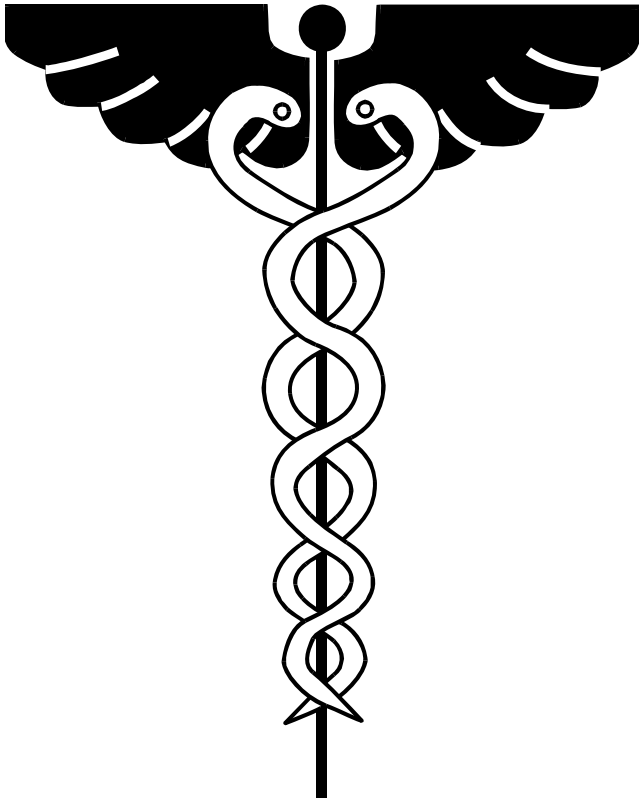
NEBRASKA HOSPITAL-MEDICAL LIABILITY ACT

ANNUAL REPORT



AS OF

DECEMBER 31, 2003

GENERAL INFORMATION ABOUT EXCESS FUND COVERAGE LEVELS

The Act requires health care providers to submit proof of financial responsibility in the form of an underlying professional liability policy with specified coverage limits. When established in 1976, these limits were $100,000/300,000 for physicians or nurse anesthetists and $100,000/1,000,000 for hospitals. The Act also established a cap on the amount a plaintiff could recover from a qualified health care provider of $500,000.

LB 692 passed by the 1984 Legislature raised the cap to $1,000,000 for incidents occurring after January 1, 1985. LB 1005 passed by the 1986 Legislature increased the amount of required underlying insurance to $200,000/600,000 for physicians or nurse anesthetists and $200,000/1,000,000 for hospitals effective January 1, 1987. On incidents occurring on or after that date the Fund provided limits of $800,000 excess of $200,000. LB 1006 passed by the 1992 Legislature then raised the cap to $1,250,000 for incidents occurring after January 1, 1993. LB 146 passed by the 2003 Legislature raised the cap to $1,750,000 for incidents occurring after January 1, 2004.

THE HISTORY OF SURCHARGE LEVELS

The Act became effective in 1976. As originally written, the Act placed a cap of $5 million on the assets of the Excess Fund. As this was approached, the surcharge for 1981 was reduced. A further reduction to the minimum surcharge of 1% was made for 1982 as the amount in the Excess Fund exceeded the cap. LB 692 passed during the 1984 Legislature modified the cap to allow for consideration of future claim costs. Following that and subsequent to an actuarial study conducted in 1984, the surcharge was raised to 50% for all categories effective January 1, 1985. This amount was reduced in succeeding years as experience was favorable and the total assets of the Excess Fund increased. This practice was reversed starting with January 1, 2001 as it became apparent that losses were increasing significantly and past loss reserves were developing upward. The current surcharge is 50%, the maximum allowed by the Act.

Hospital Surcharge	Time Period	Surcharge for Physicians & Others
15%	Original	50%
10%	1-1-81	25%
1%	1-1-82 - 12-31-84	1%
50%	1-1-85 - 12-31-87	50%
50%	1-1-88	45%
45%	1-1-89	45%
40%	1-1-90	40%
35%	1-1-91	35%
40%	1-1-92 - 12-31-93	40%
30%	1-1-94 - 12-31-94	30%
15%	1-1-95 - 12-31-95	30%
10%	1-1-96 - 12-31-96	10%
5%	1-1-97 - 12-31-00	5%
20%	1-1-01 - 12-31-01	20%
35%	1-1-02 - 12-31-02	35%
50%	1-1-03 – Current	50%

