COOPERATIVE OF AMERICAN PHYSICIANS

Dedicated to the innovation and excellence that support the success of medical practices and facilities

2014 ANNUAL REPORT

COOPERATIVE OF
AMERICAN PHYSICIANS

Mission Statement

"WE ARE LEADERS AND INNOVATORS IN THE HEALTH CARE COMMUNITY"

Statement of Principles

THROUGH ITS CORE PRODUCTS, Mutual Protection Trust (MPT) and the CAPAssurance Risk Purchasing Group, the Cooperative of American Physicians, Inc. (CAP) provides the best possible medical professional liability protection and related services, maintaining the highest ethical standards in a climate of constant improvement.

OUR MEMBERS, ASSOCIATES, AND AFFILIATES RECEIVE SERVICES that are satisfying, dependable, effective, economical, and valuable.

WE CONTINUALLY DEVELOP KNOWLEDGE and resources that meet the changing legal, societal, and medical environment.

THE ORGANIZATION'S COMMITMENT to financial integrity justifies the continuing confidence of our members.

ALL BUSINESS IS CONDUCTED in accordance with federal, state, and local regulations.

MPT MEMBERSHIP DECISIONS and the disposition of claims are reached by boards and committees of member physicians.

OUR DECISIONS ARE REACHED with information that assists us in both reducing the risks associated with operating a medical practice and enhancing patient care.

OUR EMPLOYEES ARE COMMITTED TO EXCELLENCE and continuous quality improvement.

OUR LEADERSHIP PROVIDES an atmosphere of collaboration, recognition, and fair compensation.

OUR DEDICATION to the medical community, business partners, and the public at large is exemplified by our accountability, innovation, integrity, and a commitment to quality of the highest order.

Chairs' Message

It would be impossible to comment on 2014 without first pointing out that the dedication of CAP's members in helping defeat Proposition 46 is quite likely responsible for scores of medical practices saved and the future health of Californians improved.

That is because the goal of the unprecedented coalition that gathered to defeat Proposition 46 was to protect California's Medical Injury Compensation Reform Act from a scheme that would take money out of health care delivery in order to fund higher courtroom payouts and lawyers' fees.

Thank you for keeping informed of the issues and for talking to your friends, families, and patients on why Californians must work to constantly safeguard access to care. It's a conversation that we as physicians must continue in our medical offices and in the public arena: The voters' two-to-one rejection of Proposition 46 is a good start in what should be an ongoing campaign to keep the public informed on what MICRA means for the health of California's families.

While CAP and its members vigorously pursued Proposition 46's defeat, your organization did not lose sight of what needed to be done to expand CAP's role in the health care system. Two thousand fourteen saw growth in the CAPAssurance Risk Purchasing Group, a program that augments the medical professional liability needs of very large medical groups, hospitals, and facilities with CAP's unique, detailed approach to risk management, education, and patient safety. Meanwhile, bringing members another MPT assessment with no overall increase helps our physicians make the financial investments necessary to offer the best services possible to their patients.

At CAP itself, we welcomed Amir Moradi, MD, a board-certified plastic and reconstructive surgeon in Vista, who was elected to the CAP Board of Directors in July. We thank former directors Malcolm Paul, MD, and Tammy Wu, MD, for their invaluable contributions to CAP's mission.

Now, as we get down to business in 2015, we believe that one of the most important things that CAP can do for its physicians is to help them make their own businesses thrive.

The roots of CAP's support of our members' medical practices (beyond, of course, the A.M. Best A+-rated medical professional liability protection provided through MPT) go back to the creation of our own insurance agency. Today, through CAP Physicians Insurance Agency, Inc., our members can choose from an array of coverages vital to any successful physician, including: Workers' compensation, business owners, and employment practices products for the office; disability, life, and personal umbrella insurance for home and family; and MedGuard and CyberRisk buy-ups to enhance benefits already provided through CAP membership.

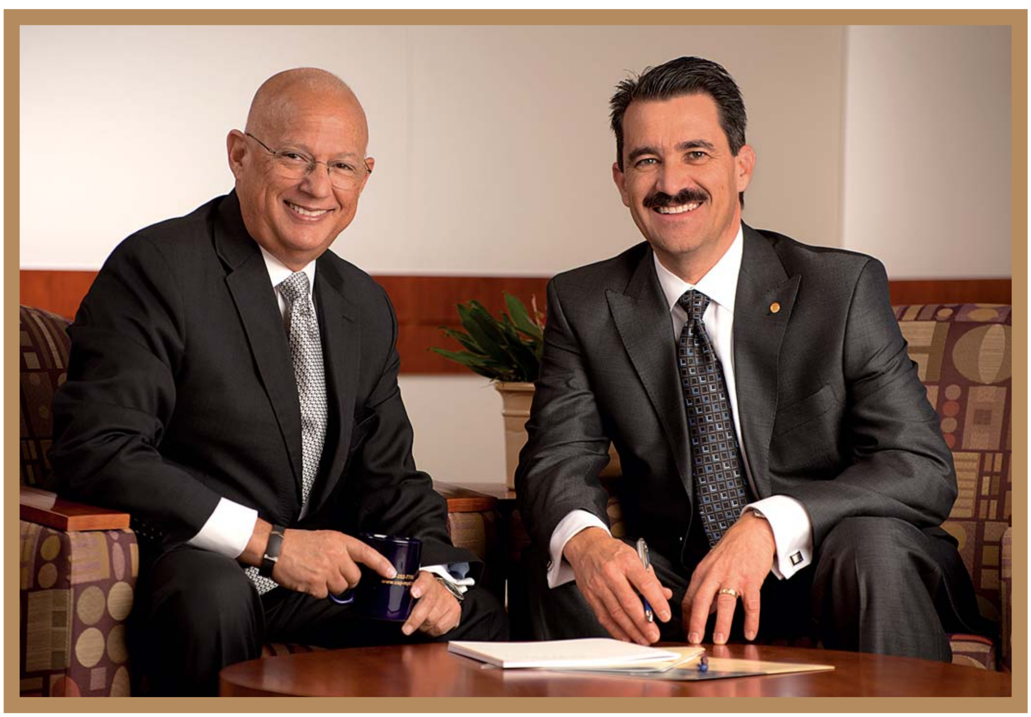
Now in its fourth year is the Practice Management Services Committee, a panel of practicing physicians and staff managers who regularly meet for the sole purpose of finding ways that CAP can help make solo and group practice more financially and personally rewarding. Early products of the Committee's thinking are the Peer Recommended Business Directory and the

CAPSource group-buying program. Through an expanding online directory, members are able to learn about vendors recommended by other members for accounting, business law, billing, and other business needs. And through CAPSource, small-group practices can gain group-purchasing efficiencies previously available only to practices many times as large.

CAP is also expanding its reach to physicians' offices through specially crafted webinars. Already, CAP has brought top-tier speakers to help members implement effective physician-reimbursement techniques and to maintain a positive web presence through social media.

