____	590,132
Net change for the year	\$ (113,655)	\$ 14,165,978	\$ 28,875,566	\$ (55,400,400)
Capital and surplus, ending	\$163,050,001	\$177,215,979	\$206,091,545	\$150,691,145

EXAMINATION CHANGES IN FINANCIAL STATEMENTS

Unassigned funds (surplus) in the amount of \$150,691,145, as reported in the Company's 2014 Annual Statement, has been accepted for examination purposes. Examination findings, in the aggregate, were considered to have no material effect on the Company's financial condition.

COMPLIANCE WITH PREVIOUS RECOMMENDATIONS

No recommendations were made as a result of the previous examination.

COMMENTARY ON CURRENT EXAMINATION FINDINGS

There are no comments or recommendations that have been made as a result of this examination.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

There are no findings warranting comment as a result of this examination.

ACKNOWLEDGEMENT

The courteous cooperation extended by the Officers and employees of the Company during this examination is hereby acknowledged.

In addition to the undersigned, Kevin Stubbs, CFE, Brian Davis and Joel Tapsoba, Financial Examiners; Linda K. Scholl, CFE, CISA, Information Systems Specialist; and Gordon Hay, FCAS, MAAA, CPCU, Actuarial Specialist; all with the Nebraska Department of Insurance, participated in this examination and assisted in the preparation of this report.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'Isaak Russell', written in a cursive style.

Isaak Russell, CFE
Supervisory Examiner
Department of Insurance
State of Nebraska

GENERAL NOTARY - State of Nebraska
BRANDIS J. COURSER
My Comm. Exp. July 23, 2018

STATE OF NEBRASKA

DEPARTMENT OF INSURANCE

Bruce R. Ramage
Director



Pete Ricketts
Governor

March 15, 2016

Preferred Professional Insurance Company
11605 Miracle Hills Drive, Suite 200
Omaha, Nebraska 68154

RE: Preferred Professional Insurance Company

To the Management of Preferred Professional Insurance Company:

The Nebraska Insurance Department's financial examination of Preferred Professional Insurance Company (the Company) has been completed for the years 2011 through 2014. During the course of the examination, we noted the following items that were not commented upon in the Report of Examination but, nevertheless, we felt deserved the attention of management.

IT Penetration Test

When reviewing the frequency of the Company's vulnerability testing, it was noted that the last penetration test was performed on February 23, 2013. The Council on CyberSecurity has released a Top 20 list of high-value, prioritized security controls, which cover the foundational components of an organization's security program, including penetration tests. It is suggested that the Company schedule regular external and internal penetration tests to identify the vulnerabilities and attack vectors that can be used to exploit its systems. Throughout the industry this best practice is conducted internally at least quarterly and by an external reviewer annually.

IT Security Policy

When reviewing the Company's IT Security Policy, it was noted that it was last reviewed on September 1, 2011. It is suggested that the Company review its IT Security Policy at least annually.

Jurat Page Clarification

It was noted that Karen Riley has served as the Chief Financial Officer for the Company since her appointment on June 8, 2011. The Nebraska Department of Insurance Analyst, Matt Sporhase noted that Karen Riley, Assistant Treasurer appears on the Company's Jurat page, but her title of Chief Financial Officer is omitted. It is suggested that, for clarification purposes, that the Company add the "CFO" title to Karen Riley's credentials on the Jurat page in future filings.

STATE OF NEBRASKA

DEPARTMENT OF INSURANCE

Bruce R. Ramge
Director



Pete Ricketts
Governor

Reinsurance Agreement - Offset Clause

Through review of each new reinsurance agreement entered into during the examination period, it was noted that two contracts included questionable Offset Clause language. The Physicians and Surgeons agreement and the Westport Insurance Corporation agreement included broad wording regarding the balances to be offset. The Nebraska Department of Insurance (NEDOI) does not take exception to an offset clause which allows offsetting among amounts due under the same reinsurance agreement. The NEDOI does have concerns if other amounts due under separate agreements are included as the clause is too broad and could have unintended consequences. Given that the terms of each reinsurance agreement should only be related to the business reinsured and that the reinsurance agreement should be a stand-alone agreement in nature, it does not appear appropriate to include an offset clause which allows for reduction of the legal financial obligations based upon amounts owed under a separate agreement. Further, allowing offset among separate agreements could lead to concerns regarding risk transfer. It is suggested that the Company ensure that all future reinsurance agreements do not include terms which allow offsetting among separate agreements. Additionally, if the Physicians and Surgeons, or Westport agreements in-force are amended for any reason, it is suggested that the offset clause be revised to only allow offsetting for that specific agreement.

