



Medical  MutualSM

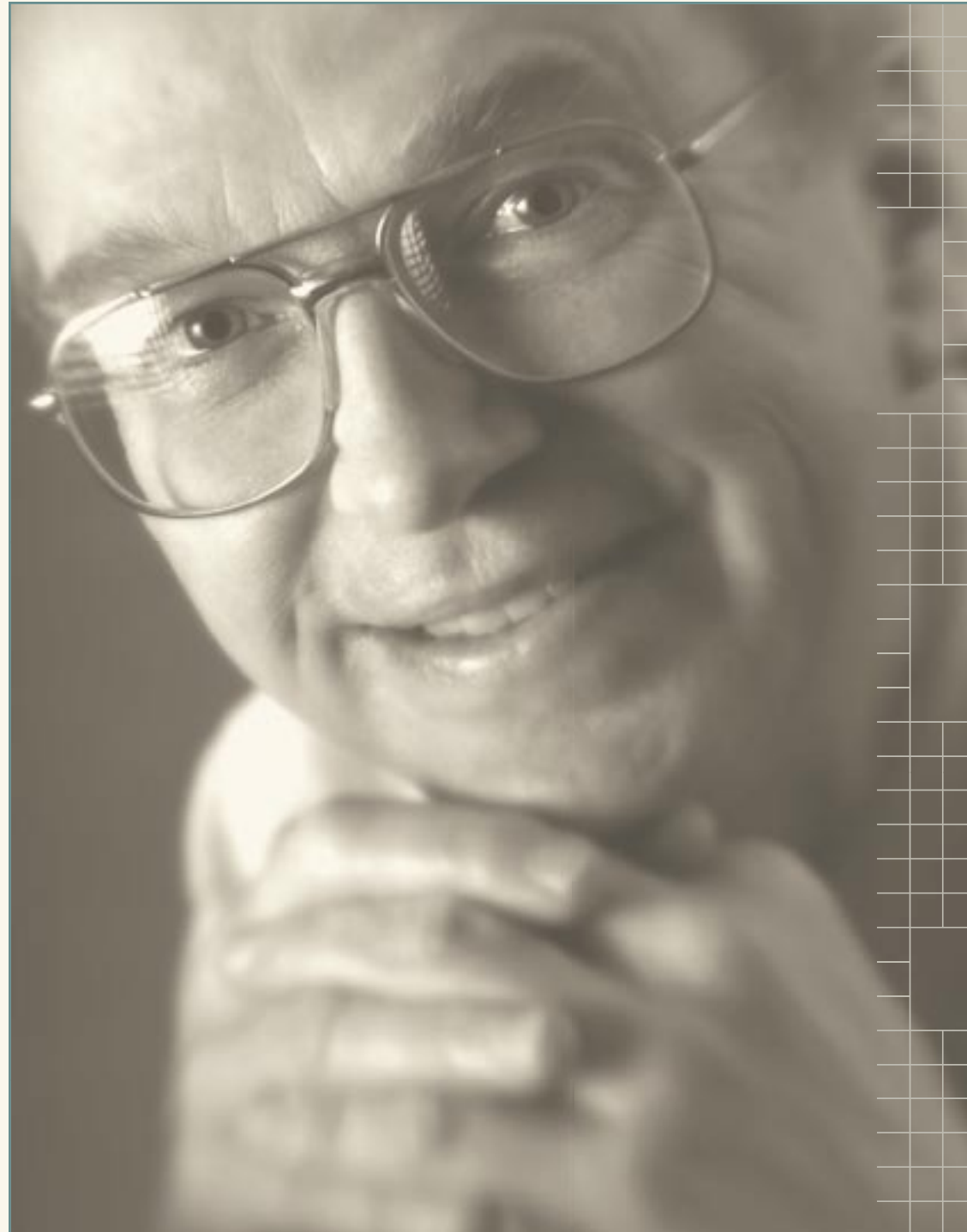
Annual Report

2004

the strength

OF STABILITY





“Medical Mutual distinguishes itself from other professional liability companies by its emphasis on preventive services. The Medical Mutual team partners with client owners, analyzing the practice environment for areas of exposure. The insurance specialists then work with practice personnel as change agents to reduce risk. This collaborative approach to prevention is a winning business strategy for both Medical Mutual and its physician members.”