CAP's focus on what health care providers need from their company extends even to the selection of our new chief executive officer, Sarah Pacini. Sarah comes to CAP from Advocate Health Care, the largest health care system in Illinois. At Advocate Health Care, Sarah developed and directed system-wide programs that helped thousands of practitioners provide quality medicine. At CAP, Sarah is charged with directing CAP's efforts to surround our physicians with practice-related solutions while also maintaining MPT's core strengths in superior claims defense and indemnity services.

As our members experiment with different practice models – or simply fine-tune their existing operations – they should continue to look to CAP as their trusted business partner.



Juan Carlos Cobo, MD
Chair, Mutual Protection Trust

Béla S. Kenessey, MD
President and Chair
Cooperative of American Physicians, Inc.

CEO's Message

As Dr. Kenessey and Dr. Cobo have indicated, 2014 brought a landmark decision for the Medical Injury Compensation Reform Act. The fight against Proposition 46 was tracked with intense interest by health care advocates across the country.

The commitment by California physicians to defeat Proposition 46, with the Cooperative of American Physicians taking a leading role, underscores the tenet that tort reform is essential to our nation's overall effort to solve our health care delivery challenges.

While CAP celebrates the resounding support that MICRA received from California's voters, we remain vigilant in the current health care environment. The one constant for physicians and health care entities remains relentless change. With increasing cost pressures, complex regulatory frameworks, and shifting health care delivery and payment paradigms, physicians, medical groups, hospitals, and other health care facilities face ever more hurdles to their ability to thrive and prosper. CAP believes these challenges are surmountable with the proper support and resources.

In addition to providing industry-leading medical professional liability protection, CAP supplies its members with the education, information, and resources to ensure their success in the "new normal" of health care.

CAP members receive risk management, practice management, and tailored insurance agency services to support their independence and financial health. From ICD-10, HIPAA, Online Reputation, and payment and reimbursement action guides and webinars, to human resource manuals and education programs – CAP offers the value-added member support tools that promote the success of the medical practice.

Certainly, it is CAP's emphasis on the "big picture" of health care practice that differentiates the medical professional liability services brought through the Mutual Protection Trust and the CAPAssurance Risk Purchasing Group from the other choices available to physicians, medical groups, and health care facilities.

With a background overseeing the medical professional liability insurance, risk transfer, and risk management portfolio of a large integrated health system, I understand the big picture – and the impact it has on delivering quality outcomes in today's health care environment. I see the challenges and opportunities you face in practicing medicine, and I look forward to leading the innovation and excellence that CAP delivers in providing superior professional liability protection, risk management, and practice management services to you.

I am thrilled to have joined the organization as your new chief executive officer on February 1, 2015, and I am committed to ensuring CAP continues to identify, achieve, and sustain viable and creative opportunities to spearhead the success of the physicians and health care entities we are privileged to serve and support.

Sarah E. Pacini, JD
Chief Executive Officer

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Cooperative of American Physicians, Inc.

CAP 2014 Financial Reports

COOPERATIVE OF AMERICAN PHYSICIANS, INC. (CAP) AND SUBSIDIARIES AND
MUTUAL PROTECTION TRUST (MPT)

Report to the Membership

BY THE CAP AND MPT AUDIT COMMITTEE

The consolidated financial statements of CAP, the financial statements of MPT, and related financial information included in this annual report, have been prepared by CAP and MPT, whose management is responsible for its integrity. These financial statements, which necessarily reflect estimates and judgments have been prepared in conformity with U.S. generally accepted accounting principles.

The financial statements as of and for the years ended December 31, 2014 and 2013 have been audited by Ernst & Young LLP, independent auditors, as set forth in their reports appearing on pages 9 and 29.

CAP and MPT maintain a system of internal controls to provide reasonable assurance that assets are safeguarded and transactions are properly executed and recorded.

The Audit Committee, which consists solely of members who are not employees of the Company, meets periodically with management and the independent auditors to review the scope of their activities and to discuss internal controls and financial reporting matters. The independent auditors have full and free access to the Audit Committee and meet with the Committee both with and without the presence of Company management.

This report will be filed with the Department of Corporations with a statement from the Board of Trustees that this report was prepared from the official books and records of CAP and MPT.

Glenn Weissman MD

Glenn Weissman, MD
Chair
CAP and MPT Audit Committee
March 19, 2015

Report of Independent Auditors

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

BOARD OF DIRECTORS
COOPERATIVE OF AMERICAN PHYSICIANS, INC.

We have audited the accompanying consolidated financial statements of the Cooperative of American Physicians, Inc. and Subsidiaries, which comprise the consolidated balance sheets as of December 31, 2014 and 2013, and the related consolidated statements of comprehensive income, changes in members' equity and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in conformity with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of material misstatement, whether due to fraud or error.

Auditor's Responsibility

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. 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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Cooperative of American Physicians, Inc. and Subsidiaries at December 31, 2014 and 2013, and the consolidated results of their operations and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP

Los Angeles, California
March 19, 2015

Consolidated Balance Sheets

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

	December 31	
	2014	2013
ASSETS		
Cash and cash equivalents	$ 6,260,000	$ 6,326,000
Restricted cash	1,820,000	930,000
Short-term investments	350,000	—
Fixed income securities, at fair value	31,894,000	29,468,000
Equity securities, at fair value	4,707,000	4,029,000
Income taxes receivable	—	289,000
Premiums receivable	4,064,000	2,721,000
Funds held by reinsured	1,515,000	538,000
Receivable from affiliated entities	1,512,000	1,709,000
Receivable for claims and risk management services	478,000	327,000
Other assets	1,121,000	1,387,000
	$53,721,000	$47,724,000
LIABILITIES AND MEMBERS' EQUITY		
Liabilities:		
Reserves for losses and loss adjustment expenses	$13,799,000	$12,988,000
Payable to affiliated entities	—	295,000
Dues received in advance	1,045,000	945,000
Deferred tax liabilities, net	114,000	25,000
Unearned premiums	753,000	667,000
Income taxes payable	619,000	—
Unearned claims and risk management services	471,000	126,000
Premiums payable	5,880,000	3,651,000
Accounts payable and other liabilities	3,937,000	3,672,000
	26,618,000	22,369,000
Contingencies and commitments (see Notes 5 and 9)		
Total Members' Equity:		
Members' equity	26,369,000	24,864,000
Accumulated other comprehensive income	734,000	491,000
	27,103,000	25,355,000
	$53,721,000	$47,724,000

The accompanying notes are an integral part of these financial statements.

Consolidated Statements of Comprehensive Income

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

	Years Ended December 31 2014	2013
Revenues		
Member and participant dues	$ 3,249,000	$ 3,192,000
Claims and risk management service revenues	41,925,000	42,923,000
Premiums earned	5,699,000	5,343,000
Commissions earned	1,593,000	1,434,000
Investment income, net	950,000	841,000
Ancillary service revenues	2,000	14,000
Administrative fee	64,000	60,000
Total Revenues	53,482,000	53,807,000
Expenses		
Salaries and related expenses	29,037,000	28,328,000
Other operating costs	19,126,000	19,788,000
Losses and loss adjustment expenses	2,901,000	4,659,000
Total Expenses	51,064,000	52,775,000
Income Before Income Taxes	2,418,000	1,032,000
Income Tax Expense	913,000	330,000
Net Income	1,505,000	702,000
Other Comprehensive Income (Loss), Net		
Net unrealized gains (losses) on securities available-for-sale, net of taxes	243,000	(361,000)
Comprehensive Income	$ 1,748,000	$ 341,000

The accompanying notes are an integral part of these financial statements.