Reinsurance Agreement - Entire Agreement Clause

When reviewing the Company's Physicians and Surgeons reinsurance contract, it was noted that the contract included an Entire Agreement Clause. From the initial response provided, the entire agreement was not contained within the contract, nor was specific coverage information evident until an additional document was provided. It is suggested that the Company comply with its Entire Agreement Clause and that each executed reinsurance contract contain the agreement, in its entirety. If the agreement requires separate attachments containing pertinent data, they should be included as supplemental exhibits or attachments to the agreement.

Common Stock Valuation

While testing the valuation of certain investments, it was noted that Medcath Corp (Medcath) common stock, CUSIP #58404W109 was shown to be valued incorrectly on PPIC's annual statement. The valuation in question was obtained from the investment custodian, who also noted that the pricing information was based on the last pricing date of September 21, 2012. Medcath has since entered liquidation and is no longer actively traded; therefore no current value was obtained. Since the examiner was unable to determine the value of this stock, it is suggested that the Company reach out to its custodian and determine if there is evidence which supports the Company's fair value reporting or non-admit the stock in future annual statements. Also, it is suggested that the Company monitor its custodian to ensure that its investments are properly valued.

STATE OF NEBRASKA

DEPARTMENT OF INSURANCE

Bruce R. Ramage
Director



Pete Ricketts
Governor

Formalized Controls

Through control testing, the exam team noted that the Company utilizes a mix of formal and informal controls. Subsequent to the examination, the exam team provided a list of informal controls that were noted during the exam that could be bolstered. The exam team also provided, in that list, controls the Company has in place but where the control process was not followed entirely. It is suggested that the Company self-assess and determine areas where formalized signoffs could be added and adhered to for the benefit of the control environment.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Isak Russell".

Isak Russell, CFE
Supervisory Examiner
Department of Insurance
State of Nebraska

State of Nebraska,

County of Lancaster,

Isaak Russell _____, being duly sworn, states as follows:

1. I have authority to represent the Department of Insurance of the State of Nebraska in the examination of Preferred Professional Insurance Company.
2. The Department of Insurance of the State of Nebraska is accredited under the National Association of Insurance Commissioners Financial Regulation Standards and Accreditation.
3. I have reviewed the examination work papers and examination report, and the examination of Preferred Professional Insurance Company was performed in a manner consistent with the standards and procedures required by the Department of Insurance of the State of Nebraska.

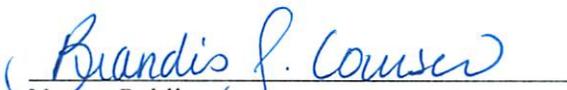
The affiant says nothing further.



Examiner-in-Charge's Signature

Subscribed and sworn before me by Isaak Russell on this 13th day of April, 2016.

(SEAL)



Notary Public

My commission expires July 25, 2018 [date].



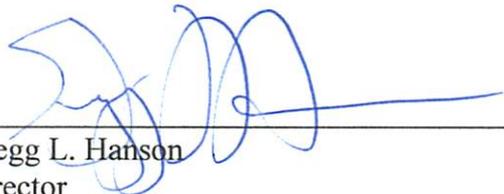


Preferred Professional Insurance Company®

Affidavit

I, Gregg L. Hanson, a member of the PPIC® Board of Directors, hereby swear that I have received a copy of the PPIC Report of Financial Examination as of December 31, 2014, conducted by the State of Nebraska Department of Insurance.

Dated this 17 day of May, 2016.



Gregg L. Hanson
Director

State of MA

County of Suffolk

Gregg L. Hanson, a member of the PPIC Board of Directors, personally appeared before me and swore that he received a copy of the PPIC Report of Financial Examination as of December 31, 2014, conducted by the State of Nebraska Department of Insurance.

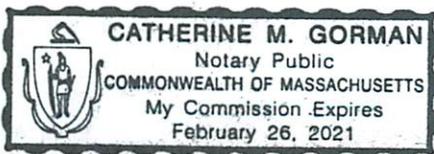
Dated this 17th day of May, 2016.



Notary

Notary Seal

Commission Expires:



10/10/2011

Supplemental Agreement to the Lease

THIS SUPPLEMENTAL AGREEMENT

is made this 10th day of October 2011, between the undersigned parties, who are duly qualified to execute the same, and who are bound by the terms and conditions of the Lease, the text of which is attached hereto for reference.

WITNESSETH that the parties have read and understand the contents of this Supplemental Agreement and have signed the same.

[Signature]

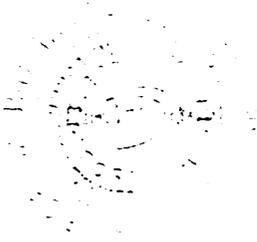
10/10/2011

10/10/2011

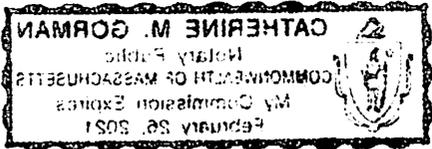
IN WITNESS WHEREOF, the parties have hereunto set their hands and seals at the City of Boston, Massachusetts, on the 10th day of October 2011.