Financial Status of the Excess Fund as of December 31, 2003

Balance January 1, 2003	$54,787,592
Excess Fund Surcharges (net refunds)	9,466,767
Residual Premiums (net refunds)	574,785
Interest/Dividends Earned	2,746,737
Investment Gain (Loss) less Investment Expense	717,431
Claims Payments during 2003	(11,036,500)
Claims Expenses during 2003	(81,682)
General Expenses during 2003	(122,869)
Balance December 31, 2003	$57,052,261

Liabilities of the Excess Fund

The aggregate liabilities of the Excess Fund are subject to significant uncertainty. Some of these sources of uncertainty are the same as those faced by insurers of medical professional liability – the long time to settlement and the uncertain outcome of cases. For the Excess Fund, the relatively small number of cases paid each year increases variability for purely statistical reasons. The Excess Fund has also faced uncertainties based on attempts to change the Excess Fund's coverage through litigation. And finally, since the second half of 2002, the Excess Fund has been involved with a multiple-defendant action involving Hepatitis "C" and a Fremont oncology clinic.

In the report provided a year ago, the Department declined to publish an overall estimate of liability on account of these uncertainties. Since then, however, the Excess Fund has prevailed in an important court case challenging the cap in the law (Gourley) and the Department has substantially reduced its estimation of liabilities arising out of the multiple-defendant Hepatitis "C" situation. While the caveats about uncertainty must still be stressed, an estimation of overall liabilities is now feasible as long as these uncertainties are understood. The Department's casualty actuary, Alan Wickman, has estimated unpaid losses and unpaid loss adjustment expenses on a following-form basis, undiscounted for prospective investment income, of $55MM as of 12/31/2003. Unearned premiums and surcharges as of 12/31/2003 are approximately $5MM.

The reader will note that this aggregate liability of approximately $60MM exceeds the $57MM balance in the Fund as of 12/31/2003, although this difference would evaporate and a modest positive balance would be shown if the liabilities were discounted for investment income.

Without diminishing the significance of a possible negative "net worth," the reader should note that that the current liabilities will take a long time to be paid. If it is eventually found that the liabilities have been overestimated, then there will be no deficiency at all or investment income will take care of it. But even if it develops that the Department's current estimates are low, the Excess Fund will have collected surcharges for a number of years in the meantime, and the Excess Fund's financial health will be at least as much a function of its future receipts and liabilities as its current liabilities.

At this writing, there is a proposal in the Unicameral (LB 998), which the Department backs, that would increase the underlying insurance requirement from $200,000 per incident to $500,000. One might ask whether the results just cited – which are significantly more upbeat than a year ago – provide an indication that the proposed legislation is unnecessary. To respond to that possible question – the increased threshold is necessary.

Average incurred losses on a claims-made basis in recent years have exceeded the current annual income for the Excess Fund, and the current rate at which the Excess Fund is incurring liability (on a following-form basis) is substantially in excess of its current income. Something needs to be done – now – to avoid deterioration in the Fund's financial condition in years to come. An increase in the threshold would allow the Excess Fund to increase surcharge income; it will reduce the value of the claims incurred by the Excess Fund, and would make claims management easier for the Excess Fund and more straightforward for insurers writing primary coverage. It is a change that is overdue.

SYNOPSIS OF RECEIPTS AND HEALTH CARE PROVIDERS PARTICIPATING UNDER THE NEBRASKA HOSPITAL-MEDICAL LIABILITY ACT

Excess Fund

	Dec. 31, 1999	Dec. 31, 2000	Dec. 31, 2001	Dec. 31, 2002	Dec. 31, 2003
Physicians	2,640	2,878	2,966	3,107	3,662
Hospitals	61	69	75	85	94
CRNA	149	183	171	193	213
D.O.	39	42	47	48	51
Total	2,889	3,172	3,259	3,433	4,020
Excess Fund Surcharge Collected	$617,577	$889,202	$3,683,419	$5,901,357	$9,466,767

Residual Fund

	Dec. 31, 1999	Dec. 31, 2000	Dec. 31, 2001	Dec. 31, 2002	Dec. 31, 2003
Physicians	1	1	8	22	13
Hospitals	0	0	0	1	0
CRNA	0	0	0	0	2
O.D.	0	0	0	0	0
Total	1	1	8	23	24
Premium Collected	$11,367	$12,233	$169,995	$542,876	$574,785

CLAIMS MADE AGAINST THE EXCESS AND RESIDUAL FUND

(see notes on the following pages)