Consolidated Statements of Changes in Members' Equity

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

	Members' Equity	Accumulated Other Comprehensive Income	Total Members' Equity
Balance at January 1, 2013	$24,162,000	$ 852,000	$25,014,000
Net Income	702,000	—	702,000
Other Comprehensive Loss			
(net of deferred income taxes of $186,000)	—	(361,000)	(361,000)
Balance at December 31, 2013	24,864,000	491,000	25,355,000
Net Income	1,505,000	—	1,505,000
Other Comprehensive Income			
(net of deferred income taxes of $125,000)	—	243,000	243,000
Balance at December 31, 2014	$26,369,000	$ 734,000	$27,103,000

The accompanying notes are an integral part of these financial statements.

Consolidated Statements of Cash Flows

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

	Years Ended December 31	
	2014	2013
Operating Activities		
Net income	$ 1,505,000	$ 702,000
Adjustments to reconcile net income to net cash provided by operating activities:		
Net amortization on fixed income securities	389,000	310,000
Net realized investment gains	(91,000)	(67,000)
Deferred income taxes	(36,000)	19,000
Changes in operating assets and liabilities:		
Restricted cash	(890,000)	(65,000)
Income taxes	908,000	(37,000)
Premiums receivable	(1,343,000)	60,000
Funds held by reinsured	(977,000)	(538,000)
Receivable from affiliated entities	197,000	(1,380,000)
Receivable for claims and risk management services	(151,000)	(327,000)
Other assets	266,000	(606,000)
Reserves for losses and loss adjustment expenses	811,000	2,475,000
Payable to affiliated entities	(295,000)	48,000
Dues received in advance	100,000	6,000
Unearned premiums	86,000	634,000
Unearned claims and risk management services	345,000	126,000
Premiums payable	2,229,000	5,000
Accounts payable and other liabilities	265,000	986,000
Net Cash Provided by Operating Activities	3,318,000	2,351,000
Investing Activities		
Purchases of fixed income and equity securities	(9,539,000)	(10,731,000)
Proceeds from sale or maturity of fixed income and equity securities	6,505,000	7,144,000
Purchase of short-term investment	(350,000)	—
Net Cash Used in Investing Activities	(3,384,000)	(3,587,000)
Net Change in Cash and Cash Equivalents	(66,000)	(1,236,000)
Cash and Cash Equivalents at Beginning of Year	6,326,000	7,562,000
Cash and Cash Equivalents at End of Year	$ 6,260,000	$ 6,326,000

The accompanying notes are an integral part of these financial statements.

Notes to Consolidated Financial Statements

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

Note 1: Organization

The Cooperative of American Physicians, Inc. (CAP) was incorporated in 1975 for the purpose of providing various services relating to the general and professional welfare of its membership, which is comprised exclusively of physicians and surgeons licensed to practice in California. On January 1, 2013, physician members of the Hawaii Association of Physicians for Indemnification (HAPI), a group of physicians and surgeons licensed to practice in Hawaii, became non-voting participants in CAP and receive certain benefits from CAP pursuant to an agreement. Additional non-voting participants have been added through the CAPAssurance Program, which is more fully described below.

CAP formed Mutual Protection Trust (MPT) in 1977 in accordance with California legislation enacted in 1976 permitting the formation of such interindemnity arrangements to provide medical professional liability protection for physicians. MPT is a separate legal entity governed by its Board of Trustees. Physicians covered by MPT are required to be members of CAP.

In April 2013, CAP formed CAPAssurance, A Risk Purchasing Group ("CAPAssurance"), a non-profit, unincorporated association domiciled in California that was established to allow large physician groups, hospitals, and facilities access to a medical professional liability insurance product. As a risk purchasing group, CAPAssurance is not a subsidiary of CAP and is comprised of physician groups and medical facilities that purchase their liability insurance through CAPAssurance. Insurance under the program is provided by a national medical professional liability insurance company, with certain risk management, claims administration, and other policy services provided by CAP under agreements that became effective in March 2013 for hospitals and July 2013 for large physician groups (collectively the "CAPAssurance Program") (see Note 2). In 2014, CAP began collecting premiums on new or renewal business produced through the CAPAssurance Program. Physicians and medical facilities that are insured through the CAPAssurance Program can access various benefits of CAP as non-voting participants. CAP, with the CAPAssurance Program, can now better serve larger medical groups with professional liability coverage either through an insurance product or through the interindemnity arrangement provided by MPT.

In 2002, CAP formed the Cooperative of American Physicians Insurance Company, Inc. (CAPIC), a wholly owned subsidiary domiciled in the state of Hawaii under that state's captive insurance statutes. The primary purpose of CAPIC is to offer supplemental reinsurance and insurance coverage to its affiliate MPT and supplemental insurance coverage to CAP. In December 2011, CAPIC received approval from the state of Hawaii to be re-licensed as a Class 3 risk retention captive insurance company effective January 1, 2012, and the name was changed to Cooperative of American Physicians Insurance Company, Inc., a Risk Retention Group as it relates to operations after December 31, 2011. As a risk retention group, CAPIC, in addition to its current products, offered medical professional liability insurance coverage to targeted larger physician medical groups. In the second quarter of 2013, CAP determined that larger physician medical groups could be better served through an insurance product provided by a larger national medical professional liability insurance company and managed by CAP. This made it unnecessary for CAPIC to operate as a risk retention group and so on May 23, 2013, CAPIC was re-licensed to a Class 4 sponsored captive insurance company. Under its new license, CAPIC entered into a pro-rata reinsurance agreement with the insurance company providing insurance coverage for the CAPAssurance Program and thereby participates in the underwriting results. Under the reinsurance agreement, CAPIC participates on a pro-rata basis at rates that vary based on the type of insured covered by the policies. The policy acquisition costs and claims administration expenses of the insurance company on these policies are also reimbursed by CAPIC on the same pro-rata basis per the terms of the reinsurance agreement. CAPIC amortizes these expenses over the related policy term. These expenses include certain claims administration and other policy services provided by CAP to the insurance company under the CAPAssurance Program. CAPIC is consolidated in the operations of CAP.

In 2006, CAP formed the Cooperative of American Physicians Insurance Services, Inc. (CAPIS), a wholly owned subsidiary domiciled in Delaware, and licensed as a broker-dealer by the Financial Industry Regulatory Authority. CAPIS provides CAP and its affiliate, MPT, with an alternative distribution channel for both the products offered by CAP and the medical professional liability protection services of MPT. Operations commenced in 2007 and are consolidated with the operations of CAP. More recently, it was determined that this alternative distribution channel was no longer necessary, and the company was dissolved on February 20, 2015.

In 2007, CAP formed the CAP Physicians Insurance Agency, Inc. (CAP Agency), a wholly owned subsidiary of CAP domiciled in California, which provides access to business and other coverages for CAP members and participants. In addition,

Notes to Consolidated Financial Statements

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

Note 1: Organization (continued)

under an agreement that became effective January 1, 2013, CAP Agency performs the billing and collection obligations under CAP's group disability and life program. The operations of CAP Agency are consolidated with the operations of CAP.

