Does your medical liability carrier do enough to protect your reputation and career? TMLT’s philosophy is to defend doctors, not pay non-meritorious claims. Guided by this philosophy, we have resolved more than 38,000 claims, closing more than 87% with no indemnity payment. The right protection can make all the difference. TMLT is your partner in trust.

TEXAS MEDICAL LIABILITY TRUST
P.O. Box 160140
Austin, TX 78716-0140
512-425-5800 • 800-580-8658
www.tmlt.org

Partners in Practice
Patients, paperwork, and the rapid pace of today’s medical practice can eat up the clock. TMLT can save you time. Apply for medical liability coverage online. Pay your premium online. Take our online CME courses. All at a time and place convenient for you. Have a claim to report? We’re available to you by phone 24-7. Take TMLT to work with you. We are your partner in practice, prevention, and protection. TMLT is your partner in trust.

The only health care liability claim trust created and endorsed by Texas Medical Association
Welcome to Trust, the 2005 Annual Report Magazine of Texas Medical Liability Trust. This publication will provide you with information on the financial condition of TMLT, as well as a “year in review” of Trust operations. We have also included two feature articles that we hope will be of interest: an excerpt from Case Closed: A collection of TMLT closed claim studies and “Partners in Trust.” Our third feature article is a winning essay from one of the 2005 TMLT Memorial Scholarship recipients.

TMLT’s financial strength allows us to provide our policyholders with the support and service they deserve and have come to expect over our 26-year history. The information, facts and figures on the pages that follow speak for themselves and illustrate why TMLT is the premier medical liability carrier in Texas.

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CHAIRMAN’S MESSAGE

“Time cools, time clarifies; no mood can be maintained quite unaltered through the course of hours.”

Mark Twain

IN 2006 I WILL SERVE MY FINAL year on the TMLT Board of Governors. Since the medical liability reforms of 2003, I have been honored to serve as TMLT’s Board chairman for the past two years. The understanding and appreciation I have gained for what TMLT and TMA undertake every day on behalf of physicians is something I wish every Texas doctor could experience. I encourage you to become active in the TMLT, the TMA, your county and specialty society. Physician participation and support is vital to the success of these organizations that serve us so well.

I first became a TMLT policyholder in 1985. Securing medical liability coverage through TMLT was one of the best business decisions I ever made for my medical career. I have practiced as an ob-gyn in Dallas for 35 years, the past 21 under the Trust’s medical liability protection. During a time when one in four Texas physicians was being sued, I delivered babies confident that TMLT’s tough claims and defense services would protect me if I ever needed them.

Over the years, I have also been active on various Texas Medical Association committees, including 9 years on the TMA Board of Trustees. It became clear to me that serving physician members was the number one priority for both of these strong organizations. By working closely together, could their physician memberships be better served? When I was elected to the TMLT Governing Board, I made it my personal goal that, before my years of TMLT board service were over, I would see a strengthening of the TMLT-TMA bond and unparalleled service to the physician members of these organizations.

As practicing physicians and members of the TMLT Board of Governors, we bring first-hand experience and a unique perspective to the management of TMLT. The 2005 accomplishments are a continuation of the Trust’s amazing tale of struggle, recovery, and success since the crisis years of the early 2000s. Because of the positive effects of tort reform on TMLT claim experience, the Board of Governors approved a strategic plan to “give back” to policyholders. Tom Cotten’s message will provide the details of this plan, which will take effect in 2006. During the previous medical liability crisis, when faced with increasing claims frequency and severity, we made tough decisions that had very real effects on policyholders. Now we are in a position to give back to our fellow physicians, and we do so gratefully.

In the future, TMLT will continue to explore other ways to support our policyholders and the medical community that serves them. Some of the most prominent medical organizations in Texas count on TMLT for support of their programs. These organizations include the TMA, the Texas Osteopathic Medical Association, TAPA, and a number of county and specialty societies. We have worked together to reach physicians with risk management initiatives, resident educational programs, and to share information. These partnerships have helped us reach our respective objectives, form strong friendships, and gain a clearer understanding of those issues important to physicians of different specialties who practice in different geographic.
what TMLT could become, we keep our core principles in sight. We work for you, and every employee at TMLT is dedicated to safeguarding the professional reputations of those practicing medicine in Texas. On behalf of the TMLT Board of Governors, thank you for your continued support.

Dennis J. Factor, MD
Chairman, Board of Governors

In the future, TMLT will continue to explore other ways to support our policyholders and the medical community that serves them.

Left to right: Robert I. Parks, MD, Secretary-Treasurer; Richard C. Geis, MD; Dennis J. Factor, MD, Chairman; Stuart McDonald, MD; Daniel A. Chester, MD; Jimmy Strong, MD; Tom Cotten, President and CEO; Dave Kittrell, MD, Vice Chairman; Alan Baum, MD; David G. Joseph, MD.

TMLT 2005 BOARD OF GOVERNORS

Dennis J. Factor, MD, Chairman
OB-GYN
Dallas, Texas
Policyholder since 1986

Dave W. Kittrell, MD, Vice-Chairman
OB-GYN
San Antonio, Texas
Policyholder since 1979

Robert I. Parks, MD,
Secretary-Treasurer
Anesthesiologist
Dallas, Texas
Policyholder since 1993

Alan C. Baum, MD
Ophthalmology
Houston, Texas
Policyholder since 1984

Daniel A. Chester, MD
OB-GYN
McAllen, Texas
Policyholder since 1980

Richard C. Geis, MD
Thoracic/Cardiovascular Surgery
Houston, Texas
Policyholder since 1980

David G. Joseph, MD
Family Practice
Austin, Texas
Policyholder since 1997

Stuart D. McDonald, MD
Pulmonary & Critical Care
Ft. Worth, Texas
Policyholder since 1993

Jimmy L. Strong, MD
Pediatrician
Abilene, Texas
Policyholder since 1990

locations. I can report that I have seen a stronger TMLT and TMA in action together, working on shared goals to benefit their members.

TMLT continues to grow in number of policyholders and scope of services. As we have expanded our vision for
THIS HAS BEEN an outstanding year for TMLT. I am gratified and proud for you to read of our 2005 accomplishments — many of them record setting — of our challenges, and of the plans we have for TMLT’s future. In preparing this message, I was reminded that, not very long ago, the financial and industry news was not a story I looked forward to sharing with you. In our 1999 annual report, TMLT had recorded its first bottom line loss in many years, jury awards were increasing along with legal costs, and our competition was creating turmoil in the industry through their willingness to secure new business at a loss. Claims frequency and severity were beginning their ascent.

With hindsight, we know now that 1999 was the start of a 6-year struggle for TMLT. Our industry was unstable, lawsuits and claims were at historic highs, other insurance providers were bailing out of Texas leaving many physicians to fend for a new medical liability carrier. TMLT stayed the course in Texas, made some difficult but necessary decisions to respond to the medical liability crisis, and continued working for physicians and the future of the Trust.

Three years later, I told you in my 2002 annual report message that “It is our hope that proposals made and passed in the 2003 legislative session will provide some financial relief for our policyholders and for the medical liability insurance industry, restoring healthy competition and choice to Texas.” The following year, through the efforts of TMLT, TMA, TAPA and many others, medical liability reform was achieved and Proposition 12 was passed. Two years after this historic tort reform, the Texas Department of Insurance lists more than 30 carriers licensed to write medical liability coverage in Texas. Claims are down; competition has returned; rates continue to drop; and physicians now have significant choice in who will protect their medical careers.

These important achievements required a fierce, coordinated effort among physicians, organized medicine, the medical liability insurance industry, and the legislature. We must remember what we can accomplish when we work together, and we must remain vigilant to retain our hard won victories.

Gold Medal Performance

TMLT broke longstanding company records this year. The positive effects of medical liability reform and a Texas medical liability market that was slow to respond with reduced rates combined to position TMLT for an outstanding year in every area. Based on sound actuarial data, we reduced our rates 5% at the beginning of 2005. At the close of the year, we reduced them another 5%, effective January 1, 2006, for a combined total of 22% since the inception of medical liability reform in 2003. For the first time in TMLT history, we declared a $10 million dollar dividend. This dividend will amount to another 5% reduction in premium in 2006 for each renewing policyholder. As you will read in the financial pages of this report, our surplus is stronger than it has ever been, ensuring our ability to cover large claims. The Trust had a healthy growth rate of 8%, adding 1,820 new policyholders. Retention of existing accounts exceeded 93% for the second year. We took more cases to trial than ever before, and won 92 of
99. The last week of the year, we won our 44th case in a row. We reduced indemnity payout by $25.7 million, the biggest payout reduction in TMLT’s 26 years of operation. Our risk-management education offerings continued to grow and participation continued to increase. We announced that our practice review discount would increase to 5% — with no dollar amount limit to this earned credit — to encourage more policyholders to participate in this patient safety activity. We made changes to our experience credit program and eliminated the service charge for policyholders.

What Lies Ahead

With such a successful year behind us, we now move confidently into 2006, assessing the challenges that lie ahead for TMLT. We will work all year to prepare for the 2007 legislative session and the confrontations that may arise for achieved medical liability reforms. Our business plan includes adding a new policyholder services department charged with the mission of providing unparalleled customer service to all TMLT, TOMA, and TMIC policyholders. To help us achieve this level of service, our new computer system, Infinity, will be implemented in early 2006. Additional customer service enhancements will include changes to our web site. More and more physicians access the web site for information, quotations, to apply for coverage, and to take our online CME courses. We plan to offer a members only section on www.tmlt.org where you can come and view your account, find out the status of your risk management discounts, obtain a certificate of insurance, and more. The litigation preparation DVD produced last year with the collaboration of our claims and risk management departments will receive broader distribution in 2006. With more competitors now in the marketplace, we are undertaking a study on how TMLT is perceived as an organization by our policyholders, by potential policyholders, by our agents, and by organized medicine. This type of study is called a “branding” study and should help us make the right decisions about our products and services as we move forward in a more competitive marketplace. We are energized by these new initiatives and we will welcome your feedback as they are implemented over the course of 2006.

W. Thomas Cotten
President and CEO

2005 TMLT at a Glance

CLAIM OPERATIONS

Number of claims received: 1,598
Number of claims closed: 2,360
Claim frequency (including mass litigation) 12.09%
Percentage of claims paid without indemnity: 87.67%
Number of cases taken to trial: 99
Number of trial victories: 92

RISK MANAGEMENT

Number of physicians receiving practice reviews: 1,767
Problem most frequently encountered during practice reviews: medical records
Number of physicians attending TMA-TMLT CME programs: 1,676
Number of physicians completing TMLT online CME courses: 1,806
Total number of physicians attending TMLT CME programs: 2,510
Number of physicians completing Reporter CME: 4,177

UNDERWRITING

Total policyholder count: 13,220
Number of policies cancelled due to underwriting action: 32
Retention rate: 93.2%
Total number of applications received: 2,336

SALES

Number of new policies: 1,820
Total new written premium: $15,113,364
Total quotes made: 4,791
Number of personal visits by sales staff: 230
Number of medical conferences attended: 22
Total number of direct mail campaigns: 75
While good fortune may smile on you, good prevention practices are not a matter of luck. At TMLT we provide education and onsite practice reviews to our policy holders free of charge, because we believe in giving our doctors tools to prevent a claim before it happens. That’s more than good luck. It’s good health care.  