William D. Zalabak, Jr.
• Practice Administrator
• Mountain Medical Associates, L. L. P.
• Clyde, NC



TO OUR MEMBERS

“Physician.” Over the course of time, perhaps there has been no more honorable profession. Men and women who are medical doctors are a special breed—a select few who have been called and singled out to heal and to provide hope to all. Without physicians, disease and illness would maim and kill. Without physicians, pain and suffering would be uncontrollable. Without physicians, the quality of life we enjoy today would not be possible. We depend on physicians every day to make our world a better place.

Hardly anyone would disagree with the preceding comments. Yet today, physicians have never faced more serious threats. From the expectations of perfection in treatment and complete cures for every disease, to the endless avalanche of information required to submit to obtain declining reimbursements, physicians have never faced more pressure. Patients, and the health insurance companies who cover them, want quality care, at a bargain price. As a result, physicians are being required to do more with less—to work longer hours, see more patients, and streamline their expenses where possible. Some would argue that this is a good thing, in that the system demands greater efficiency. However, more knowledgeable people recognize the danger in “high volume” medicine—time constraints cause the patient-physician relationship to become strained, and the risk of errors to increase. No wonder more and more physicians are contemplating giving up the profession they love.

As a physician-owned and directed company, Medical Mutual understands the tremendous pressure that physicians face today. During our meetings with hundreds of you last year, we heard you describe horror stories about how difficult it is today to practice medicine. From HIPAA to class action suits involving popular medications, physicians face a constant barrage of issues that consume countless amounts of time—time that otherwise could be spent with patients. Unfortunately, Medical Mutual cannot solve all of the issues you face today. But we can help reduce the likelihood of your being sued for malpractice. And, if you are sued, we can defend you better than anyone else. That is why physicians formed our company 30 years ago. That is why we still exist today.

2004 was a very busy and active year for your company. We continued the pursuit of new ideas in risk management, focusing, with the help of nationally renowned experts, on appropriate communication methods of adverse outcomes—physician to patient, and physician to physician. We explored new ideas in the area of claims defense to reduce the amount of time and expense required to investigate and adjudicate claims, and we worked with hundreds of physicians as they looked at new procedures and techniques to improve their care giving ability. We did extensive underwriting research in certain specialties, such as bariatric surgery, to make sure we fully understood the various risk elements involved in these areas. We worked with physicians in these specialties to develop ways to mitigate risk we discovered. And, internally, we implemented new

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OPERATING HIGHLIGHTS:

A. M. Best upgrades the financial rating of Medical Mutual to “A” Excellent.

The total physicians insured by the Company surpasses 8,000, an all time high.

Written premiums increase 18% to almost \$114 million.

The Company’s operating expense ratio drops to 9.1%—among the lowest, if not the lowest, in the industry.

The Company’s investments provide an overall yield of 7.02%.

Net income of the Company is \$6.8 million, which allows the Company to maintain financial ratios necessary to support its industry and regulatory ratings.

Subsidiary operations of the company contribute an aggregate of \$2.8 million in income to support core insurance operations.

**MAINTAINING RISK /
EDUCATING MEMBERS:**

The Risk Management Department at Medical Mutual successfully achieves four year re-accreditation by the Accreditation Council for Continuing Medical Education (ACCME).

1,500 providers are awarded with Level 1 Continuing Medical Education (CME) credits, totaling more than 3400 credit hours.

Nearly 500 providers are surveyed through the Priority Practice Quality Survey (PPQS) instrument focusing 61% of their effort on reaching practices with five or fewer providers.