In 2003, CAP entered into a patent licensing and consulting agreement, which authorizes the use of CAP's claims-paid insurance policy form and intellectual knowledge to a third party. Under this agreement, CAP receives royalty payments based on a percentage of premiums earned.

Effective January 1, 2010, CAP and MPT entered into an administrative and management services agreement whereby CAP provides membership, claim, risk management, financial, and other administrative and management services to MPT. CAP receives monthly fees from MPT for these services. Effective January 1, 2013, MPT and CAPIC entered into a services agreement whereby CAPIC provides claims legal defense services to MPT physicians. MPT pays CAPIC monthly fees for these services that are based on actual costs incurred (see Note 7).

CAP sponsors the CAP State Political Action Committee and the CAP Federal Political Action Committee, which solicit and accept donations from members of CAP and make contributions in support of candidates for public office. CAP also maintains the Cooperative of American Physicians State Independent Expenditure Committee and the Cooperative of American Physicians Federal Independent Expenditure Committee, which participate in independent expenditure candidate campaigns. These committees are subject to laws and regulations of the state of California and the federal government.

Note 2: Summary of Significant Accounting Policies

BASIS OF FINANCIAL STATEMENT PRESENTATION

The consolidated financial statements of CAP and its wholly owned subsidiaries, CAPIC, CAPIS and CAP Agency (collectively, the Company), have been prepared in accordance with U.S. generally accepted accounting principles (GAAP). This basis of accounting requires the use of management estimates that affect the reported amounts of assets and liabilities and disclosure of assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Actual results may differ from those estimates. Intercompany transactions and balances have been eliminated in consolidation.

The expenses of CAP are incurred on behalf of its members and participants, MPT, and the political action committees. For certain membership benefit expenses, CAP is reimbursed by MPT. Ancillary service revenues include royalties under certain license agreements. Membership dues are $250 per member. For participants, the dues vary based on the benefits selected by such participants.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents include cash and short-term highly liquid investments with maturities of 90 days or less at acquisition and are principally stated at amortized cost.

RESTRICTED CASH

Restricted cash represents funds held in Premium Trust accounts for CAP Agency and CAPAssurance premiums and premium related receipts. Disbursements are made from these accounts to pay premiums to insurance companies, agent commissions to CAP Agency, dues and claims and risk management service fees to CAP, and excise surplus lines taxes to taxing authorities.

SHORT-TERM INVESTMENTS

Short-term investments include investments with remaining maturities of one year or less at the time of acquisition and are principally stated at amortized cost.

INVESTMENTS

Investments are classified as available-for-sale and are carried at fair value. Transfers between fair value hierarchy levels 1, 2, or 3 are recognized on the actual date of the circumstances that caused the transfer to occur. Unrealized gains and losses are accounted for, net of tax, as a component of accumulated other comprehensive income in members' equity. Realized gains

Notes to Consolidated Financial Statements

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

Note 2: Summary of Significant Accounting Policies (continued)

and losses from sales transactions occurring during the year are recognized in operations using the specific identification method. Unrealized gains and losses are determined using the specific identification method. Investment income is recorded as earned. Premiums and discounts on investment securities are primarily amortized using the interest method over the estimated lives of the investments. Adjustments for other-than-temporary market declines are recorded when determination of loss is probable and is reported as a write-down of cost or amortized cost to fair value.

CONCENTRATION OF CREDIT RISK

Financial instruments which potentially subject the Company to concentrations of credit risk consist principally of temporary cash investments and fixed income securities. The Company places its temporary cash investments with high credit quality financial institutions. Concentrations of credit risk with respect to fixed income securities are limited due to the large number of such investments and their distribution across many different sectors. The Company's investments in federal agency securities are considered to have an implicit guarantee as to principal from the U.S. government and are considered to have minimal credit risk.

FAIR VALUE OF FINANCIAL INSTRUMENTS

Estimated fair value amounts, defined as the price that would be received to sell an asset or paid to transfer a liability (i.e., the "exit price") in an orderly transaction between market participants at the measurement date, have been determined using available market information and other appropriate valuation methodologies. However, considerable judgment is required in developing the estimates of fair value where quoted market prices are not available. Accordingly, these estimates are not necessarily indicative of the amounts that could be realized in a current market exchange. The use of different market assumptions or estimating methodologies may have an effect on the estimated fair value amounts.

The following methods and assumptions were used by the Company in estimating the fair value disclosures for financial instruments in the accompanying consolidated financial statements and in these notes:

Cash and cash equivalents, restricted cash, short-term investments, premiums receivable, funds held by reinsured, receivable from affiliated entities, receivable for claims and risk management services, payable to affiliated entities, dues received in advance, premiums payable, accounts payable and other liabilities. The carrying amounts for these financial instruments as reported in the accompanying consolidated balance sheets approximate their estimated fair values.

Investments. The Company determines the fair value of its financial instruments based on the fair value hierarchy established in Accounting Standards Codification (ASC) 820, which requires an entity to disclose the use of observable inputs and minimize the use of unobservable inputs for measuring fair value. Estimates of fair value measurements for these securities are estimated using relevant inputs, including available relevant market information, benchmark curves, benchmarking of like securities, sector groupings, and matrix pricing. Additionally, an Option Adjusted Spread model is used to develop prepayment and interest rate scenarios. Industry standard models are used to analyze and value securities with embedded options or prepayment sensitivities.

Each asset class is evaluated based on relevant market information, relevant credit information, perceived market movements and sector news. The market inputs utilized in the pricing evaluation include benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, reference data, and industry and economic events. The extent of the use of each market input depends on the asset class and the market conditions. Depending on the security, the priority of the use of inputs may change or some market inputs may not be relevant. For some securities, additional inputs may be necessary.

This method of valuation will only produce an estimate of fair value if there is objectively verifiable information to produce a valuation. If objectively verifiable information is not available, the Company would be required to produce an estimate of fair value using some of the same methodologies, but would have to make assumptions for market based inputs that are unavailable due to market conditions.

Because the fair value estimates of most fixed income securities are determined by evaluations that are based on observable market information rather than market quotes, most estimates of fair value for fixed income securities are based on estimates using objectively verifiable information and are included in the amount disclosed in Level 2 of the hierarchy. The values of

Notes to Consolidated Financial Statements

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

Note 2: Summary of Significant Accounting Policies (continued)

states and municipalities, U.S. treasuries, corporate bonds, residential mortgage-backed securities, commercial mortgage-backed securities and asset-backed securities are based on the observable market information and as such, is included in the Level 2 hierarchy. Level 1 is limited to unadjusted quoted prices in active markets for identical instruments and includes all equity securities.