*TMLT is your partner in trust.*
TMLT Awards $35,000 in Medical Student Scholarships

In 2005, the TMLT Board of Directors awarded the first TMLT Memorial Scholarships to seven Texas medical students.

The TMLT Memorial Scholarships were created to recognize academically gifted Texas medical students who are interested in finding creative ways to enhance patient safety. Applicants were asked to communicate their ideas in a short essay. The $5,000 scholarships were awarded to one student at each Texas medical school that participated in the competition. Scholarship recipients were chosen based on the student’s written essay, academic achievement, and financial need. Winning essays were published on the TMLT web site (www.tmlt.org) and in TMLT’s newsletter, the Reporter.

“We were very lucky to receive so many outstanding applications. The Board had a difficult time selecting the scholarship recipients because all the candidates were impressive,” says Tom Cotten, President and CEO of TMLT. “The essays demonstrated that Texas medical students have given considerable thought to how they will address patient safety when they practice medicine,” says Cotten.

The recipients were:

Bradley Lega, a fourth-year medical student at Baylor College of Medicine;

Rodolfo Jose Oviedo, a third-year medical student at the University of Texas Medical School at San Antonio;

Erin K. Shiner, a third-year medical student at Texas Tech University Health Science Center School of Medicine; and

Rebecca Wald, a third-year medical student at the University of Texas Southwestern Medical School.

TMLT will award the Memorial Scholarships in 2006. Bradley Lega’s scholarship-winning essay is featured on page 16 of this publication.

Residents Train in MedMal 101

TMLT WORKS with many Texas residency programs to help educate resident physicians about medical liability insurance, what to look for in a provider, what risk management can do, where to find the best programs, and how to keep medical records that can be defended in court.

Information on these topics is often not provided in the residents’ planned curriculum. It is important that they are introduced to the concepts, and that they have a resource as they move into their medical careers.

TMLT presents courses on these topics at no cost to the residency programs.
Successful Trial Year for our Physicians

Improving claim service became a major focus for the Claim Operations Department in 2005.

The Claim Operations Department at TMLT is coming out of their best year yet, including a winning streak of 44 cases in a row. Though they had more claims taken to trial last year than any other (99), their win rate was 93%, having lost seven cases and won 92.

Out of the 99 cases that went to trial, the total demands by plaintiffs totaled $30 million. For all of these cases, only $1.37 million was paid out.

2005 was the busiest trial year in TMLT history. Claim staff noted that physicians are becoming more reluctant to settle out of court and instead push to go to trial. “Many doctors worry about future insurability, the possibility of a report to the National Practitioner Databank, and the potential for investigation by the Texas Medical Board,” says Bob Fields, Executive Vice President of Claim Operations. The TMB now has a policy to investigate any physician who has three claims within five years. Due to more stringent enforcement by the TMB, the claim department saw an increase in the number of physicians requesting Medefense reimbursement in 2005.

Also in 2005, indemnity payments dropped significantly. In 2004, TMLT paid $76.6 million in indemnity. In 2005, that number dropped to $50.9 million. The average paid claim in 2004 was $219,485; conversely, in 2005, the average was $174,643.

The department closed 1,695 non-mass litigation claims and 665 mass litigation claims in 2005. The percentage of cases closed without indemnity payment remained high in 2005 at 87.67%.

In addition to managing claims, claim staff worked with underwriting staff to revise and refine the TMLT policies. “The medical liability reforms of 2003 made it necessary to rework the policies,” says Fields. “It is a long and complicated processes, but it is necessary.” TMLT policyholders will be informed of the changes to the policy in a letter sent at renewal.

The department was also busy testing a new computer system, Infinity. Under the new system, new protocols are being developed that will ultimately help the department and company better access and process claims.

Along with the Risk Management and Communications and Advertising Departments, Claims helped develop the CME program You’ve Been Sued and contributed to Case Closed.

Improving claim service became a major focus for the Claim Operations Department in 2005, as goals were set for supervisors to meet with physicians at an earlier point in the claim process, prior to mediation and trial. “We wanted supervisors to personally meet with policyholders sooner, so they will get to know the members of their defense team sooner,” says Fields.

“Medical liability reform is working to keep frivolous cases out of the system . . .”
Case Closed

Case Closed contains 50 closed claim studies based on actual TMLT claims. It was written as a collaboration of staff from the Communications & Advertising, Claims, and Risk Management departments, and is available free of charge.

This valuable publication dissects and expands on 50 real-life closed claims, allowing you to learn from the experience of other physicians and to practice safe medicine. The examined claims identify clear management issues, including documentation errors, failure to diagnose, and miscommunication. They demonstrate how judgment errors led to allegations of medical wrongdoing and where risk management may have prevented grave outcomes or increased the physician’s defensibility.

Additionally, by completing the CME activity included in Case Closed you can earn 4 hours of CME, including 1 ethics hour. TMLT policyholders who complete the CME activity also receive a 3% premium discount (maximum of $1,000) applied to their next eligible policy period.

To order a free copy of Case Closed, please email claimbook@tmlt.org. Please include your name and mailing address.

On May 16, 2005, Texas was removed from the American Medical Association’s list of states in medical liability crisis. The AMA cited the medical liability reforms of 2003 (House Bill 4 and Proposition 12) as the reason for the improved conditions in Texas. Across the state, malpractice claims are down and physician recruitment and retention are up. Rate reductions announced by TMLT and other medical liability carriers have saved Texas physicians millions of dollars.

At TMLT, claims intake and frequency are down. Indemnity payments have decreased considerably. Medical liability reform is working to keep frivolous cases out of the system. The caps on noneconomic damages — the cornerstone of the 2003 reforms — mitigate the unpredictability and subjectivity of awards for pain and suffering. This makes it possible to evaluate cases more accurately and keep insurance rates at a reasonable level.

What has often been lost in the countless stories in the media about medical liability reform in Texas is that legitimate malpractice claims are still going to court. In these cases, economic damages are preserved. Plaintiffs can still collect unlimited damages for past and future medical bills, lost wages, and custodial care. Pain and suffering damages are recoverable up to $250,000 or up to $750,00 if institutions are involved. By capping only noneconomic damages, Proposition 12 allows insurers to maintain a reasonable rate structure without affecting the rights of plaintiffs to collect economic damages for meritorious claims.

The medical liability reforms of 2003 are working as predicted. Texans now have greater access to the health care they need. According to the Texas Alliance for Patient Access, 3,000 physicians have come to Texas since reforms were passed. This includes an increase in physicians in high-risk specialties such as obstetrics-gynecology, orthopedic surgery, and neurosurgery. The Rio Grande Valley has also seen growth in the number of physicians. Overall, medical liability reform has been good for Texas patients and Texas physicians.
Risk Management

The focus of a practice review is decreasing a physician’s chance of being sued and improving patient safety in the practice.

Risk Management is part of the core philosophy at TMLT. It is always advantageous if a company’s claim department and legal team are top-rate, but if prevention techniques can be implemented from the start, everyone benefits.

During 2005, the Risk Management Department completed several projects that led to a heightened awareness of patient safety for TMLT’s policyholders.

With the help of a production company, Risk Management produced a 40-minute video that was incorporated in a 3-hour CME program, You’ve Been Sued: Successfully Navigating the Litigation Process (see page 11). The program was very well received: attendance at the program was up 68% over our 2004 programs.

Additionally, the online CME courses gained popularity, with participation increasing 60% over 2004.

In order to increase the emphasis on the medical liability issues, risk staff completely revised the practice review process in 2005. Based on feedback from Board members and TMLT policyholders, the forms and documents used during a practice review were modified, including specialty-specific questionnaires and medical records review forms.

Risk staff will continue to have resources available regarding practice management and regulatory issues, but the focus of practice review is decreasing a physician’s chance of being sued, as well as improving patient safety in the practice.

During the practice review, a risk management representative identifies areas specific to a physician’s practice that make him or her especially vulnerable to possible claims. “This can positively affect the health care environment resulting in improved communication, reduced systems failures, and hopefully improved patient care,” says Jane Holeman, Vice President of Risk Management.

A practice review may be the only face-to-face contact a policyholder has with a TMLT representative. “Risk management generally has the most frequent contact with policyholders and is in an excellent position to build relationships that establish trust,” says Holeman.

Both the Risk Management and Claim Departments work closely together. “Although it is difficult, if not impossible, to measure the effectiveness of risk management activities on frequency and severity of claims, if only one claim is averted that had the potential for a significant settlement, then risk management works, and has made a positive impact on claims and ultimately, TMLT’s bottom line,” says Holeman.

Holeman advises that though some risk management tenets hold true for all specialties, such as documentation and communication, there is no “one size fits all” advice. In 2006, Risk Management will be focusing on specialty-specific needs and planning additional staff education. Additionally, new CME programs will be geared toward certain specialties, such as radiology, pathology, anesthesia, and hospital-based medicine.
Risk management generally has the most frequent contact with policyholders and is in an excellent position to build relationships that establish trust.

JANE HOLEMAN
Vice President
Risk Management

A significant amount of time and energy of the entire Risk Management Department was focused on coordinating, developing, and presenting the fall seminar series, You’ve Been Sued: Successfully Navigating the Litigation Process. We identified a need for educating physicians who may be involved in a lawsuit, on the importance of taking an active role in their defense, especially preparing for deposition. We also wanted to focus on the emotional impact that a claim or lawsuit has on physicians and their families. This was a collaborative project between the Claim and Risk Management Departments with planning meetings beginning in February 2005. Defense attorneys drafted scripts from actual depositions and played the roles of plaintiff’s attorneys. The deposition scenarios included risk management messages reinforcing the importance of thorough documentation, legible handwriting, informed consent discussions, and avoidance of record alteration. Incorporating basic risk management processes into medical practice will assist physicians in their defense in the event they are involved in litigation.

Throughout the year we spent countless hours working with a production company, resulting in a DVD that depicted various deposition scenarios. This demonstrated physician responses to the oft-times intimidating questions of a plaintiff’s attorney. Their responses had the potential for ultimately being either helpful or detrimental to a successful defense. We used the “local talent” of our Claim Department supervisors to play the roles of the physicians. With their experience attending depositions and trials and being familiar with the attitudes and emotions of physicians going through the litigation process, they did an excellent job!