Seminars targeted to medical office staff occur in practices undergoing a Risk Management survey, reaching nearly 500 attendees.

Medical Mutual initiates a comprehensive informed consent review process including clinical review by many of our physicians.

technology platforms that will give us more detailed, meaningful data to help us better analyze and manage our business in the future.

2004 produced solid financial results for the Company. As we discussed in our December *MedNotes* article, it is important for the Company to achieve an operating profit and to attain certain financial ratios. Outside rating and regulatory organizations consider those ratios in their determination of our financial strength and solvency. We are pleased that during 2004, AM Best, the oldest and most respected insurance rating organization, upgraded Medical Mutual from an "A-" to an "A". Medical Mutual joins a small group of only eight malpractice insurance companies that carry the "A" rating. We have worked hard to achieve this rating because we know how important it is for you to feel confident that this company will always be here when you need us. Medical Mutual and its rating are testaments to what physicians can do when they work together to solve a common problem.

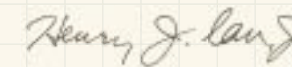
In the 2003 Annual Report, we spoke considerably about the need for meaningful tort reform in North Carolina. During 2004, we traveled across the State holding a series of meetings to educate and inform physicians about the medical malpractice landscape and the importance of their engagement in the campaign for reform. More than a thousand physicians attended those meetings. Efforts undertaken in coalescing a large number of physicians, singularly focused on medical liability reform, has spurred a non-partisan approach to aggressively pursuing reform. The execution of that strategy is now occurring daily, in conjunction with the efforts of the North Carolina Medical Society.

We believe that certain reforms can be achieved in 2005, so long as physicians remain actively engaged in the political process. No one can speak as effectively as you can for your patients and your profession. Thanks to all of you who have taken up the cause and are using your time and influence to make a difference.

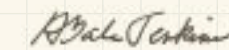
Throughout our report this year, we have highlighted some of the accomplishments achieved by the Company this year. Perhaps more importantly, we have also included comments from five of your colleagues regarding what Medical Mutual means to them and their practices.

Our mission is to serve you and provide you with the most affordable, stable malpractice insurance program possible. That was the mission of the Company in 1975, and it remains even more true in 2005. We sincerely appreciate your support and are honored and privileged to count you as a member of the Medical Mutual family.

Sincerely yours,



Henry J. Carr, Jr., MD
Chairman and President



A. Dale Jenkins
Chief Executive Officer

"I have had the pleasure of working with Medical Mutual since 1987. Our group of 50 years has participated with the Company since its inception. We have found Medical Mutual to be extremely helpful in educating us about malpractice and working with us to reduce our risks.

As rural obstetricians/gynecologists, we are exposed to high risk patients on a regular basis. We have found great comfort in personally knowing Medical Mutual management and the Diamond Defense Team. We look forward to continuing our relationship through these difficult times."

Steve Chamberlain, MD
• Obstetrician/Gynecologist
• Shelby Women's Care
• Shelby, NC



P R O T E C T I N G Y O U R F U T U R E





“Medical Mutual and its representatives have been an indispensable resource to our group as we continue to face the medical malpractice crisis. As emergency physicians, we take on a lot of risk and have come to rely on the excellent insights and advice made available by Medical Mutual. I really feel that a partnership has been forged and that our group is better able to care for patients in this challenging environment. The leadership Medical Mutual has shown in tackling the liability crisis has been outstanding. We are glad to have such a partner working with us to continue to provide quality health care to our community.”