The following table presents investments on the accompanying consolidated balance sheet that are stated at fair value and the fair value measurements used as of December 31, 2014 and 2013 (see Note 3):

	Total	Level 1	Level 2
DECEMBER 31, 2014			
Fixed income securities			
States and municipalities	**$14,441,000**	**$ —**	**$14,441,000**
US Treasuries	**350,000**	**—**	**350,000**
Corporate bonds	**2,821,000**	**—**	**2,821,000**
Residential mortgage-backed securities	**8,425,000**	**—**	**8,425,000**
Commercial mortgage-backed securities	**3,364,000**	**—**	**3,364,000**
Asset-backed securities	**2,843,000**	**—**	**2,843,000**
Total fixed income securities	**32,244,000**	**—**	**32,244,000**
Equity securities: mutual funds	**4,707,000**	**4,707,000**	**—**
Total fixed income and equity securities	**$36,951,000**	**$4,707,000**	**$32,244,000**
DECEMBER 31, 2013			
Fixed income securities			
States and municipalities	$10,468,000	$ —	$10,468,000
Corporate bonds	6,362,000	—	6,362,000
Residential mortgage-backed securities	6,862,000	—	6,862,000
Commercial mortgage-backed securities	3,720,000	—	3,720,000
Asset-backed securities	2,056,000	—	2,056,000
Total fixed income securities	29,468,000	—	29,468,000
Equity securities: mutual funds	4,029,000	4,029,000	—
Total fixed income and equity securities	$33,497,000	$4,029,000	$29,468,000

There were no securities at December 31, 2014 or 2013, whose fair value measurements were based on Level 3: Unobservable inputs.

There were no significant transfers in and out of Level 1 and Level 2 fair value measurements during the years ended December 31, 2014 or 2013.

REVENUES

Dues: Members' dues are recognized on January 1 of each year and earned ratably over the year. For participants, dues are recognized on a pro rata basis over the related agreement or insurance policy term.

Claims and risk management service revenues: These services are comprised primarily of services provided to MPT and to an insurance company pursuant to the CAPAssurance Program (see Notes 1 and 7). Claims and risk management services to MPT are recognized as earned, and are derived under agreements to provide certain administrative, claims legal defense, and management services. For all services except claims legal defense, revenues are determined based on actual expenses incurred plus a margin. The calculation of expense to MPT is based on the ratio of assessments, dues and revenues of MPT to total assessments, dues and revenues of the Company and MPT combined. The Company excludes revenues from this administrative and management services agreement in calculating this ratio. The claims legal defense service revenues are determined based on actual costs incurred and represent services provided by CAPIC to MPT physicians pursuant to an agreement effective January 1, 2013.

Notes to Consolidated Financial Statements

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

Note 2: Summary of Significant Accounting Policies (continued)

The claims and risk management services under the CAPAssurance Program are derived from agreements with an insurance company that became effective in the second and third quarters of 2013. These services consist of claims administration, risk management and certain insurance services in the areas of underwriting support, risk management, marketing, and other administrative services. The insurance company retains underwriting authority on all policies issued. Service fees are based on percentages of premiums on policies issued. If a policy is cancelled prior to its expiration date, the Company returns service fees to the insurance company based on the unearned premium of the cancelled policy. These service obligations are part of other agreements that together allow the Company to offer a medical professional liability insurance product to large physician medical groups, hospitals, and medical facilities. One of these other agreements is a pro-rata reinsurance agreement between CAPIC and the insurance company. This enables the Company to participate in the underwriting results on insurance policies issued by the insurance company through the CAPAssurance Program. Accordingly, the Company will not only generate claims and risk management service revenues on policies issued by the insurance company, but will also recognize premiums earned through the reinsurance agreement and dues revenue for any physician and medical facility participants who purchase benefits from CAP.

The Company recognizes the marketing services revenues at the inception of the policy period since these services are complete as of the inception of the policy. Underwriting support, risk management and other administration services under the CAPAssurance Program (“policy services”) are recognized over the related policy term. Policy services are provided during the policy term. Service fees are subject to return should the underlying policy be cancelled. For claims administration services, an estimated payout period of reported claims is used to recognize service fee revenue. This period is generally longer than the related policy term and is aligned with the Company’s obligation to provide claims administration services on reported claims until final resolution of the claim. The allocation of service fees between claims administration and policy services is based on the premium percentages for such services as stated in the underlying agreements. The Company determined these rates to be reasonable by comparing these percentages to the recent historical experience of the insurance company and found such rates comparable. The insurance company is a leading provider of medical professional liability insurance nationwide and is considered representative of what competitive policy services cost should approximate.

Premiums: Premiums are recognized on a pro rata basis over the policy term.

Reinsurance: CAPIC is involved in the assumption of reinsurance with a non-affiliated company. CAPIC participates on a pro-rata basis in the first $1.0 million of exposure on medical professional liability policies at rates that vary based on the type of insured covered by the policies. Assumed premiums written under this agreement were $1,224,000 and $878,000 for the years ended December 31, 2014 and 2013, respectively. Premiums earned under this agreement were $1,138,000 and $212,000 for the years ended December 31, 2014 and 2013, respectively. CAPIC is consolidated in the operations of CAP.

Commissions Earned: Commissions on premiums billed and commission adjustments, including policy cancellations and override commissions, are recorded when estimable or received. Supplemental commissions are received from insurance companies as additional incentive for achieving specified premium volume goals and/or the loss experience of the insurance placed by the Company. Supplemental commissions are recognized when the Company receives data from the insurance companies that allows the amounts to be reasonably estimated. Commission expense represents amounts the Company pays on business placed by insurance brokers and agents based on agreed-upon commission percentages between the Company and the insurance brokers and agents. Commission expense is recognized on the effective date of the related MPT coverage period. Commission income is reported gross of commission expense.

Royalties: Royalties are recognized as earned and is included in ancillary service revenues in the accompanying consolidated statements of comprehensive income.

RESERVES FOR LOSSES AND LOSS ADJUSTMENT EXPENSES

Reserves for losses and loss adjustment expenses under contracts of insurance and reinsurance written on a claims-made form is determined from reported losses and an amount, based on an actuarial evaluation which considers past experience, for development on such losses. Such liabilities are necessarily based on estimates and, while management believes that the amount is within a reasonable range of adequacy, the ultimate liability may be in excess of, or less than, the amount pro-

Notes to Consolidated Financial Statements

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

Note 2: Summary of Significant Accounting Policies (continued)

vided. Changes in estimates of the liabilities resulting from their periodic review and differences between estimates and ultimate payments are reflected in current operations.

PREMIUMS RECEIVABLE AND PREMIUMS PAYABLE

The Company records premiums receivable and payable under its agency billed and CAPAssurance business using the accrual basis. Under this method, new and renewal premiums on policies produced by CAP Agency on agency billed business or CAP on CAPAssurance Program business is recognized as a premium receivable from the physician, group or medical facility and a premium payable to the insurance company. Cash received from agency or CAP billings reduce the premiums receivable and cash payments to the insurance company reduce the premiums payable. For business where CAP Agency is not obligated to perform billing services, accounts are settled on a cash basis.

FUNDS HELD BY REINSURED

In 2013, CAPIC entered into a pro-rata reinsurance agreement with an insurance company as part of the CAPAssurance Program (see Note 1). Under the terms of the agreement, premiums assumed, less specified policy acquisition costs and claims administration expenses, are held by the insurance company to secure incurred but unpaid obligations of CAPIC, such as incurred but unpaid claims and unearned premiums. Should the assumed premiums, net of expenses, be insufficient to secure these unpaid obligations, then additional funds will be paid to the insurance company to make up any shortfall. In December 2014, the Company funded $222,000 in additional funds to the insurance company. The amounts held by the insurance company are reported as funds held by reinsured.