The DVD, Successfully Navigating Your Deposition, was incorporated into a 3-hour live seminar that was presented last fall in six locations across the state. This resulted in a risk management educational activity that was creative, informative, entertaining, and engaging. The program was a tremendous success with approximately 1,000 physicians attending, a 68% increase over attendance at the 2004 fall seminar series. An obstetrician/gynecologist from Ft. Worth wrote in his program evaluation, “I have been to many of these types of courses, but this one was THE BEST ever… the presentation was outstanding!”

During the practice review, a risk management representative identifies areas specific to a physician’s practice that make him or her especially vulnerable to possible claims.

"Risk management generally has the most frequent contact with policyholders and is in an excellent position to build relationships that establish trust."
Protecting and Serving our Policyholders

For more than 25 years, customer service and the retention of policyholders have been the top priorities of TMLT’s Underwriting Services Department.

In 2005, the Underwriting Services Department witnessed more competition entering the marketplace. With so many new companies offering medical professional liability coverage in Texas, some physicians made their selection of a carrier based solely on price. Recent history has shown that this is not a wise course of action when one’s professional reputation is at stake.

“At TMLT, we strive to keep the cost of superior coverage at a level that will assure protection of the policyholder and maintain lasting financial stability for the Trust,” says John Alexander, Vice President of Underwriting Services. In addition to the rate reductions and dividends announced in 2005, enhancements were made to available discount opportunities. TMLT broadened the eligibility criteria for the experience credit, increasing the number of policyholders receiving these credits from 6,184 to 7,245. This equaled $8 million more in credits awarded by TMLT.

Educating policyholders on how to avoid circumstances that could lead to claims is a valuable benefit of TMLT’s risk management practice review. To further highlight its availability, the practice review discount was increased from 3% to 5%. This discount remains on the policy for two additional renewal periods.

“Proactive pricing enhancements such as these have more long-term sustainability than rate reductions,” says Alexander. “Since the claims environment can change quickly, it is important to be aware that the premiums collected today will be used to pay claims in the future. The integrity of TMLT’s premium rates is strong and this provides the Trust with strength and stability.”

The Underwriting Services Department works closely with the TMLT Board of Governors when underwriting actions — such as non-renewal or a reduction in limits — must be taken. The Underwriting Review Committee is made up of five Board members who provide input on the medical culpability issues of each case. The underwriters then use this information to set policy renewal terms. In 2005, underwriting action was taken on just 3.1% of TMLT policyholders.

In 2005, policyholder retention remained high at 93% for the second consecutive year. Other important service standards that the department tracks apply to how quickly policies are issued. This year, 91% of new business applications were processed within 15 days and 90% of renewal policies were mailed 30 days prior to the renewal date. “This has been accomplished through the dedicated efforts of our professionally licensed staff, consisting of nine underwriters, two underwriting managers, and 22 support staff,” says Alexander.

“In 2006, we will take service to the next level, improving timeliness and responsiveness,” says Alexander. “With the help of our new, custom-designed computer system, we will aim to consistently retain 90% or more of our current policyholders, as we have in 2004 and 2005.”

TMLT is the most respected and preferred provider of medical professional liability coverage in Texas. The Underwriting Services Department, through the use of time-tested standards, makes prudent decisions on the selection and renewal of the Trust’s business. “Although TMLT cannot insure every Texas physician, we endeavor to make a positive impact on
the quality of health care and provide our policyholders with peace of mind,” says Alexander.

“At TMLT, we strive to keep the cost of superior coverage at a level that will assure protection of the policyholder and maintain lasting financial stability for the Trust.”

If you are unfamiliar with the advantages offered by www.tmlt.org, please visit our website soon for in depth information and helpful updates to our online services.

TMLT’s online CME page is undergoing transformation for 2006. Our CME courses are accredited and can earn you premium discounts. Take the course(s) of your choice at a time and place convenient for your schedule. The entire process can be handled online.

Have you signed up for your practice review? Policyholders can request this free service on the web site. Read what the practice review process requires of you and your staff so you can be prepared to participate fully in the process. Successful completion can earn you additional premium discounts.

You can visit www.tmlt.org to request a quote, learn about discounts, or apply for coverage. You can even pay your premium online with your credit card.

Be proactive in preventing claims and lawsuits. Reading the Reporter and other TMLT publications can help you practice safe medicine.

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Be proactive in preventing claims and lawsuits. Reading the Reporter and other TMLT publications can help you practice safe medicine.
Promoting the TMLT Advantage

Meeting the demands of the market and better serving TMLT’s physicians

The Sales and Marketing Department at TMLT had their hands full in 2005. The emergence of new competition and the concern that brings kept them en pointe. Yet the department was secure in the knowledge that TMLT sets the industry standard and provides the best protection for Texas physicians.

With the materialization of new competition, the first response was one of anticipation; the Sales and Marketing team asked what they could do to meet the demands of the market and attract new policyholders. Although TMLT’s market share stands at nearly 50% based on TMA membership, there is still significant opportunity for growth and development.

“The threat posed by many of the new start-ups is muted by under-capitalization, high expense operations, and lack of bundled services, particularly claims and risk management,” says Don Chow, Senior Vice President of Sales and Marketing.

Even so, a few of these firms aggressively appeal to “cost-only” buyers, and will continue to do so. As the younger generation of physicians emerge from medical school and begin their search for liability insurance, the low prices of competitors will require TMLT to aggressively educate young physicians on the benefits of selecting an established insurer and not the cut-rate services of many start-up carriers. “Having a long term perspective on the benefits of a carrier like TMLT is critical to new physicians understanding the true value of our organization,” says Chow.

However, according to Chow, more legitimate threats come from carriers that are well established nationally but display a minor presence in Texas. Due to medical liability reforms passed in 2003, these firms are vying for increased market share and are anxious to establish a stronger hold. As the fourth largest market for medical liability insurance countrywide, representing more than $800 million in available premium, Texas is a very attractive state offering immense opportunity.

In response to the wave of new competition, TMLT will continue to focus on the value of its services. It has become apparent other firms cannot compete with TMLT’s record in both claims and risk management. “After 26 years in business, we know that what keeps policyholders renewing year after year isn’t just the price tag, but the entire package,” says Chow.

Among the many benefits of being a TMLT policyholder is the ability to have direct input in controlling the cost of the medical liability premium. “If physicians will leverage all the opportunities available including experience credits and risk management programs — CME courses and practice reviews — they can significantly reduce their annual costs,” according to Chow.

Although primarily a direct writer of insurance, TMLT has engaged in strategic relationships with carefully selected agents that have access to its franchise. “Given TMLT’s growth objectives, partnering with selected agents allows us to maximize our potential especially with physicians in a group,” says Chow.

Another strategy that has served TMLT well is the strong relationship with organized medicine. From the TMA to the county and specialty societies, TMLT continues to enjoy exclusive endorsements from these entities. Responding to the needs of physicians is a common goal that TMLT shares with organized medicine and the Sales and Marketing team will continue to cultivate these relationships in the years ahead.

“Although the challenges of a softening market are upon us, we will continue to respond quickly and appropriately to retain our leadership position in the state allowing TMLT to continue to grow its policyholder base profitably,” says Chow.
After 26 years in business, we know that what keeps policyholders renewing year after year isn’t just the price tag but the entire package.

Time is a valuable commodity, especially for busy physicians. Recognizing the importance of speed and convenience, TMLT is working toward increased use of the Internet as a tool to keep connected, share information with our policyholders, and to make TMLT account management more accessible to you.

Have you visited www.tmlt.org lately? You will see that in 2005 we improved our existing online individual application, making it easier and faster to use. We developed a special group application to make online application available and easier for a group administrator to manage. We have lots of current information to share with you on risk management tips, closed claim studies, and risk alerts.

In 2006 we are planning to expand our web site services for policyholders by adding a members only section. This new section will be available to all current TMLT policyholders and will be password protected. Like paying a bill online and applying for coverage, the members only section will allow you to manage and request information about your policy at your convenience. For example, you will be able to view and print a proof of coverage, update your contact information, subscribe to and request TMLT publications, view your policy, view the histories connected to your policy, and more.

This site will also provide contacts to specific people in the Claims, Underwriting, Risk Management, and Sales departments, so you can save time and get the information you need regarding your policy quickly and efficiently. If you have any suggestions about services you would like to see available in our members only section, please contact us at feedback@tmlt.org.

THE TMLT COMMUNICATIONS and Advertising Department received three 2005 Bronze Quill awards from the International Association of Business Communicators (IABC). Bronze Quill is a communication award and evaluation program for those in the communications profession. Judging for Austin's Bronze Quill competition was handled by a panel of distinguished, international communications professionals, including IABC Vice Chairman Warren Bickford from Canada. IABC is the association for communications professionals and has more than 13,000 members internationally.

TMLT winning communications entries were:

- 2003 Annual Report – The Journey
- What if? Direct mail post card campaign
- the Reporter newsletter

In addition, the Reporter newsletter was recognized in 2005 with awards from Publications Management and from the Society for Technical Communication.

Award-winning Communications for TMLT Physicians

DON CHOW
Senior Vice President
Sales and Marketing
Doing What’s Best for the Patient and the Physician

In February 2005, TMLT announced the creation of the TMLT Memorial Scholarships. (For more information on the TMLT Memorial Scholarship, please see page 7). For the essay portion of the scholarship competition, students were asked to write 1,000 words answering the question: “What can individual physicians do to ensure patient safety and minimize the risk of medical malpractice suits?” The essays by all seven scholarship winners were published in the Reporter. One of these winning essays is published below.

“These essays demonstrate that Texas medical students have given considerable thought to how they will address patient safety when they practice medicine and their ideas are impressive,” said Tom Cotten, president and CEO of TMLT.

Bradley Lega
Fourth-year medical student at Baylor College of Medicine

HUnter S. Thompson, the author of Fear and Loathing in Las Vegas and Fear and Loathing on the Campaign Trail, recently shot himself. This is a shame for many reasons, but one of them is that he never had the chance to write a book called Fear and Loathing in a White Coat: A Chronicle of Doctors, Lawyers, and Malpractice. Fear and loathing seem like two most appropriate concepts to describe the average physician’s view of malpractice: fear of being sued, loathing for the wolfish lawyers that patrol the flanks of medical practice looking for the weak and the old. The fear begins early in training as professors emphasize points about disease management with phrases like: “And if you don’t do this, start finding a lawyer.” The loathing comes from many sources, including unending TV ads for Jim Adler the Texas Hammer, an over-exposed malpractice attorney who evidently takes advice from professional wrestlers.