Marylu Kataja, MD, FACEP
 • Emergency Physician
 • Cabarrus Emergency Medicine Associates
 • Chief of Staff, NorthEast Hospital Medical Staff
 • Concord, NC



BALANCE SHEET

ASSETS	December 31, 2004	December 31, 2003
Invested Assets	\$ 232,248,055	\$ 202,770,227
Accrued Investment Income	1,886,273	1,757,528
Premiums Receivable	32,635,796	27,424,603
Information Technology Systems	290,998	307,837
Federal Income Taxes	4,594,141	3,785,053
Guaranty Capital Subscription	0	0
Other Assets	672,375	359,656
Total Assets	\$ 272,327,638	\$ 236,404,904

LIABILITIES AND POLICYHOLDERS' SURPLUS

Liabilities		
Loss and LAE Reserves	\$ 126,000,000	\$ 108,800,000
Unearned Premium Reserves	36,638,856	29,789,721
Reinsurance Balances Payable	25,280,493	24,576,904
Other Liabilities	8,274,519	6,723,916
Total Liabilities	\$ 196,193,868	\$ 169,890,541
Policyholders' Surplus	\$ 76,133,770	\$ 66,514,363
Total Liabilities and Policyholder's Surplus	\$ 272,327,638	\$ 236,404,904

MAINTAINING FINANCIAL STRENGTH:

Total assets of the Company grow to \$272 million.

The Company's capital and surplus increase to over \$76 million due to the operating results of the Company and its subsidiaries.

\$126 million is set aside to pay claims that have been reported to the Company—an all time high.

The Company sees its net written premiums to surplus ratio climb slightly to 104%, which remains in line with the industry benchmark of 100%.

The Company's combined ratio, which is the ratio of claims and expenses incurred compared to earned premiums, drops slightly to 95.5%, which is far below the industry average.

Reinsurance programs of the Company are renewed with highly rated carriers at terms resulting in \$1 million annual savings.

**HANDLING AND
DEFENDING CLAIMS:**

707 incidents, claims and suits are reported against Medical Mutual members—a decline of 27 from the number reported during 2003.

The Company pays total claims and claim related expenses of \$50.2 million—an increase of \$6 million from the amount paid in 2003.

63 claims are paid during the year for which the amount exceeds \$100,000, and 9 claims are paid where the amount exceeds \$1 million.

Of the claims closed during the year, 86% are closed without any payment being made to the plaintiff; on average, the Company spends \$15,000 defending each of those claims.

The Company tries 36 cases to a jury verdict, experiencing only 5 losses.

Community Boards gather in Greensboro for a tort reform kick off seminar.