RECEIVABLE FOR CLAIMS AND RISK MANAGEMENT SERVICES

The receivable for claims and risk management services represents uncollected claims, risk management and insurance services fees on insurance policies issued under the CAPAssurance Program (see Note 1). A receivable is established at the inception date of the issued policies and CAP collects these service fees based on the premium payment terms of the issued policies.

UNEARNED CLAIMS AND RISK MANAGEMENT SERVICES

Risk management and insurance services provided by CAP under the CAPAssurance Program are recognized over the underlying insurance policy periods. Claims administration services provided by CAP under this program are recognized over an estimated payout period of reported claims. Unearned claims and risk management services represents the amount of these service fees that relate to either the unexpired policy periods or the unexpired claim payout period as of the balance sheet date (See Note 1).

CAPITAL REQUIREMENTS

CAPIC is required by the state of Hawaii to maintain capital and surplus in an amount, and in certain investments, deemed appropriate by the Hawaii State Insurance Commissioner. At December 31, 2014 and 2013, CAPIC exceeded the minimum requirement of $1,000,000. Hawaii law provides that no dividends may be paid to shareholders without prior approval of the Insurance Commissioner. No dividends were declared or paid for the years ended December 31, 2014 and 2013.

INCOME TAXES

CAP and its wholly owned subsidiaries file a consolidated federal income tax return. CAP allocates income taxes to these subsidiaries based on the separate return method. Income taxes are provided for current taxes payable or refundable and the temporary differences arising from future tax consequences of events that have been recognized in the Company's financial statements or income tax returns. The effects of income taxes are measured based on enacted tax laws and rates. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Valuation allowances are recognized if, based on the weight of available evidence, it is more likely than not that some portion of the deferred tax assets will not be realized. Interest and penalties on tax amounts paid or received are included in investment income, net and other operating costs, respectively.

Notes to Consolidated Financial Statements

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

Note 2: Summary of Significant Accounting Policies (continued)

COMPREHENSIVE INCOME

Comprehensive income consists of net income and other comprehensive income (loss). Other comprehensive income (loss) refers to revenues, expenses, gains and losses that are not included in net income less reclassification adjustments for gains or losses, but rather are recorded in comprehensive income. For the years ended December 31, 2014 and 2013, other comprehensive income (loss) consists solely of net unrealized gains and losses, net of tax, on securities classified as available-for-sale. Reclassification adjustments related to available-for-sale securities for the years ended December 31, 2014 and 2013 were as follows:

	2014	2013
Net realized investment gains (losses) included in the calculation of investment income, net	**$ 7,000**	$(53,000)
Tax effect (at 34%)	**(2,000)**	18,000
Net realized investment gains (losses) reclassified from other comprehensive income	**$ 5,000**	$(35,000)

NEW ACCOUNTING STANDARDS

In February 2013, the FASB issued an update to clarify the scope and applicability of a particular disclosure to nonpublic entities that resulted from the issuance of Accounting Standards Update No. 2011-04, *Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs.* This update clarifies that nonpublic entities that have total assets of $100 million or more or that have one or more derivatives are not exempted from the requirement to disclose "the level of the fair value hierarchy within which the fair value measurements are categorized in their entirety (Level 1, 2, or 3)" for items that are not measured at fair value in the statement of financial position but for which fair value is disclosed. The adoption of this update did not have a material impact on the Company's consolidated financial statements.

In February 2013, the FASB issued an update to improve the reporting of reclassifications out of accumulated other comprehensive income. The amendments in this update require an entity to report the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in net income if the amounts being reclassified are required under U.S. GAAP to be reclassified in their entirety to net income in the same reporting period. An entity is required to cross-reference other disclosures required under U.S. GAAP that provide additional detail about those amounts. The amendments do not change the current requirements for reporting net income or other comprehensive income in financial statements. This update is effective prospectively for reporting periods beginning after December 15, 2013, and may be adopted earlier. The Company adopted this guidance effective January 1, 2014. The adoption of this update did not have a material impact on the Company's consolidated financial statements.

In July 2013, the FASB issued an update regarding the financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. The objective of this update is to reduce diversity in practice by providing guidance on the presentation of unrecognized tax benefits in order to better reflect the manner in which an entity would settle at the reporting date any additional income taxes that would result from the disallowance of a tax position when net operating loss carryforwards, similar tax losses, or tax credit carryforwards exist. This update will be effective for reporting periods beginning after December 15, 2014, and may be adopted earlier. The adoption of this update is not expected to have a material impact on the Company's consolidated financial statements.

RECLASSIFICATIONS

Certain reclassifications have been made to the prior year financial statements to conform to the current year presentation.

SUBSEQUENT EVENTS

The Company has completed an evaluation of all subsequent events through March 19, 2015, which is the date the financial statements were available for issuance, and has concluded that no subsequent event occurred which would require recognition or disclosure.

Notes to Consolidated Financial Statements

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

Note 3: Investments

Investment securities, exclusive of cash and cash equivalents are comprised of the following:

	Amortized Cost/Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
DECEMBER 31, 2014				
Fixed income securities				
States and municipalities	$13,935,000	$ 507,000	$ (1,000)	$14,441,000
US Treasuries	350,000	—	—	350,000
Corporate bonds	2,791,000	31,000	(1,000)	2,821,000
Residential mortgage-backed securities	8,334,000	145,000	(54,000)	8,425,000
Commercial mortgage-backed securities	3,350,000	21,000	(7,000)	3,364,000
Asset-backed securities	2,838,000	6,000	(1,000)	2,843,000
Total fixed income securities	31,598,000	710,000	(64,000)	32,244,000
Equity securities: mutual funds	4,242,000	568,000	(103,000)	4,707,000
Total fixed income and equity securities	$35,840,000	$1,278,000	$(167,000)	$36,951,000
DECEMBER 31, 2013				
Fixed income securities				
States and municipalities	$10,141,000	$ 347,000	$ (20,000)	$10,468,000
Corporate bonds	6,302,000	111,000	(51,000)	6,362,000
Residential mortgage-backed securities	6,932,000	137,000	(207,000)	6,862,000
Commercial mortgage-backed securities	3,706,000	32,000	(18,000)	3,720,000
Asset-backed securities	2,031,000	26,000	(1,000)	2,056,000
Total fixed income securities	29,112,000	653,000	(297,000)	29,468,000
Equity securities: mutual funds	3,642,000	387,000	—	4,029,000
Total fixed income and equity securities	$32,754,000	$1,040,000	$(297,000)	$33,497,000

The amortized cost and fair value of fixed income securities available-for-sale as of December 31, 2014, by contractual repayment date of principal, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Fair Value
Due in one year or less	$ 1,117,000	$ 1,125,000
Due after one year through five years	6,715,000	6,851,000
Due after five years through 10 years	6,169,000	6,456,000
Due after 10 years	3,075,000	3,180,000
	17,076,000	17,612,000
Mortgage-backed and asset-backed securities	14,522,000	14,632,000
	$31,598,000	$32,244,000

For the years ended December 31, 2014 and 2013, proceeds from sales of investments were $4,341,000 and $4,017,000, respectively.