After starting clinical rotations, I noticed that loathing associates itself with malpractice in another, more subtle form. Stories of lawsuits become a way for residents to express their dislike for their peers. During my medicine rotation, the team’s intern complained about how lazy one of the surgery residents was, and then added, “He’s already been sued twice.” The story is petty, but it shows that physicians often think that their less competent and careful peers are the ones being sued, that a lawsuit is something like a professional scarlet letter. The advice these physicians give about malpractice reflects their attitude — I can’t count how many times I’ve heard the sentence “If you do what’s best for the patient, you won’t be sued.”

I call this method of malpractice avoidance the Edwards method, after the Puritan preacher whose sermon “Sinners in the Hands of an Angry God” has some legendary metaphors about the consequences of immorality. In the Edwards method, if a physician always does what she’s supposed to, she can live with a clear conscience and without fear of legal reprisal. The method theoretically ensures infallible patient care: if a physician always does what’s best for the patient, then patient safety should be one of her prime concerns.

But what’s best for the patient? The conventional term “standard of care” is a fluctuating and nebulous concept, especially for unusual cases. Plus, bad things happen to good people: innocent women were drowned as witches, pious Franciscans caught the plague, and good doctors suffer lawsuits.

This last point leads to a second often-repeated prescription for avoiding malpractice: documentation. If a physician carefully documents what she does and her reasoning behind difficult decisions, her defense lawyers will have powerful weapons to keep the wolves at bay. I call this the Nixon method, since Nixon’s tapes illustrate how documentation can cause problems for people...
who aren’t doing what’s right. The Nixon method’s emphasis on documentation implies that a physician must maintain constant vigilance, thinking of each page in the patient’s chart as a piece of evidence of her own defense. It also contributes to the adversarial nature that pervades too many doctor-patient relationships, a trend that can’t be good for patient safety no matter how artful the argument. Finally, in my limited experience, mistakes often occur when doctors forget to do things that they normally would do — forgetting to recheck a patient’s potassium level after ordering an ACE inhibitor, for instance. But the Nixon method does nothing for these types of errors, since a physician can’t document something she forgets to do.

It appears then that serious flaws weaken both the Edwards method and the Nixon method, even though they are the basis for 70% of the advice that medical students hear about malpractice. I think an approach that I call the Aristotle method solves some of these problems and could serve as a model for how physicians avoid malpractice and promote patient safety. The Aristotle method is built around virtue, as is Aristotelian ethics. It stems from the observation that physicians-in-training learn their habits by emulating some of their superiors, especially residents, attendings, and other students that have won the respect of their peers. Co-workers attribute virtues such as “hard-working,” “sharp,” “strong,” and “efficient,” to these role-models, but the Aristotle method doesn’t mean that physicians can avoid malpractice by being stronger and sharper. It means that when taking care of patients, students should imagine themselves verbalizing their analysis and decision-making to one of their professional heroes. This mental exercise finds potholes in reasoning, and the act of forcing oneself to construct a coherent narrative helps identify things that the physician may have initially forgotten to do.

The Aristotle method is not the same thing as asking inane self-questions like “What would Osler do in my position?” It advocates mental recapitulation, not simple mimicry. We may find that we disagree with our role models’ imagined opinion, but we should then be able to offer good reasons for doing so. And if we honestly don’t know what he or she would think, then it might be time to consult the literature. This idea may initially seem similar to the Edwards model, in which physicians practice in constant fear of judgment for deviating from some standard, but I think it’s more positive since most of us want to win recognition of the people we look up to and we’re willing to work hard for it. And by thinking about what a specific person’s thoughts or criticisms might be, it avoids the vagueness inherent in “standard of care.” It may also look similar to the Nixon model, since documenting one’s reasoning generates the same kind of narrative as imaginary verbalization. But I think it’s less cynical since it creates habits from virtue rather than lawsuit avoidance, and it actively helps prevent errors of omission.

As with any good practice, the Aristotle method could be instituted if the professionals we respect tell us that it’s a good idea. I think it’s a way that avoiding lawsuits and promoting patient safety can converge.
Case Closed: Bariatric Surgery Complications not Recognized

The following is an excerpt from Case Closed: A collection of TMLT closed claim studies, volume 2

CASE 2 Presentation

A primary care physician referred his patient, a 36-year old woman, to a general surgeon for consultation about vertical banded gastroplasty. The patient was 5’9” in height and weighed 290 pounds. The surgeon discussed the procedure — its risks and benefits — with the patient, and provided her with a three-page handout.

Physician action

Six months later, the surgeon performed the vertical banded gastroplasty on the patient. The procedure was carried out without complication, and the patient did well postoperatively. Four days after the surgery, a barium swallow study was performed, and it showed no evidence of extravasation of contrast. The patient was discharged.

The surgeon next saw the patient eight days later for removal of her skin clips. The patient’s weight was 268 pounds and she did not report any problems. She was told to return in one month.

Seven days after this office visit, the patient came to the emergency department (ED) with fever and left-sided pleuritic chest pain. An x-ray showed a left lower lobe infiltrate and the patient was diagnosed with community-acquired pneumonia. She was given Erythromycin and discharged.

Three days later, she again came to the ED with complaints of left-sided chest pain, fever, chills, nausea, vomiting, weakness, and headache. The patient was admitted, and her care was turned over to a hospitalist who consulted the surgeon to rule out any complications from the gastroplasty. On her second day in the hospital, the surgeon ordered a CT scan, which revealed a left upper quadrant abdominal abscess. The surgeon performed an exploratory laparotomy and drained the abscess. No areas of perforation were noted.

One day after the laparotomy, the patient continued to have fever and infection. The surgeon started the patient on prophylactic Heparin for the prevention of deep venous thrombosis. Throughout the patient’s hospital stay, the surgeon ordered early and frequent ambulation and TED hose as a prophylactic measure. The surgeon ordered a barium swallow study, which showed a small leak from the stomach. An NG tube was placed, and the surgeon opted to use suction and TPN to avoid further surgery.

On her 7th day in the hospital, the patient developed shortness of breath and hypoxia for the first time. The hospitalist consulted a pulmonologist, and ordered a ventilation/perfusion lung scan. The radiologist read the scan and orally reported to the hospitalist that it was negative for pulmonary embolism. However, the radiologist’s written report indicated “low to indeterminate for possible pulmonary embolism.” This report was not read by the hospitalist until ten days later. In retrospect, the hospitalist indicated that if he had known about this finding, he would have started the patient on Heparin or placed a Greenfield filter.

The patient’s condition worsened, and she was returned to the OR. The
later when she began to complain of chest pain. The hospitalist and pulmonologist ordered another lung scan and again, the radiologist read the scan as having a low probability for pulmonary embolism. The next day, the hospitalist received a call from the radiologist who was now changing the report to indicate an “intermediate to high probability of pulmonary embolism.” The hospitalist and pulmonologist ordered a change from prophylactic anticoagulation to full Heparin anticoagulation.

The next day, the surgeon placed a Greenfield filter in the patient’s inferior vena cava, and performed a total gastrectomy, cholecystectomy and appendectomy. The patient remained in critical condition for the next two days. She began to have seizures, suffered an acute brain stem stroke, and became neurologically unresponsive. The patient’s family signed a DNR order and the patient died.

An autopsy was performed and the pathologist determined the cause of death to be submassive pulmonary emboli with prolonged heart failure and shock leading to acute respiratory distress syndrome. The findings also revealed the presence of chronic gastritis suggesting the possibility of pre-existing heliobacter-induced gastritis and peptic perforation following the gastroplasty.

**Allegations**

A lawsuit was filed against the surgeon and the allegations included:

- failure to provide prophylactic anticoagulation at the time of the original surgery;
- failure to perform a barium swallow study before the gastroplasty; and
- employing an improper technique to repair the leak in the stomach.

**Legal implications**

The plaintiff’s case did not focus on the initial surgery, but the postoperative care. The plaintiff’s expert was critical of the surgeon for not performing a barium swallow before the second surgery. This would have revealed the leak and would have allowed it to be repaired earlier. Though the cause of death was pulmonary emboli, it was the opinion of the plaintiff’s expert that the patient’s infection led to the pulmonary emboli. He could not offer any explanation as to how this occurred. The expert stated that it was not reasonable to rely on a pulmonologist who was saying the patient had a low probability of pulmonary emboli.

Defense consultants were supportive of the surgeon’s care in this case. Though a leak did occur, the barium swallow performed four days after the gastroplasty negated the possibility that a tear occurred during the surgery. The experts believe the leak occurred because of the patient’s pre-existing gastritis.

The cause of death was pulmonary embolism, not infection. Regarding the plaintiff’s claim that the infection led to the pulmonary emboli, defense experts indicated this was a “ridiculous statement,” and that there is a “mountain of literature” to dispute this. The consultant surgeons also stated that it was reasonable for the surgeon to rely on the hospitalist and pulmonologist who were following the patient’s pulmonary status.

**Disposition**

This case was taken to trial and the jury returned a verdict in favor of the defense.

**Risk management considerations**

The TMLT claim department has identified patient selection, informed consent and postoperative follow up as prevalent issues in lawsuits alleging malpractice before, during, or after surgical weight reduction procedures.

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**This case was taken to trial and the jury returned a verdict in favor of the defense.**

surgeon repositioned the chest tube and repaired the leak in the stomach. The patient did well postoperatively and continued to improve until two days...
HISTORY IS FILLED WITH STORIES OF “rugged individuals” coming together to fight for a common cause. This type of solidarity led to the creation of our country and later to the great state of Texas. But while early Texas citizens were working together to create a government, early Texas physicians stood together to create what would become one of the premier health systems in the United States. These pioneers created the foundation for the Texas health care system, which today includes eight medical schools, 450 residency programs, and 118 county medical societies.

TMLT is not an insurance company, but a self-insured trust established by Texas Insurance Code Article 21.49-4 to provide coverage against health care liability claims to members of the Texas Medical Association.
In the 1970s, Texas physicians again stood together — this time to find a solution to the medical liability crisis that was making malpractice insurance unaffordable and unavailable. One group of pioneering physicians worked through the Texas Medical Association and eventually to the state capitol to create their own insurance provider — Texas Medical Liability Trust.

TMLT is not an insurance company, but a self-insured trust established by Texas Insurance Code Article 21.49-4 to provide coverage against health care liability claims to members of the Texas Medical Association. The liability crisis of the 1970s and the desire of physicians to control their own destiny led to the formation of this unique organization, designed by physicians to benefit physicians.

**Committed to the medical community**

Physicians wanted a company that was committed to the entire medical community in Texas, not a company that would “red line” certain regions or physicians. TMLT is currently the only carrier that has consistently covered physicians of all specialties who practice in all areas of Texas.

**Run by physicians**

The founders of TMLT believed that physicians could be their own best advocates. TMLT is physician-owned and led by a Board of Governors elected by policyholders. Board members are practicing physicians who bring first-hand experience and a unique perspective to the management of TMLT.