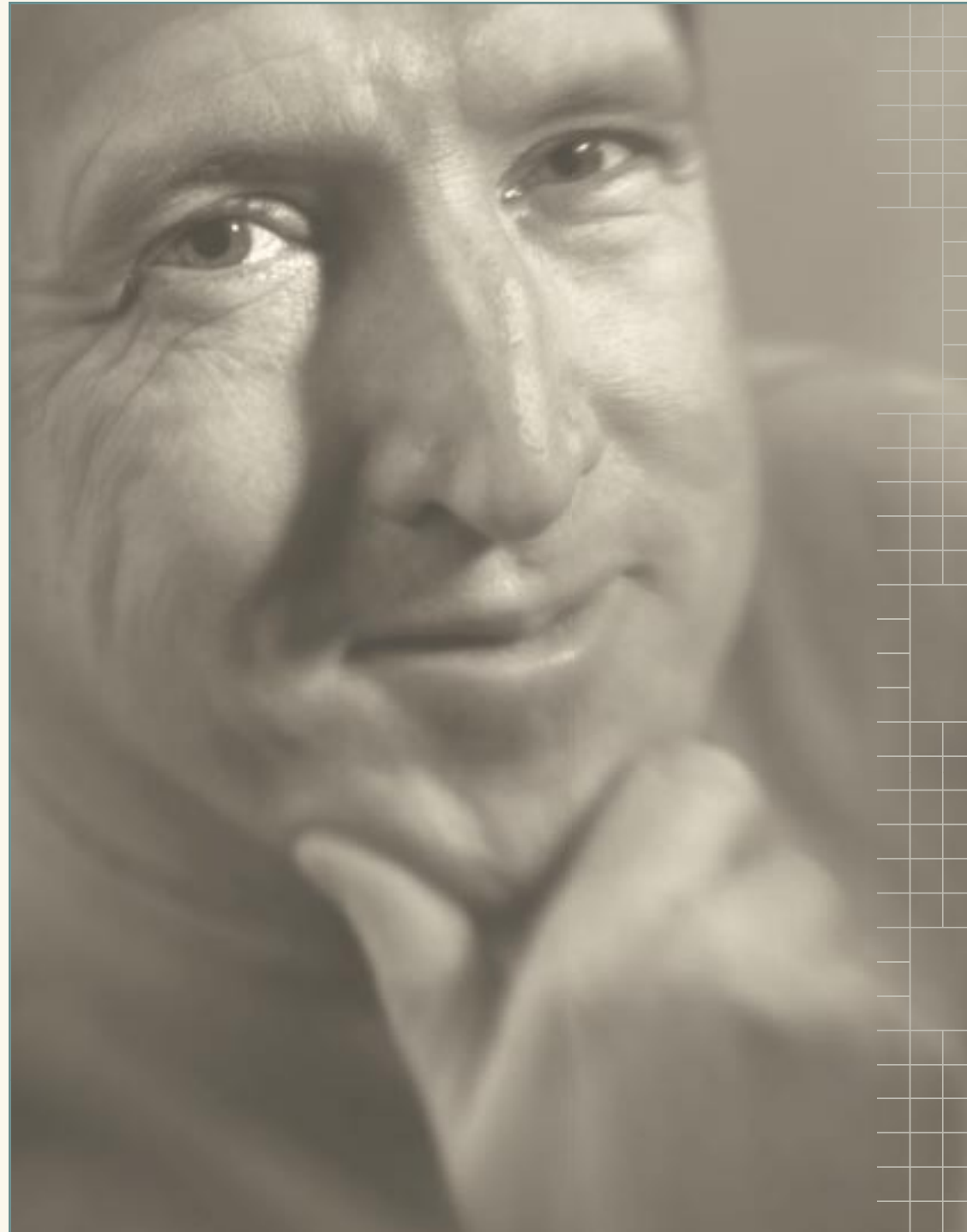
INCOME STATEMENT

	December 31, 2004	December 31, 2003
Direct Written Premiums	\$ 113,807,413	\$ 96,243,700
Assumed Premiums	689,904	521,634
Ceded Reinsurance Premiums	(35,608,376)	(34,995,518)
Net Written Premiums	78,888,941	61,769,816
Change in Unearned Premium Reserve	(6,849,135)	(6,197,962)
Net Earned Premiums	\$ 72,039,806	\$ 55,571,854
Commission (Expense)	(91,456)	102,343
Loss and Loss Adjustment Expense Incurred	(62,284,875)	(48,281,138)
Premium Taxes	(2,564,947)	(2,361,102)
Other Underwriting Expenses	(5,042,233)	(4,266,007)
Underwriting Gain/(Loss)	2,056,295	765,950
Net Investment Income	5,731,200	5,761,487
Other Income	554,381	425,500
Operating Income	8,341,876	6,952,937
Realized Capital Gains	1,688,607	458,687
Federal Income Tax	(3,199,000)	(2,618,000)
Net Income	6,831,483	4,793,624

“I’m fortunate. For the nearly 20 years I have been covered by Medical Mutual, I haven’t needed to call on them. Yet, knowing that they are there, operating in the background, gives me great peace of mind. The information they provide on risk management has been very educational. It is clear to me that the staff at Medical Mutual understand the risk I take each day for my patients. I know that if the need should arise, I can count on their experience and support to assist me. I can’t imagine walking into a patient’s room without that knowledge.”