Notes to Consolidated Financial Statements

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

Note 3: Investments (continued)

The following table shows the gross unrealized losses and fair value aggregated by investment category and length of time those securities have been in a continuous unrealized loss position:

	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
DECEMBER 31, 2014						
Fixed income securities						
States and municipalities	$ 730,000	$ (1,000)	$ —	$ —	$ 730,000	$ (1,000)
Corporate bonds	482,000	(1,000)	—	—	482,000	(1,000)
Residential mortgage-backed securities	1,290,000	(1,000)	2,545,000	(53,000)	3,835,000	(54,000)
Commercial mortgage-backed securities	429,000	(1,000)	501,000	(6,000)	930,000	(7,000)
Asset-backed securities	832,000	(1,000)	—	—	832,000	(1,000)
Total fixed income securities	3,763,000	(5,000)	3,046,000	(59,000)	6,809,000	(64,000)
Equity securities: mutual funds	2,898,000	(103,000)	—	—	2,898,000	(103,000)
Total fixed income and equity securities	$ 6,661,000	$(108,000)	$3,046,000	$(59,000)	$ 9,707,000	$(167,000)
DECEMBER 31, 2013						
Fixed income securities						
States and municipalities	$ 1,607,000	$ (20,000)	$ —	$ —	$ 1,607,000	$ (20,000)
Corporate bonds	2,221,000	(51,000)	—	—	2,221,000	(51,000)
Residential mortgage-backed securities	3,303,000	(207,000)	—	—	3,303,000	(207,000)
Commercial mortgage-backed securities	2,913,000	(18,000)	—	—	2,913,000	(18,000)
Asset-backed securities	249,000	(1,000)	—	—	249,000	(1,000)
Total fixed income securities	10,293,000	(297,000)	—	—	10,293,000	(297,000)
Equity securities: mutual funds	—	—	—	—	—	—
Total fixed income and equity securities	$10,293,000	$(297,000)	$ —	$ —	$10,293,000	$(297,000)

The Company reviews at least quarterly its investment portfolio for securities that may have an other-than-temporary impairment. In its impairment analysis, the Company takes into consideration numerous criteria, including the duration and extent of any decline in estimated fair value, industry factors, downgrades by rating agencies, liquidity and fundamental factors of the issuers, as well as its ability and intent to retain its investment in the issuer to allow for any anticipated recovery in market value or maturity. If the decline is determined to be other than temporary, the investment's amortized cost is written down to estimated fair value with the unrealized loss recognized in earnings as a realized loss on investments. As of December 31, 2014 and 2013, none of the Company's investments whose estimated fair values were less than amortized costs were considered to be other-than-temporarily impaired given the severity and duration of the impairment and the credit quality of the issuers. Regarding equity securities, the Company has evaluated the near-term prospects of the securities in relation to the severity and duration of the impairment and intends to hold these securities until a recovery of fair value has occurred. The Company does not intend to sell its investments whose fair values are less than amortized cost and it is not more likely than not that the Company will be required to sell the investments before recovery of the amortized cost bases, which may be maturity.

Notes to Consolidated Financial Statements

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

Note 3: Investments (continued)

Investment income, net is summarized as follows:

	Years Ended December 31 2014	2013
Interest income	$1,282,000	$1,116,000
Gains on sales of investments	99,000	113,000
Losses on sales of investments	(8,000)	(46,000)
Investment management fees and expenses	(34,000)	(32,000)
Net amortization of premium on fixed income securities	(389,000)	(310,000)
Investment income, net	$ 950,000	$ 841,000

Note 4: Reserves for Losses and Loss Adjustment Expenses

The activity in the reserves for losses and loss adjustment expenses is summarized as follows:

	December 31 2014	2013
Reserves — beginning of year	$12,988,000	$10,513,000
Incurred related to:		
Current year	6,237,000	5,570,000
Prior years	(3,336,000)	(911,000)
Total incurred	2,901,000	4,659,000
Paid related to:		
Current year	(606,000)	(320,000)
Prior years	(1,484,000)	(1,864,000)
Total paid	(2,090,000)	(2,184,000)
Reserves — end of year	$13,799,000	$12,988,000

For the year ended December 31, 2014, the provision for losses and loss adjustment expenses in prior years decreased $3,336,000, comprised primarily of favorable development on the 2010 through 2013 claims-made years totaling $3,225,000, and favorable development on the 2007 and 2008 claims-made years totaling $113,000. For the year ended December 31, 2013, the provision for losses and loss adjustment expenses in prior years decreased $911,000, comprised of favorable development totaling $1,253,000, mainly on the 2006, 2007, 2009, 2011 and 2012 claims-made years, offset by $342,000 in adverse development on the 2008 and 2010 claims-made years. For the year ended December 31, 2014, the favorable development was due to both lower than expected claim frequency and lower than expected claim severity. For the year ended December 31, 2013, the favorable development was due mainly to lower than anticipated severity of incurred claims, and the adverse development was due mainly to higher than anticipated severity of incurred claims.

Note 5: Contingencies

The Company is subject to legal proceedings arising from the normal conduct of its business. In the opinion of management, any ultimate liability that may arise from these proceedings will not have a material effect on the Company's financial position.

Notes to Consolidated Financial Statements

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

Note 6: Income Taxes

The components of the provision for income taxes are as follows:

	Years Ended December 31	
	2014	2013
Current	$949,000	$311,000
Deferred	(36,000)	19,000
	$913,000	$330,000

A reconciliation of income tax expense computed at the federal statutory tax rate to total income tax expense is summarized as follows:

	Years Ended December 31	
	2014	2013
Federal income tax expense at 34%	$822,000	$ 351,000
Increase (decrease) in taxes resulting from:		
State income tax expense (net of federal benefit)	28,000	30,000
Employee benefit plan	24,000	22,000
Tax effect of PAC Committee's reimbursement for taxes	90,000	78,000
Tax-exempt investment income	(81,000)	(129,000)
Meals and entertainment exclusion	23,000	27,000
Other	7,000	(49,000)
Total federal income tax expense	$913,000	$ 330,000

The significant components of deferred income tax assets and liabilities are as follows:

	December 31	
	2014	2013
Deferred tax assets:		
Discounting of reserves for losses and loss adjustment expenses	$ 434,000	$ 462,000
Other-than-temporary impairments of other investments	17,000	17,000
Capital loss carryover	18,000	18,000
Employee benefit obligations	214,000	125,000
State taxes	—	5,000
Unearned premiums	55,000	48,000
Deferred commissions	13,000	14,000
Deferred tax assets	751,000	689,000
Deferred tax liabilities:		
Unrealized gain on investments	(378,000)	(253,000)
State tax on unremitted earnings of subsidiaries	(199,000)	(182,000)
Accretion of bond discount	(181,000)	(181,000)
Deferred acquisition costs	(91,000)	(88,000)
State taxes	(4,000)	—
Other items	(12,000)	(10,000)
Deferred tax liabilities	(865,000)	(714,000)
Deferred tax liability, net	$(114,000)	$ (25,000)

Notes to Consolidated Financial Statements

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

Note 6: Income Taxes (continued)

The Company has not established a valuation allowance against deferred tax assets as it has been determined that it is more likely than not that the assets will be realized.