**Not just settle claims**

Since our inception, TMLT’s philosophy has been to defend doctors, not pay claims. Our founders wanted a company that would allow physicians to set the tone for their defense. Only by aggressively defending non-meritorious claims can we protect a physician’s reputation and keep the number of malpractice suits filed against all physicians in check.

**Our Trust is a unique organization, designed by physicians to benefit physicians.**

**Based on Texas experience**

TMLT offers one line of coverage and offers it in one state — Texas. Our entire business focus is on Texas physicians and how to protect their practices. Our rates are set based on the claim experience of Texas physicians, unlike some national carriers who set their rates based on national claim data. Additionally, our Texas-based claim staff and defense attorneys understand the Texas legal system, the venues, and the judges.

**Stability**

TMLT was founded by physicians who wanted to create a stable source of medical liability insurance for the state’s medical community. Those physicians also wanted a company that would stick by physicians when market conditions in Texas worsened. 26 years later, TMLT has weathered two medical liability crises, and has grown to become the largest provider in Texas, currently insuring more than 13,000 physicians.

**Consent to settle**

Again, wanting to control their own destiny, Texas physicians wanted an insurance policy that required a policyholder’s consent before settling a case. The TMLT professional liability policy says “the Trust shall not settle any claim or lawsuit without first obtaining the consent of the Named Insured.” Not all medical liability companies include such a provision in their policies. Some are silent on the issue, while others stipulate that the carrier retains the power to settle a claim.

**No profit motive**

Formed as a not-for-profit trust, TMLT has no profit motive. We are not a stock company with an obligation to shareholders. TMLT’s founders knew that it would be impossible to maximize shareholder returns and defend physicians regardless of cost. For this reason, we set responsible premiums that allow for financial stability and that uphold our end of the insurance contract.

**Flexibility**

As a trust and not an insurance company, TMLT is not subject to regulation by the Texas Department of Insurance. TMLT’s founders recognized the importance of allowing physicians to regulate their own company. This structure allows us the flexibility to survive in a volatile insurance market like Texas. When market conditions change, TMLT can respond quickly and efficiently.

But while TMLT is not subject to TDI regulation, we do voluntarily comply with reporting requests. We provide the TDI with our audited financial statements, our rates, our policy forms, and closed claim reports. We also assist the TDI with their data studies.

**Responsible investment philosophy**

Our founders wanted TMLT to adopt a conservative policy for the investment of its assets with the objective of achieving maximum yield with maximum safety. Today, we still keep to this philosophy. Trust assets are invested in investment quality securities to generate income to meet operating expenses and actuarial assumptions.
TMLT’s financial condition continues to improve as evidenced in the accompanying audited financial statements for 2005 and 2004. Total assets and surplus are at record high levels. Surplus has grown from $148 Million at the end of 2004 to $203 Million at the end of 2005. We continue the goal that we started after 2001 which was to enhance our financial strength responsibly, keeping the policyholder’s interest first and foremost.

The accompanying consolidated financial statements have been prepared under management’s direction in conformity with accounting principles generally accepted in the United States and where appropriate, reflect estimates based on management’s best judgment. The financial information included in this annual report is consistent in all material respects with that contained in the audited financial statements. Management is responsible for the integrity and objectivity of the Company’s financial statements.

Calhoun & Co., TMLT’s independent public accountants have audited management’s financial statements and their report appears on page 24. Their report expresses an informed opinion that the consolidated financial statements presents fairly, in all material respects, the consolidated financial position of TMLT. As required by auditing standards generally accepted in the United States, the independent public accountants obtained a sufficient understanding of the internal controls in place in order to plan their audit and determine the nature, timing and extent of other tests to be performed.

Management also recognizes its responsibility for fostering a strong ethical climate so that TMLT’s affairs are conducted according to the highest standards of personal and corporate conduct.

Total assets at the end of 2005 were $589 Million compared to $550 Million in 2004 or an increase of $39 Million. The largest increase was an increase of $43 Million in total investments (bonds and equities) due to the continued positive cash flow from operations and additional surplus contributions. Liabilities decreased $17 Million primarily due to a decrease of $31 Million in the reserve for unpaid losses and expenses due to the continued favorable claims experience. Offsetting this decrease is an increase in liabilities of $9 Million for the policy dividend declared in 2005 that is payable in 2006. Surplus increased $55 Million to $203 Million due primarily to current year net earnings of $52 Million.

Professional liability written premiums vary from period to period for a number of reasons. Some of the more common differences result from changes to premium rates, the volume of new business written during the period, the loss of business to competitors or due to our own underwriting decisions. Total written premium in 2005 was $191 Million compared to $189 Million in 2004 while net earned premium income in 2005 was $165 Million compared to $168 Million in 2004. This small change can be attributed to a 5% rate reduction that was implemented in 2005 offset by new written business.

Net investment income and capital

<table>
<thead>
<tr>
<th>Year</th>
<th>Investment Income (Dollars in Millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>01</td>
<td>$12.8</td>
</tr>
<tr>
<td>02</td>
<td>$13.4</td>
</tr>
<tr>
<td>03</td>
<td>$14.3</td>
</tr>
<tr>
<td>04</td>
<td>$15.4</td>
</tr>
<tr>
<td>05</td>
<td>$16.4</td>
</tr>
</tbody>
</table>

Today, we believe we have a competitive advantage in the market due to our size, geographic scope, and name recognition.
gains increased $2.6 Million to $17.3 Million in 2005. The increase in our net investment income in 2005 as compared to 2004 is due to higher average invested funds in 2005 and a slight increase in current interest rates which slightly increased the yield of our fixed maturity securities. We also increased the proportion of the portfolio that is invested in tax-exempt securities because of the higher after-tax yields available on these securities. Our overall investment strategy is to focus on maximizing current income from our investment portfolio while maintaining safety, liquidity, duration and portfolio diversification. Professional third party asset managers whose results are evaluated periodically by management generally manage the portfolio. The asset managers typically have the authority to make investment decisions, subject to investment policies; within the asset class they are responsible for managing. The passage of tort reform was a major victory for TMLT in 2003. We are seeing the impact of this in our financial statements. Our loss ratio was 45.8% in 2005 compared to 72.3% in 2004. Our combined ratio in 2005 was 64.2% compared to 83.2% in 2004. Without the dividend declared in 2005, the combined ratio would have been 58.6%. All of these ratios are lower than the composite ratio of mal specialty writers. TMLT ended the year 2005 with pre tax net income of $76.8 Million compared to $44.3 Million for 2004.

We are currently operating in challenging market conditions. New carriers are coming into Texas and existing carriers are lowering rates. From mid-2004 through 2005 small competitors with limited capital have entered Texas. These smaller companies tend to focus on limited pools of risk or geographic areas, but generally try to gain market share through lower premiums or less stringent underwriting. We have lost some of our business to the competitors, but our market position has largely allowed us to attract new customers to offset their departure. Our strategy is not to compete on price, but to demonstrate the value in the coverage we provide. We believe that we have a competitive advantage in the current market due to our size, geographic scope and name recognition, as well as our heritage as a policyholder-founded company with a long-term commitment to the professional liability insurance industry. We have achieved these advantages through our balance sheet strength, claims defense expertise and ability to deliver a high level of service to our insureds and agents. At TMLT – the carrier that stayed in Texas and has already lowered rates and initiated a dividend program that we hope to continue as long as financial results will support it — we have continued to strengthen our balance sheet to provide the financial stability our policyholders deserve. Our premiums are set to provide insurance coverage at a fair price — not to maximize profits. TMLT is doctor owned and TMLT’s responsibility is to provide its policyholders with a financially sound carrier and insurance coverage at a fair price.

Ray Demel
Senior Vice President and CFO

\[\text{Written Premium (Dollars in Millions)}\]

\[
\begin{array}{cccccc}
01 & 02 & 03 & 04 & 05 \\
$130.4 & $175.5 & $191.7 & $188.6 & $190.7 \\
\end{array}
\]

\[\text{Total Assets (Dollars in Millions)}\]

\[
\begin{array}{cccccc}
01 & 02 & 03 & 04 & 05 \\
$333.9 & $428.1 & $507.6 & $550.5 & $588.7 \\
\end{array}
\]
Independent
Auditor’s Report

Board of Directors
Texas Medical Liability Trust and Subsidiary
Austin, Texas

We have audited the accompanying consolidated balance sheets of Texas Medical Liability Trust and Subsidiary as of December 31, 2005 and 2004, and the related consolidated statements of operations, changes in policyholders’ surplus and cash flows for the years then ended. These financial statements are the responsibility of the Trust’s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall combined financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Texas Medical Liability Trust and Subsidiary at December 31, 2005 and 2004, and the consolidated results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

March 31, 2006
**December 31, 2005**

<table>
<thead>
<tr>
<th>Description</th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Assets</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Securities, available-for-sale, at fair value:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fixed-maturity securities</td>
<td>$316,764</td>
<td>$293,000</td>
</tr>
<tr>
<td>Common stocks</td>
<td>40,457</td>
<td>21,155</td>
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<tr>
<td>Preferred stocks</td>
<td>1,197</td>
<td>1,663</td>
</tr>
<tr>
<td>Securities, held to maturity – fixed maturity annuities</td>
<td>24,500</td>
<td>24,500</td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>45,415</td>
<td>39,347</td>
</tr>
<tr>
<td>Premiums receivable</td>
<td>60,629</td>
<td>60,782</td>
</tr>
<tr>
<td>Accrued interest receivable</td>
<td>3,632</td>
<td>3,061</td>
</tr>
<tr>
<td>Surplus contributions receivable</td>
<td>1,025</td>
<td>3,000</td>
</tr>
<tr>
<td>Reinsurance recoverables:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>On paid losses</td>
<td>3,655</td>
<td>10,975</td>
</tr>
<tr>
<td>On unpaid losses and loss adjustment expenses</td>
<td>50,633</td>
<td>53,411</td>
</tr>
<tr>
<td>Prepaid reinsurance premiums</td>
<td>9,794</td>
<td>10,298</td>
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<tr>
<td>Federal income tax recoverable</td>
<td>-</td>
<td>4,300</td>
</tr>
<tr>
<td>Deferred tax asset</td>
<td>16,300</td>
<td>15,600</td>
</tr>
<tr>
<td>Deposits</td>
<td>4,145</td>
<td>3,906</td>
</tr>
<tr>
<td>Other</td>
<td>10,560</td>
<td>5,507</td>
</tr>
<tr>
<td><strong>Total assets</strong></td>
<td>$588,706</td>
<td>$550,505</td>
</tr>
</tbody>
</table>
## Balance Sheets