WITNESSETH that the parties have read and understand the contents of this Supplemental Agreement and have signed the same.

[Signature]



10/10/2011





Preferred Professional Insurance Company[®]

Affidavit

I, Richard G. Hayes, a member of the PPIC[®] Board of Directors, hereby swear that I have received a copy of the PPIC Report of Financial Examination as of December 31, 2014, conducted by the State of Nebraska Department of Insurance.

Dated this 16 day of May, 2016.

Richard G. Hayes
Director

State of Massachusetts

County of Suffolk

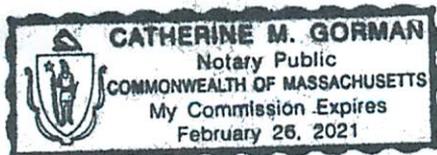
Richard G. Hayes, a member of the PPIC Board of Directors, personally appeared before me and swore that he received a copy of the PPIC Report of Financial Examination as of December 31, 2014, conducted by the State of Nebraska Department of Insurance.

Dated this 16 day of May, 2016.

Notary

Notary Seal

Commission Expires:





February 28, 2021
M. Commission Expires
COMMONWEALTH OF MASSACHUSETTS
Notary Public
CATHERINE M. GORMAN





Preferred Professional Insurance Company®

Affidavit

I, Lynnette M. Matza, a member of the PPIC® Board of Directors, hereby swear that I have received a copy of the PPIC Report of Financial Examination as of December 31, 2014, conducted by the State of Nebraska Department of Insurance.

Dated this 16th day of May, 2016.



Lynnette M. Matza
Director

State of Nebraska

County of Douglas

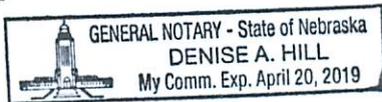
Lynnette M. Matza, a member of the PPIC Board of Directors, personally appeared before me and swore that he received a copy of the PPIC Report of Financial Examination as of December 31, 2014, conducted by the State of Nebraska Department of Insurance.

Dated this 16th day of May, 2016.



Notary

Notary Seal



Commission Expires: 4-20-19



Preferred Professional Insurance Company®

Affidavit

I, Donna Miele-Cesario, a member of the PPIC® Board of Directors, hereby swear that I have received a copy of the PPIC Report of Financial Examination as of December 31, 2014, conducted by the State of Nebraska Department of Insurance.

Dated this 16 day of May, 2016.

Donna Miele-Cesario
Donna Miele-Cesario
Director

State of Massachusetts
County of Suffolk

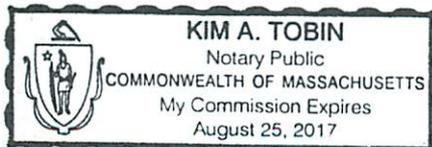
Donna Miele-Cesario, a member of the PPIC Board of Directors, personally appeared before me and swore that he received a copy of the PPIC Report of Financial Examination as of December 31, 2014, conducted by the State of Nebraska Department of Insurance.

Dated this 16th day of May, 2016.

Kim A. Tobin
Notary

Notary Seal

Commission Expires: August 25, 2017





KIM A. TOBIN
Governor
Commonwealth of Massachusetts
January 19, 2017



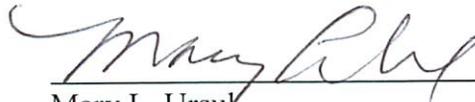


Preferred Professional Insurance Company®

Affidavit

I, Mary L. Ursul, a member of the PPIC® Board of Directors, hereby swear that I have received a copy of the PPIC Report of Financial Examination as of December 31, 2014, conducted by the State of Nebraska Department of Insurance.

Dated this 16th day of May, 2016.



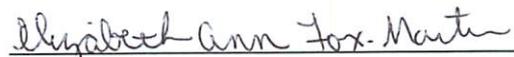
Mary L. Ursul
Director

State of MI

County of INGHAM

Mary L. Ursul, a member of the PPIC Board of Directors, personally appeared before me and swore that he received a copy of the PPIC Report of Financial Examination as of December 31, 2014, conducted by the State of Nebraska Department of Insurance.

Dated this 16th day of May, 2016.



Notary

Notary Seal

ELIZABETH ANN FOX-MARTIN
Notary Public, State of Michigan
County of Ionia
My Commission Expires 11-03-2019
Acting in the County of INGHAM

Commission Expires: 2019