(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)
Year	Unpaid Claim Counts -- Start of Year	New Claim Counts Reported	Development of Old Claim Counts	Net Claim Counts Incurred	Number of Claims Paid	Claim Counts Unpaid -- End of Year	Unpaid Claim $$$ -- Start of Year	$$$'s for New Claims Reported this Year	Development of Old Claim Reserves	Net $$$'s Incurred	Claims Paid	Claim $$$'s Unpaid End of Year
1976	0.00	0.00	0.00	0.00	0.00	0.00	0	0	0	0	0	0
1977	0.00	0.00	0.00	0.00	0.00	0.00	0	0	0	0	0	0
1978	0.00	0.00	0.00	0.00	0.00	0.00	0	0	0	0	0	0
1979	0.00	0.00	0.00	0.00	0.00	0.00	0	0	0	0	0	0
1980	0.00	2.00	0.00	2.00	0.00	2.00	0	305,000	0	305,000	0	305,000
1981	2.00	2.00	0.00	2.00	0.00	4.00	305,000	265,000	0	265,000	0	570,000
1982	4.00	3.00	0.00	3.00	0.00	7.00	570,000	625,000	0	625,000	0	1,195,000
1983	7.00	8.00	0.00	8.00	0.00	15.00	1,195,000	2,389,500	0	2,389,500	0	3,584,500
1984	15.00	12.00	0.00	12.00	6.00	21.00	3,584,500	1,865,957	0	1,865,957	1,293,231	4,157,226
1985	21.00	9.00	0.00	9.00	4.00	26.00	4,157,226	1,961,985	0	1,961,985	1,030,787	5,088,424
1986	26.00	10.00	0.00	10.00	9.00	27.00	5,088,424	2,181,887	0	2,181,887	1,840,844	5,429,467
1987	27.00	17.00	-1.00	16.00	5.00	38.00	5,429,467	2,373,161	(650,000)	1,723,161	953,117	6,199,511
1988	38.00	21.00	-6.00	15.00	6.00	47.00	6,199,511	3,075,000	181,385	3,256,385	1,460,896	7,995,000
1989	47.00	18.00	-9.00	9.00	8.00	48.00	7,995,000	2,275,000	(307,836)	1,967,164	1,867,164	8,095,000
1990	48.00	9.00	-13.00	-4.00	7.00	37.00	8,095,000	995,000	(684,931)	310,069	1,695,069	6,710,000
1991	37.00	22.00	-2.00	20.00	10.00	47.00	6,710,000	3,410,000	367,308	3,777,308	4,297,308	6,190,000
1992	47.00	39.00	-15.00	24.00	10.00	61.00	6,190,000	7,230,000	(161,903)	7,068,097	1,953,097	11,305,000
1993	61.00	34.00	-19.00	15.00	9.00	67.00	11,305,000	6,400,000	(2,653,999)	3,746,001	2,001,001	13,050,000
1994	67.00	29.00	-16.00	13.00	10.00	70.00	13,050,000	5,265,000	(3,648,459)	1,616,541	3,016,541	11,650,000
1995	70.00	27.00	-20.00	7.00	10.00	67.00	11,650,000	3,840,001	(893,221)	2,946,780	2,861,779	11,735,001
1996	67.00	32.00	-16.00	16.00	15.46	67.54	11,735,001	6,825,000	(2,116,802)	4,708,198	2,693,198	13,750,001
1997	67.54	41.00	-19.00	22.00	10.54	79.00	13,750,001	7,750,000	(450,403)	7,299,597	3,324,598	17,725,000
1998	79.00	28.00	-24.00	4.00	11.00	72.00	17,725,000	4,650,000	(2,589,572)	2,060,428	2,860,428	16,925,000
1999	72.00	52.00	-8.00	44.00	12.82	103.18	16,925,000	9,310,000	(275,178)	9,034,822	4,659,822	21,300,000
2000	103.18	66.00	-15.00	51.00	24.00	130.18	21,300,000	18,291,188	4,167,250	22,458,438	9,318,438	34,440,000
2001	130.18	45.00	-11.00	34.00	23.00	141.18	34,440,000	12,775,000	(1,155,000)	11,620,000	8,060,000	38,000,000
2002	141.18	66.00	-22.00	44.00	28.28	156.90	38,000,000	23,110,000	(3,902,600)	19,207,400	10,837,400	46,370,000
2003	156.90	48.00	-17.00	31.00	27.72	160.18	46,370,000	13,960,000	(4,478,500)	9,481,500	11,036,500	44,815,000

Notes to the Table showing Claims Made

The table shown on the preceding page contains different information than the several tables shown in years past. The numbers that are comparable are the number of claims paid and the dollars of claims paid. Even with the number of claims paid, however, there are a couple of minor corrections to figures from old years.