### Liabilities and Policyholders’ Surplus

#### Liabilities

<table>
<thead>
<tr>
<th>Reserves:</th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unpaid losses and loss adjustment expenses</td>
<td>$240,833</td>
<td>$271,559</td>
</tr>
<tr>
<td>Unearned premiums</td>
<td>90,568</td>
<td>90,308</td>
</tr>
<tr>
<td><strong>Total liabilities</strong></td>
<td>385,292</td>
<td>402,830</td>
</tr>
<tr>
<td>Revolving line-of-credit</td>
<td>13,518</td>
<td>13,518</td>
</tr>
<tr>
<td>Premiums received in advance</td>
<td>3,967</td>
<td>5,101</td>
</tr>
<tr>
<td>Income Tax Payable</td>
<td>1,100</td>
<td>-</td>
</tr>
<tr>
<td>Dividends Payable</td>
<td>9,000</td>
<td>-</td>
</tr>
<tr>
<td>Accounts payable and accrued expenses</td>
<td>876</td>
<td>182</td>
</tr>
<tr>
<td>Reinsurance premiums payable</td>
<td>25,430</td>
<td>22,162</td>
</tr>
</tbody>
</table>

Total liabilities: 385,292

#### Commitments and contingencies

(Notes 3, 4, 6, 8, 9 and 10)

<table>
<thead>
<tr>
<th>Policyholders’ surplus:</th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Contributed surplus</td>
<td>91,629</td>
<td>83,820</td>
</tr>
<tr>
<td>Surplus contributions receivable</td>
<td>(4,761)</td>
<td>(4,833)</td>
</tr>
<tr>
<td><strong>Accumulated other comprehensive (loss) income</strong></td>
<td>(3,207)</td>
<td>1,184</td>
</tr>
<tr>
<td><strong>Unassigned surplus</strong></td>
<td>119,753</td>
<td>67,504</td>
</tr>
<tr>
<td><strong>Total policyholders’ surplus</strong></td>
<td>203,414</td>
<td>147,675</td>
</tr>
</tbody>
</table>

Total liabilities and policyholders’ surplus: $588,706

See accompanying summary of accounting policies and notes to consolidated financial statements.
### Statements of Operations

**Years Ended December 31, 2005**

<table>
<thead>
<tr>
<th>Description</th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Premiums earned, net of reinsurance</td>
<td>$164,656</td>
<td>$167,739</td>
</tr>
<tr>
<td>Investment income, net of investment expenses</td>
<td>16,447</td>
<td>15,446</td>
</tr>
<tr>
<td>Net realized gain (losses) on securities available for sale</td>
<td>891</td>
<td>(746)</td>
</tr>
<tr>
<td>Other revenue</td>
<td>3,245</td>
<td>2,798</td>
</tr>
<tr>
<td><strong>Total revenues</strong></td>
<td><strong>185,239</strong></td>
<td><strong>185,237</strong></td>
</tr>
</tbody>
</table>

**Losses and expenses:**

<table>
<thead>
<tr>
<th>Description</th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Losses and loss adjustment expenses</td>
<td>73,223</td>
<td>119,005</td>
</tr>
<tr>
<td>Policyholder dividends</td>
<td>9,000</td>
<td>-</td>
</tr>
<tr>
<td>Other underwriting expenses</td>
<td>26,129</td>
<td>21,897</td>
</tr>
<tr>
<td><strong>Total operating expenses</strong></td>
<td><strong>108,352</strong></td>
<td><strong>140,902</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Description</th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net income before income tax expense</td>
<td>76,887</td>
<td>44,335</td>
</tr>
<tr>
<td>Income tax expense</td>
<td>24,638</td>
<td>3,085</td>
</tr>
<tr>
<td><strong>Net income</strong></td>
<td><strong>$52,249</strong></td>
<td><strong>$41,250</strong></td>
</tr>
</tbody>
</table>

*See accompanying summary of accounting policies and notes to consolidated financial statements.*
## Statements of Changes in Policyholders’ Surplus

<table>
<thead>
<tr>
<th></th>
<th>Accumulated Other Policyholders’ Surplus</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Contributed</td>
</tr>
<tr>
<td><strong>Balance, January 1, 2004</strong></td>
<td>$67,321</td>
</tr>
<tr>
<td>Other comprehensive income</td>
<td>-</td>
</tr>
<tr>
<td>Net income</td>
<td>-</td>
</tr>
<tr>
<td>Contributed surplus, net</td>
<td>11,666</td>
</tr>
<tr>
<td><strong>Balance, December 31, 2004</strong></td>
<td>$78,987</td>
</tr>
<tr>
<td>Other comprehensive loss</td>
<td>-</td>
</tr>
<tr>
<td>Net income</td>
<td>-</td>
</tr>
<tr>
<td>Contributed surplus, net</td>
<td>7,881</td>
</tr>
<tr>
<td><strong>Balance, December 31, 2005</strong></td>
<td>$86,868</td>
</tr>
</tbody>
</table>

See accompanying summary of accounting policies and notes to consolidated financial statements.
<table>
<thead>
<tr>
<th>statements of cash flows</th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Operating activities:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net income</td>
<td>$52,249</td>
<td>$41,250</td>
</tr>
<tr>
<td>Adjustments to reconcile net income to net cash provided by operating activities:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Depreciation</td>
<td>657</td>
<td>510</td>
</tr>
<tr>
<td>Loss on disposal of fixed assets</td>
<td>11</td>
<td>7</td>
</tr>
<tr>
<td>Deferred income taxes</td>
<td>1,562</td>
<td>(5,629)</td>
</tr>
<tr>
<td>Net realized (gains) losses</td>
<td>(1,185)</td>
<td>746</td>
</tr>
<tr>
<td>Amortization of premium / accretion of discount in bonds</td>
<td>1,713</td>
<td>1,209</td>
</tr>
<tr>
<td>Changes in operating assets and liabilities:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Premiums receivable</td>
<td>(981)</td>
<td>2,581</td>
</tr>
<tr>
<td>Reinsurance recoverables</td>
<td>10,098</td>
<td>(10,719)</td>
</tr>
<tr>
<td>Federal income tax recoverable</td>
<td>4,300</td>
<td>(3,900)</td>
</tr>
<tr>
<td>Reserves</td>
<td>(30,466)</td>
<td>(1,009)</td>
</tr>
<tr>
<td>Reinsurance premium balances</td>
<td>3,772</td>
<td>(9,249)</td>
</tr>
<tr>
<td>Federal income tax payable</td>
<td>1,100</td>
<td>-</td>
</tr>
<tr>
<td>Deposits</td>
<td>(239)</td>
<td>3,229</td>
</tr>
<tr>
<td>Policyholder dividends payable</td>
<td>9,000</td>
<td>-</td>
</tr>
<tr>
<td>Other</td>
<td>211</td>
<td>(1,043)</td>
</tr>
<tr>
<td><strong>Net cash provided by operating activities</strong></td>
<td>51,802</td>
<td>17,983</td>
</tr>
<tr>
<td><strong>Investing activities:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Purchases of securities</td>
<td>(143,519)</td>
<td>(132,266)</td>
</tr>
<tr>
<td>Proceeds from disposals and maturities of securities</td>
<td>93,738</td>
<td>101,975</td>
</tr>
<tr>
<td>Investment in partnership</td>
<td>(2,400)</td>
<td>-</td>
</tr>
<tr>
<td>Purchases of fixed assets</td>
<td>(3,409)</td>
<td>(3,581)</td>
</tr>
<tr>
<td><strong>Net cash used in investing activities</strong></td>
<td>(55,590)</td>
<td>(33,872)</td>
</tr>
<tr>
<td><strong>Financing activities:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Surplus contributions</td>
<td>9,856</td>
<td>12,966</td>
</tr>
<tr>
<td><strong>Net change in cash and cash equivalents</strong></td>
<td>6,068</td>
<td>(2,923)</td>
</tr>
<tr>
<td>Cash and cash equivalents, beginning of year</td>
<td>39,347</td>
<td>42,270</td>
</tr>
<tr>
<td><strong>Cash and cash equivalents, end of year</strong></td>
<td>$45,415</td>
<td>$39,347</td>
</tr>
</tbody>
</table>

See accompanying summary of accounting policies and notes to consolidated financial statements.
Summary of Significant Accounting Policies

Organization

Texas Medical Liability Trust (TMLT) was formed in June 1978 to provide professional liability insurance coverage to eligible physicians who are members of the Texas Medical Association (TMA) and who practice primarily in Texas. TMLT was organized under Article 21.49-4 of the Texas Insurance Code under the name “Texas Medical Association Health Care Liability Claim Trust” and began operations in 1979.

TMLT provides professional liability coverage to certain physicians who are non-TMA members and the ancillary staff of TMLT’s policyholders through its wholly-owned subsidiary, Texas Medical Insurance Company (TMIC), which was formed in 1995 as a state-regulated property/casualty insurance company.

Basis of Presentation

The consolidated financial statements include the accounts of TMLT and TMIC (collectively the “Trust”) after elimination of all significant intercompany accounts.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Such estimates and assumptions could change in the future as more information becomes known which could impact the amounts reported and disclosed herein.

Premiums

Policies written are generally for a one-year term and premiums are recorded as earned on a pro rata basis over the life of the policy. Policies are written on both an occurrence and claims-made basis. Unearned premiums represent the portion of premiums written which are applicable to the unexpired terms of the policies in force and are computed on a daily pro-rata basis.

Billings for calendar year premiums are rendered in advance of the premium year. Also, surplus deposits are received from physicians applying for coverage in advance of approval of their application. Premiums and deposits collected in advance of the period covered are classified as premiums received in advance.

Unpaid Losses and Loss Adjustment Expenses

Unpaid losses and loss adjustment expenses represent the estimated liability for claims reported through year end (case-basis) plus the estimated losses and loss adjustment expenses relating to incidents incurred but not yet reported. These amounts have been estimated by management and the Trust’s consulting actuaries based on available industry data and the Trust’s actual experience and represent estimates of the ultimate cost of all losses incurred, but unpaid, through year end. However, the ultimate cost of settling claims may vary significantly from the estimated liability. The estimates are continually reviewed and adjusted as necessary; such adjustments are included in current operations and are accounted for as changes in estimates.
Unpaid losses and loss adjustment expenses have been discounted using a 6% factor as of December 31, 2005 and 2004. This discount reduces gross unpaid losses and loss adjustment expenses to their present value. The discount amount was approximately $15,800 at December 31, 2005 and 2004.

The Trust considers anticipated investment income in determining whether a premium deficiency exists on the unexpired terms of the policies in force. No such deficiency exists as of December 31, 2005 and 2004.

Reinsurance

Amounts recoverable from reinsurers for unpaid losses and loss adjustment expenses and the amounts payable to reinsurers for reinsurance premiums are estimated in a manner consistent with the related liabilities associated with the reinsured policies. Consistent with the estimate of the unpaid loss and loss adjustment expenses, the reinsurance balances are discounted at a rate of 4%. Adjustments to the provisional reinsurance premiums are provided for in the ceded premiums.