Maha Abdul-Hafez Elkordy, MD
 • Oncologist
 • Medical Oncology/Hematology Cancer Centers of North Carolina
 • Cary, NC





“When I finished my Family Medicine residency, there was no doubt I would choose Medical Mutual as my insurer. I remember the ‘70s when doctors struggled with an impending mal-practice insurance crisis. In response to this urgent need, doctors in this state founded this great company. We must continue to ensure fairness for patients and physicians in the current judicial system. Our compelling challenge for the present will be to become politically involved and to expedite this process.”

Mott Blair, IV, MD
 • Family Physician
 • Blair Family Practice
 • Wallace, NC



BOARD OF DIRECTORS

Henry J. Carr, Jr., MD
 Chairman

Thomas H. McCoy, MD
 Vice Chairman

H. David Bruton, MD
 Secretary

Charles C. Crowell, III, MD
 A. Dale Jenkins

Victoria C. D. Neave, MD
 Rachel H. Ross, MD

Robert E. Schaaf, MD
 Chris M. Teigland, MD

In Memoriam:

August M. Oelrich, MD (1916-2004)

Dr. Oelrich served on the Medical Mutual

Board of Directors from 1975 until 1989.

He was one of the founding directors.

COMMUNITY BOARDS

Coastal:

William A. Crafford, Jr., MD
 Thaddeus Dunn, MD
 J. William Eakins, MD
 Jessica Burkett, MD
 Mott Blair, IV, MD
 James Hundley, MD
 Michael Moulton, MD

Jeff Kobs, MD

Robert Littleton, MC
 Robert McConville, MD
 William Nebel, MD
 Frank Palombaro, MD
 H. Cliff Patterson, MD
 Earl Ransom, MD
 John W. Rusher, MD
 George Venters, MD

Eastern:

Millard F. Banker, IV, MD
 Deanna Boyette, MD
 Robert Hartley, MD
 Michael Weaver, MD

Triad:

Slade Howell, MD
 John Mann, MD
 Robert Nudelman, MD
 Brian Sumner, MD

Triangle:

Robert Bilbro, MD
 Russ Fisher, MD
 Joan T. Jordan, MD

Charles V. Taft, MD

Virgil Willard, II, MD
 Kyle Young, MD
 Peter Young, MD

Metrolina:

Akinyele O. Aluko, MD
 Dan Dillon, MD
 Allen Dobson, Jr., MD
 Hunter Dyer, MD
 Paul Galentine, MD
 Winston Godwin, Jr., MD
 Steve G. Justus, MD
 Johnson Kelly, MD
 Robert Petrilli, MD
 Clifford Roemer, MD
 Frank Stranick, MD
 Kevin Weiss, MD

Mountain:

Harry Burton, MD
 Steven A. Chamberlain, MD
 Ted Humble, MD
 Harry Lipham, MD

Peter Mangone, MD
 James Montgomery, MD
 Edward Plyler, MD
 William Snoddy, MD

Virginia:

Anthony Cetrone, MD
 Thomas Clifford, MD
 William Dichtel, MD
 Howard Fraunce, MD
 John Kowalski, MD
 John McConnell, MD
 Barry Rothman, MD

COMMUNITY INVOLVEMENT:

Our Community and Administrator Advisory Boards meet twice annually; their input and counsel continue to provide valuable benefits to the Company.

Brenda Mohl, a Thomasville practice administrator, is the recipient of the Medical Mutual/North Carolina Medical Group Managers' Administrator of the Year Award.

The Company and our employees donate almost \$30,000 to the local United Way Campaign.

Medical Mutual participates in community service projects for the Susan G. Komen Breast Cancer Foundation, Special Olympics, Food Bank of North Carolina, Raleigh Rescue Mission, Methodist Home for Children, Habitat for Humanity, Martin Street Baptist Church Clothes Closet, and the American Red Cross.

The Company offers Health and Wellness Seminars for its employees, providing information about cardiovascular health and stress management.



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