The prior tables indicated the total loss liability at the end of the year for the Excess Fund. These numbers were not consistently presented in prior reports. In some years, this number was merely the sum of all case-basis reserves; it was done on a developed occurrence basis in some years, and on a developed following-form basis in other years.

The prior tables showed claim counts for all claims made. This included claims that were reported to us even though the total claim value was relatively modest and we saw no reasonable possibility that the claim could develop into something that would cost the Excess Fund money. The table this year shows claim counts only where we had a payment or had established a reserve. This will include a few Residual claims, but 98% or 99% of these claims are purely Excess Fund claims.

This table shows Excess Fund results using undeveloped case-basis (i.e., "claims-made") reserves. Most of the coverage provided by the Excess Fund follows primary coverage written on a claims-made basis. Nevertheless, the existence of "tail" and occurrence coverages means that the liabilities of the Excess Fund are greater than those expressed a claims-made basis. A small percentage of the medical professional liability coverage written by private insurers is on an occurrence basis; coverage written in the Residual Fund is on an occurrence basis, and we provide excess coverage for health care providers with "tail" coverage.

In the second half of 2003, we became aware of a situation involving Hepatitis "C" for multiple defendants arising out of an oncology clinic in Fremont. None of our reserves or activities for that situation are reflected in this table. Their inclusion would skew the results, but the primary reason for nondisclosure is that this is an active situation and disclosure of Excess Fund reserves for a specific case would be inappropriate. With that exception, no other claims or payments have been omitted from this table.

The following comments explain the meaning of each of the columns in the table:

1. Year:

2. Unpaid Claim Counts – Start of Year: This column shows, according to our reserves at the start of the year shown, the number of claims for which we had established a reserve. For example, if we had a claim alleging chipped dental work on account of a clumsy anesthesiologist, we wouldn't show a reserve here, even though we might surmise that the plaintiff will win the case. The reason for that would be that, on an excess claim, the Excess Fund won't contribute anything to a settlement unless the judgment is at least $200,001. In the past, tables that we published had shown all of the claims reported to us, regardless of whether we ever established a reserve for the claim.

3. New Claim Counts Reported: This column shows the number of claims reported during the year on which there was either an excess reserve at the end of the year or on which there had been a payment made during the year.

4. Development of Old Claim Counts: This column shows how the claim counts in column 2 developed during the year. This number is consistently negative, although a positive value would be perfectly valid. In practice, we get claims newly reported to us with a fairly good description by the plaintiff as to the nature of the alleged injury, but we don't have defense reports and we don't know the extent of negligence. As such, our initial reserves are often overestimates. There will be underestimates as well, but the number of overestimates will typically exceed the number of underestimates.

5. Net Claim Counts Incurred: These might be viewed as "incurred claim counts" on a "calendar year basis," which is a term familiar to those that engage in insurance accounting. It is to be distinguished from being on an "occurrence" basis. Nothing on this table is on an "occurrence" basis. This column can be calculated by summing the numbers from columns 3 and 4.

6. Number of Claims Paid: As also shows up in columns 2 and 7, some of these values are fractional because some claims were paid in more than one year.

7. Claim Counts Unpaid – End of Year: When figures for the next year are given, it will be seen that this is the same number as the unpaid claim counts at the start of the next year. It can be calculated by taking the prior year claim counts (column 2), adding the net claim counts incurred (column 5) and subtracting the number of claims paid (column 6).

Columns 8 through 13 are the dollar values that "mirror" the claim counts given in columns 2 through 7. Columns 4, 10 and 13 deserve a little extra explanation, however.

The column 4 and 10 values would make it appear that the Excess Fund had no loss development prior to 1987. One would get the impression that someone was very effective at establishing reserves back then. In fact, the Excess Fund didn't regularly reserve claims on a case basis until the mid-1980's. The figures from prior to that time were entered into the computer database when the database was created in the mid-1980's, but the claims were shown as being opened with case reserves exactly equal to the final settlement value. This makes it appear, prior to 1987, that we reserved claims with perfect foresight. Such was not the case

With regard to column 13, the reader will note that the last value in this column indicates case-basis reserves of $44MM, while our total loss reserves (indicated in the discussion on page 3 of this report) are $55MM. The difference occurs because the case-basis reserves are undeveloped; because the $44MM figure does not include IBNR for the Excess Fund or IBNR for primary Residual policies written in recent years (that are on an occurrence basis); because the case-basis reserves don't include anticipated loss adjustment expense (which is relatively small) and because the $44MM figure does not include any of the liabilities of the Excess Fund arising out of the Hepatitis "C" cases.

Questions?

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