Amounts paid to reinsurers under prospective, short-duration reinsurance contracts are recorded as prepaid reinsurance premiums which are recognized as the related premiums are earned.

Investments

Statement of Financial Accounting Standards ("SFAS") No. 115 requires that certain debt and equity securities be classified into one of three categories: held-to-maturity, available-for-sale, or trading securities. Investments in debt securities that the enterprise has the positive intent and ability to hold to maturity are classified as held-to-maturity and reported at amortized cost in the statement of financial position. Securities that are bought and held principally for the purpose of selling them in the near term (thus held for only a short period of time) are classified as trading securities and reported at fair value. Trading generally reflects active and frequent buying and selling, and trading securities are generally used to generate profit on short-term differences in price. Investments not classified as either held-to-maturity or trading securities are classified as available-for-sale securities and reported at fair value.

Investments, except investments in certain annuities, are categorized as available-for-sale. Accordingly, the investment portfolio is carried at fair value. Unrealized holding gains and losses on securities are reported in accumulated other comprehensive income (loss) and are classified as a separate component of policyholders’ surplus.

Investments in annuities are classified as held to maturity and are carried at amortized cost. The Trust has the intent and ability to hold these investments to maturity.

The cost of fixed-maturity securities is adjusted for amortization of premiums and accretion of discounts to maturity, or in the case of loan-backed securities, over the estimated life of the security using the effective interest method. Such amortization and interest earned are included in investment income. Realized gains and losses are included in net realized gains on investments. The cost of securities sold is based on the specific identification method.
Summary of Significant Accounting Policies

Income Taxes
The Trust uses the liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

Acquisition Costs
Acquisition costs are expensed as they are incurred; the financial statement effect of this method does not differ significantly from the effect of using the deferral method.

Cash Equivalents
Money market funds and commercial paper with initial maturities of less than three months are considered to be cash equivalents.

Reclassifications
Certain prior year balances have been reclassified to conform to current year presentation.

Disclosures about Fair Value of Financial Instruments
The fair value of financial instruments, as defined by accounting principles generally accepted by the United States of America, approximates the recorded book value of such instruments.
1. Comprehensive Income

In accordance with SFAS 130, Reporting Comprehensive Income, the Trust presents comprehensive income within the consolidated statements of changes in policyholders’ surplus.

Components of other comprehensive income consist of the following:

<table>
<thead>
<tr>
<th>Years ended December 31,</th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>(in thousands)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Changes in unrealized (losses) gains on available-for-sale securities</td>
<td>$(6,653)</td>
<td>$1,238</td>
</tr>
<tr>
<td>Deferred income tax benefit (expense)</td>
<td>2,262</td>
<td>(420)</td>
</tr>
<tr>
<td>Other comprehensive (loss) income</td>
<td>$(4,391)</td>
<td>$818</td>
</tr>
</tbody>
</table>

Accumulated other comprehensive income shown on the consolidated statements of changes in policyholders’ surplus is solely comprised of unrealized gains (losses) from available-for-sale securities, net of tax of $(2,262) and $420 for the years ended December 31, 2005 and 2004, respectively.

2. Securities

The amortized cost and the fair value of the Trust’s investments in fixed maturity securities and annuities for both available for sale and held to maturity are summarized as follows:

<table>
<thead>
<tr>
<th>December 31, 2005:</th>
<th>Amortized Cost</th>
<th>Gross Unrealized Gains</th>
<th>Gross Unrealized Losses</th>
<th>Estimated Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>(in thousands)</td>
<td>(in thousands)</td>
<td>(in thousands)</td>
<td></td>
<td>(in thousands)</td>
</tr>
<tr>
<td>U.S. Government and its agencies</td>
<td>$116,680</td>
<td>$83</td>
<td>$1,347</td>
<td>$115,416</td>
</tr>
<tr>
<td>Annuities</td>
<td>24,500</td>
<td>3,101</td>
<td>-</td>
<td>27,601</td>
</tr>
<tr>
<td>Corporations</td>
<td>62,594</td>
<td>186</td>
<td>1,444</td>
<td>61,336</td>
</tr>
<tr>
<td>Loan-backed securities and collateralized mortgage obligations and other</td>
<td>143,352</td>
<td>666</td>
<td>4,006</td>
<td>140,012</td>
</tr>
</tbody>
</table>

| Total | $347,126 | $4,036 | $6,797 | $344,365 |

Notes to Consolidated Financial Statements
Notes to Consolidated Financial Statements

December 31, 2004:

<table>
<thead>
<tr>
<th></th>
<th>Amortized Cost</th>
<th>Gross Unrealized Gains</th>
<th>Gross Unrealized Losses</th>
<th>Estimated Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. Government and its agencies</td>
<td>$ 10,218</td>
<td>$ 283</td>
<td>$ 10</td>
<td>$ 10,491</td>
</tr>
<tr>
<td>Annuities</td>
<td>29,714</td>
<td>1,391</td>
<td>-</td>
<td>31,105</td>
</tr>
<tr>
<td>Corporations</td>
<td>95,155</td>
<td>1,738</td>
<td>520</td>
<td>96,373</td>
</tr>
<tr>
<td>Loan-backed securities</td>
<td>181,803</td>
<td>2,027</td>
<td>2,908</td>
<td>180,922</td>
</tr>
<tr>
<td>and collateralized</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>mortgage obligations</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>and other</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>$ 316,890</td>
<td>$ 5,439</td>
<td>$ 3,438</td>
<td>$ 318,891</td>
</tr>
</tbody>
</table>

At December 31, the Trust's investment in common stocks and preferred stocks had a cost basis of $40,651 and $21,635 in 2005 and 2004, respectively. Gross unrealized gains and gross unrealized losses were $4,925 and $3,922, respectively in 2005 and $3,462 and $2,279, respectively in 2004.

The fair values generally represent quoted market value prices for securities traded in the public marketplace or analytically determined values using bid or closing prices for securities not traded in the public marketplace.

The amortized cost and estimated fair value of the fixed-maturity securities and annuities at December 31, 2005 are summarized, by stated maturities, as follows:

<table>
<thead>
<tr>
<th></th>
<th>Amortized Cost</th>
<th>Estimated Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(in thousands)</td>
<td></td>
</tr>
<tr>
<td>Years to maturity:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>One or less</td>
<td>$ 2,533</td>
<td>$ 2,520</td>
</tr>
<tr>
<td>After one through five</td>
<td>68,147</td>
<td>66,733</td>
</tr>
<tr>
<td>After five through ten</td>
<td>53,975</td>
<td>52,122</td>
</tr>
<tr>
<td>More than ten</td>
<td>119,898</td>
<td>121,910</td>
</tr>
<tr>
<td>Loan-backed securities</td>
<td>102,573</td>
<td>101,080</td>
</tr>
<tr>
<td>and collateralized</td>
<td></td>
<td></td>
</tr>
<tr>
<td>mortgage obligations</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>$ 347,126</td>
<td>$ 344,365</td>
</tr>
</tbody>
</table>

Actual maturities may differ from the contractual maturities in the foregoing table because certain borrowers have the right to call or prepay obligations with or without call or prepayment penalties.

Proceeds from the sales of available-for-sale securities were $93,738 in 2005 and $98,480 in 2004. Gross realized gains and gross realized losses on these sales were $1,696 and $912, respectively, during 2005, and $1,463 and $805, respectively, during 2004. For the year ended December 31, 2005, the Trust recognized an other than temporary decline in fair market value on securities of $400 and is included in net realized losses on securities available for sale in the consolidated statements of operations.
### 3. Unpaid Losses and Loss Adjustment Expenses

The following table provides a reconciliation of the beginning and ending reserve balances for unpaid losses and loss adjustment expenses (LAE), net of reinsurance recoverables, for 2005 and 2004:

<table>
<thead>
<tr>
<th>Years ended December 31,</th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>(in thousands)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Reserve for unpaid losses and LAE, net of related reinsurance recoverables at beginning of the year</td>
<td>$218,148</td>
<td>$270,060</td>
</tr>
<tr>
<td>Add provision for claims, net of reinsurance, occurring in:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current year</td>
<td>74,192</td>
<td>75,732</td>
</tr>
<tr>
<td>Prior years</td>
<td>(969)</td>
<td>42,273</td>
</tr>
<tr>
<td>Incurred losses during the current year, net of reinsurance</td>
<td>73,223</td>
<td>119,005</td>
</tr>
<tr>
<td>Deduct payments for claims, net of reinsurance, occurring in:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current year</td>
<td>4,011</td>
<td>97,160</td>
</tr>
<tr>
<td>Prior years</td>
<td>7,587</td>
<td>163,330</td>
</tr>
<tr>
<td>Net claim payments during the year</td>
<td>101,171</td>
<td>170,917</td>
</tr>
<tr>
<td>Reserve for losses and LAE, net of related reinsurance recoverables, at end of year</td>
<td>190,200</td>
<td>218,148</td>
</tr>
<tr>
<td>Reinsurance recoverables on unpaid losses and LAE, at end of year</td>
<td>50,633</td>
<td>53,411</td>
</tr>
<tr>
<td>Reserve for unpaid losses and LAE, gross of reinsurance recoverables on unpaid losses, at end of year</td>
<td>$240,833</td>
<td>$271,559</td>
</tr>
</tbody>
</table>

The foregoing reconciliation shows that the Trust’s reserve for unpaid losses and LAE, net of related reinsurance recoverable, at December 31, 2005 decreased by approximately $969 primarily as a result of favorable reserve development. The decrease is a result of ongoing analysis of recent loss development trends. Original estimates are increased or decreased as additional information becomes known regarding individual claims. At December 31, 2004, unpaid losses and LAE, net of reinsurance increased by $43,273 for claims that had occurred on or prior to 2003. During 2004, the Trust increased reserves due to higher than anticipated loss severity and frequency, which resulted in higher reserves for 2004 and prior year’s reported claims. This change in management’s estimate of claims resulted from plaintiff’s attorney’s response to 2004 changes in the procedure for filing lawsuits and the time period allowed for discovery in Texas.

Medical malpractice claims have a very long development period. Historically, cases have taken years to be reported and, as a rule, take years to adjust, settle, or litigate. With respect to the Trust’s estimates of reserves for unpaid losses and LAE, there is
additional uncertainty related to the strength of case reserves and the effect of changes in the reinsurance of ALAE. Accordingly, should management’s assumptions as to case reserve redundancies or reinsurance recoverables differ from the actual closure of claims, reserves are likely to develop adversely. Loss and loss adjustment reserve estimates are reviewed regularly and adjusted, as appropriate.

4. Reinsurance

The Trust cedes certain risks to various reinsurers. These reinsurance arrangements allow management to control exposure to potential losses arising from large risks and provide additional capacity for growth. A significant portion of the reinsurance is affected under quota-share reinsurance contracts and, in some cases, stop-loss coverage.

Ceded premiums are charged to operations as a deduction from premiums written. The effect of reinsurance on premiums written and earned are as follows:

<table>
<thead>
<tr>
<th></th>
<th>2005 Premiums</th>
<th>2004 Premiums</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Written</td>
<td>Earned</td>
</tr>
<tr>
<td>Direct</td>
<td>$190,710</td>
<td>$191,466</td>
</tr>
<tr>
<td></td>
<td>(23,727)</td>
<td>(26,810)</td>
</tr>
<tr>
<td>Ceded</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net premiums</td>
<td>$166,983</td>
<td>$164,656</td>
</tr>
</tbody>
</table>

The amounts deducted from losses and loss adjustment expenses in the statements of operations that related to reinsurance were $8,126 for 2005 and $22,991 for 2004.

Reinsurance ceded contracts do not relieve the Trust from its obligations to policyholders. The Trust remains liable to its policyholders for the portion reinsured to the extent that any reinsurer does not meet the obligations assumed under the reinsurance agreements. To minimize its exposure to significant losses from reinsurer insolvencies, the Trust evaluates the financial condition of its reinsurers and monitors concentrations of credit risk arising from similar geographic regions, activities or economic characteristics of the reinsurers.

5. Federal Income Taxes

Significant components of the provision for income tax expense (benefit) were as follows:

<table>
<thead>
<tr>
<th>Years ended December 31,</th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>(in thousands)</td>
<td></td>
</tr>
<tr>
<td>Current expense</td>
<td>$25,338</td>
<td>$8,293</td>
</tr>
<tr>
<td>Deferred expense (benefit)</td>
<td>(700)</td>
<td>(5,208)</td>
</tr>
<tr>
<td></td>
<td>$24,638</td>
<td>$3,085</td>
</tr>
</tbody>
</table>
Significant components of the Trust’s deferred tax assets and liabilities were as follows:

<table>
<thead>
<tr>
<th>December 31,</th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td>(in thousands)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Deferred tax assets:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Loss reserve discounting</td>
<td>$ 9,521</td>
<td>$ 10,981</td>
</tr>
<tr>
<td>Unearned premium discounting</td>
<td>5,765</td>
<td>5,758</td>
</tr>
<tr>
<td>Other</td>
<td>1,615</td>
<td>1,825</td>
</tr>
<tr>
<td>Total deferred tax assets</td>
<td>16,901</td>
<td>18,564</td>
</tr>
<tr>
<td>Valuation allowance for deferred tax assets</td>
<td>-</td>
<td>(1,825)</td>
</tr>
<tr>
<td>Total deferred tax assets, net of allowance</td>
<td>16,901</td>
<td>16,739</td>
</tr>
<tr>
<td>Deferred tax liabilities:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td>(601)</td>
<td>(1,139)</td>
</tr>
<tr>
<td>Net deferred tax asset</td>
<td>$ 16,300</td>
<td>$ 15,600</td>
</tr>
</tbody>
</table>

Under the provisions of FASB Statement No. 109, the Trust is required to record a valuation allowance on a deferred tax asset, if it is more likely than not that the benefit will not be realized. Accordingly, the Trust established a valuation allowance of $1,825 as of December 31, 2004. Management believes that it is more likely than not that the net deferred tax asset recorded at December 31, 2005 will be realized from expected future taxable income.

The differences between the income tax benefit reported and the income tax benefit that would result from applying domestic federal statutory rates to pretax income in 2005 resulted primarily from the effects of tax-exempt interest and changes in the valuation allowance. Income tax paid during 2005 was $19,938.

6. Revolving Line-of-Credit

The Trust entered into an agreement with a commercial lender which provides the Trust with a revolving credit facility of $25,000 ($13,518 outstanding at December 31, 2005 and 2004). The funds available under the credit agreement may be used for general corporate purposes. The revolving credit facility expires in January, 2008. Under the revolving credit facility, the Trust granted liens with respect to certain fixed maturity investments owned by the Trust.

Interest on borrowings under the credit agreement is determined, at the Trust’s option, based on the prime rate minus 2.35% or the LIBOR rate plus a margin of 0.7%. There is a commitment fee of .08% on the unused balance. At December 31, 2005, the prime rate was 7.25%. In January 2005, the Trust entered into an interest rate swap transaction, whereby the transaction effectively hedged its variable rate to a fixed rate of 4.02% on $7,500,000. The swap will expire in February 2007. The effects of this transaction have been included in the Trust’s earnings.
7. Policyholders' Surplus

Eligible physicians desiring to purchase insurance through the Trust are required to purchase a Surplus Deposit Certificate. The Surplus Deposit Certificates are offered solely to provide surplus for the Trust and do not bear interest. Surplus contributions are refunded to the physician at the discretion of the Trust or when a physician dies, becomes disabled or retires.

As of December 31, 2005 and 2004, surplus contributions receivable of $1,000 and $3,000, respectively, represent collections subsequent to year-end but prior to the issuance of the consolidated financial statements. In accordance with EITF 85-1, these amounts were recorded as an asset as opposed to a reduction of policyholders’ surplus.

8. Commitments and Contingencies

The Trust leases office facilities and certain equipment through agreements which expire through 2011. As of December 31, 2005, the future minimum lease payments under these noncancelable agreements for the years ending December 31 are as follows:

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount (in thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>$1,135</td>
</tr>
<tr>
<td>2007</td>
<td>1,135</td>
</tr>
<tr>
<td>2008</td>
<td>1,387</td>
</tr>
<tr>
<td>2009</td>
<td>1,387</td>
</tr>
<tr>
<td>2010 and thereafter</td>
<td>2,773</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$7,817</strong></td>
</tr>
</tbody>
</table>

Total rent expense was $1,217 for 2005 and $835 for 2004.

The Trust is named as a defendant in various legal actions principally from claims made under insurance policies. Those actions are considered by the Trust in estimating the loss and loss adjustment expense reserves. The Trust's management believes that the resolution of those actions will not have a material adverse effect on the Trust's financial position or results of operations. In lieu of purchasing surety bonds on cases being appealed, the Trust has placed $4,145 in deposits with the courts.

9. Concentrations of Credit Risk

The Trust has concentrations of credit risks relating to reinsurance recoverable balances and cash balances at financial institutions in excess of insured amounts. The Trust believes the risk of incurring material losses related to these credit risks is unlikely.

10. Employee Benefit Plan

The Trust sponsors a noncontributory, defined contribution employee benefit plan, which covers all employees who have completed one year of service. The Trust makes contributions to the Plan equal to 10% of participants' salaries. Such contributions are reduced by forfeitures of participants who leave the Plan before they become fully vested. Plan expense was $1,468 for 2005 and $1,445 for 2004.
11. Fair Value of Financial Instruments

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

Cash and Cash Equivalents. For those cash equivalents, the carrying value amount is a reasonable estimate of fair value.

Investment in Securities. For investments in securities, fair values are based on quoted market prices or dealer quotes, if available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Accounts Payable, Accrued Expenses and Revolving Line-of-Credit. The carrying values approximate fair value.

The estimated fair values of the Trust’s financial instruments which are not disclosed on the face of the balance sheet or elsewhere in the notes are as follows:

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Carrying Amount</td>
<td>Fair Value</td>
</tr>
<tr>
<td>(in thousands)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>$45,415</td>
<td>$45,415</td>
</tr>
<tr>
<td>Fixed maturity securities</td>
<td>347,126</td>
<td>344,365</td>
</tr>
<tr>
<td>Common stocks</td>
<td>40,457</td>
<td>40,457</td>
</tr>
<tr>
<td>Preferred stocks</td>
<td>1,197</td>
<td>1,197</td>
</tr>
<tr>
<td>Accounts payable and</td>
<td>(875)</td>
<td>(875)</td>
</tr>
<tr>
<td>accrued expenses</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Revolving line-of-credit</td>
<td>(13,518)</td>
<td>(13,518)</td>
</tr>
</tbody>
</table>
LETTERS

“I would like to take the opportunity to tell you how much I appreciate Texas Medical Liability Trust. From Sales and Underwriting to Claims management and Counsel Selection/Support, everything has been superb. This has not been an experience that I would like to repeat, but I rest much better knowing that you are all there in the event another claim rears its ugly head.”
— a cardiovascu

“TMLT’s practice review prompted us to do an in-depth self-examination of our practice. Suggestions will be implemented and we will improve our practices and documentation.”
— a plastic surgeon in San Antonio

“Very thorough and helpful. Will use the information to decrease medical liability”
— an orthopaedic physician in Irving

“I would like to thank you personally for doing such an outstanding job preparing me and defending my case. When I went into medicine, I did it to make a difference in peoples lives, and I believe I have hundreds of times. . . Your compassion and concerns will always make an impression on me as I continue to practice medicine to the very best of my ability.”
— an ob-gyn in North Texas, commenting on TMLT defense counsel

“I really enjoyed TMLT’s online course ‘He’s not my patient—is he?’ It was really convenient being able to take it at home and the course content was interesting.”
— a family physician in El Paso

“I’d like to thank TMLT for all of their help. This was an extremely stressful time for me, and I appreciate all you did to make the situation better. I hope to never be in this situation again, but if I am it will be much less intimidating knowing I have all of you standing beside me.”
— a radiologist in East Texas

“I was very pleased with my claim supervisor. He was always informed regarding my case, the options, and facts. My defense attorney was excellent, and I felt very well represented, well prepared, and in competent hands regarding my defense.”
— a surgeon in Dallas

“Very helpful for my practice to see areas where we can improve to avoid potential liability”
— an internal medicine physician in Wichita Falls

“TMLT’s risk management education for physicians is the best I’ve ever seen. It’s interesting, comprehensive and presented in a fashion that ensures physicians understand what they need to do to minimize their exposure.”
— a general surgeon in Houston

“I wish to give my heartfelt thanks to TMLT, my claim supervisor, and my defense attorney team for their professionalism, skill, and savvy in defending me from a claim this year. My TMLT claim supervisor was my first contact with TMLT when this claim arose, and I could not have asked for a more knowledgeable, experienced, and kind individual to work with. My defense team led me through the legal maze expertly. They made themselves easily available and their obvious talent and experience was very reassuring.”
— an orthopaedic physician in Dallas, commenting on TMLT defense counsel

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“The only health care liability claim trust created and endorsed by Texas Medical Association

TMLT is your partner in trust.

Does your medical liability carrier do enough to protect your reputation and career? TMLT’s philosophy is to defend doctors, not pay non-meritorious claims. Guided by this philosophy, we have resolved more than 38,000 claims, closing more than 87% with no indemnity payment. The right protection can make all the difference. TMLT is your partner in trust.

Partners in Protection

www.tmlt.org

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