Income taxes paid for the years ended December 31, 2014 and 2013, were $40,000 and $348,000, respectively. There were no penalties on tax amounts paid in either years ended December 31, 2014 or 2013.

As of December 31, 2014 and 2013, the Company had no net operating loss carryforwards.

The Company's income tax returns are subject to audit by the Internal Revenue Service and state tax authorities. Significant disputes may arise with these tax authorities involving issues of the timing and amount of deductions and allocations of income among various tax jurisdictions because of differing interpretations of tax laws and regulations. The Company periodically evaluates its exposures associated with tax filing positions.

As of December 31, 2014 and 2013, the Company had no uncertain tax positions.

Tax years 2012 and 2013 and tax years 2010 through 2013 are subject to examination by the federal and California taxing authorities, respectively. An examination that covered the 2009 through 2011 tax years by federal authorities concluded in February 2013. The result of this examination on net income was a decrease of $116,000 for additional federal tax and $27,000 in accrued interest.

Note 7: Related Party Transactions

CAP and MPT operate under an administrative and management services agreement whereby CAP provides membership, claims, risk management, financial, and other administrative and management services to MPT. Under the agreement, CAP receives monthly fees from MPT for these services that are based on actual expenses incurred by CAP plus a margin. Total revenues of $24,982,000 and $26,526,000 for the years ended December 31, 2014 and 2013, respectively, recognized from MPT for administrative and management services under the agreement are included in claims and risk management service revenues on the consolidated statements of comprehensive income. Expenses related to these agreements are included in salaries and related expenses totaling $16,999,000 and $16,972,000 for the years ended December 31, 2014 and 2013, respectively, and in other operating costs totaling $7,301,000 and $8,833,000 for the years ended December 31, 2014 and 2013, respectively.

Effective January 1, 2013, CAPIC and MPT entered into a services agreement whereby CAPIC provides claims legal defense services to MPT physicians. CAPIC receives from MPT monthly fees for these services that are based on actual costs incurred. Claims services fees recognized under this agreement were $16,672,000 and $16,266,000 for the years ended December 31, 2014 and 2013, respectively. Included in the receivable from affiliated entities is $1,786,000 and $1,672,000 due from MPT for these services as of December 31, 2014 and 2013, respectively.

In 2014 and 2013, CAPIC had reinsurance contracts with MPT. These contracts principally provide per claim excess of loss reinsurance coverage on a claims-made form for MPT for claims reported in 2014 and 2013. Aggregate stop-loss coverage was also provided to MPT in 2013 on a claims-made basis. The aggregate stop loss coverage provided for a limit of $11,000,000 in excess of an aggregate attachment of $115,200,000. These agreements can be terminated and commuted at the end of any calendar quarter prospectively by mutual agreement of CAPIC and MPT. Premiums paid by MPT under these agreements were $2,476,000 and $3,100,000 for the years ended December 31, 2014 and 2013, respectively. CAPIC also participates in a reinsurance contract that provides MPT coverage on a claims-made basis for multiple claims arising out of one common event. Premiums received by CAPIC under this contract were $228,000 and $243,000 for the years ended December 31, 2014 and 2013, respectively. For the years ended December 31, 2014 and 2013, total affiliate reinsurance premium income under all reinsurance contracts with MPT was $2,679,000 and $3,343,000, respectively.

Notes to Consolidated Financial Statements

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

Note 7: Related Party Transactions (continued)

CAP provides its members and participants defense coverage for medical board actions with a $25,000 limit and employer practice defense coverage with a $50,000 limit. CAPIC provides insurance coverage to CAP for these benefits. MPT reimburses CAP for a portion of the cost of this coverage. CAP paid CAPIC $2,640,000 and $2,599,000 for the years ended December 31, 2014 and 2013, respectively, for this coverage, of which MPT reimbursed CAP $1,877,000 and $1,785,000 for the same respective years.

The Company sponsors a 401(k) savings plan for its employees. Employees' contributions are matched by the Company at a level that is determined by the Board of Directors. The contribution expense for the 401(k) savings plan was $712,000 and $699,000 for the years ended December 31, 2014 and 2013, respectively. Eligible employees vest in the Company's contribution over a four-year vesting schedule. The Company also sponsors a supplemental employee retirement program (SERP) for certain employees. Participants vest, on average, over a 10 year period. All of the expense related to the SERP is incurred by MPT. SERP liabilities for the Company's participants have been assumed by MPT.

The Company maintains a non-qualified deferred compensation program (NDCP) for eligible employees and Board members. Under the plan, participants can defer compensation or Board fees based on an annual election. Amounts deferred are credited with notional investment earnings on a tax deferred basis until such amounts are distributed to participants. Amounts deferred are remitted to MPT who administers the NDCP on behalf of the Company.

Note 8: Employee Benefits

The Company maintains a post-retirement medical benefit plan for certain employees. Beginning at the age of 62, participants can use amounts held in a separate post-retirement account held on their behalf (by a third party trust) to fund eligible medical expenses. Amounts paid to the trust by the Company are not refundable and become the property of the trustee on behalf of participants. The trust invests funds received from the Company in universal life insurance policies covering participants, which includes a death benefit funded by the Company until the participant reaches the vesting age of 62. While the plan establishes targeted post-retirement benefit levels for participants, there is no obligation for the Company to fully fund these levels and the employees are only eligible to receive the benefits accumulated in their account. Amounts contributed to the trust by the Company were $101,000 for the years ended December 31, 2014 and 2013.

Notes to Consolidated Financial Statements

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

Note 9: Commitments

CAP and MPT occupy their home office and regional office facilities under operating leases which provide for adjustments to the lease payments based upon contractual commitments and inflationary factors. Both companies are lessees under these operating leases. Rent expense is apportioned between CAP and MPT based primarily on the number of employees. The total rent expense under these leases was $2,442,000 and $3,312,000 for the years ended December 31, 2014 and 2013, respectively. The total rent expense apportioned to CAP was $1,683,000 and $3,264,000 for the years ended December 31, 2014 and 2013, respectively. In January 2013, CAP and MPT extended the lease covering their home office facility for an additional ten years to a new expiration date of January 31, 2024. The future minimum rental commitments under these operating leases are as follows:

Years Ending December 31	Amount
2015	$ 2,032,000
2016	1,673,000
2017	1,696,000
2018	1,751,000
2019 and after	9,120,000
	$16,272,000

Mutual Protection Trust

MPT 2014 Financial Reports

Report of Independent Auditors

BOARD OF TRUSTEES
MUTUAL PROTECTION TRUST

We have audited the accompanying financial statements of the Mutual Protection Trust, which comprise the balance sheets as of December 31, 2014 and 2013, and the related statements of operations and net increase (decrease) in members' equity, changes in members' equity and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in conformity with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of material misstatement, whether due to fraud or error.

Auditor's Responsibility

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. 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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Mutual Protection Trust at December 31, 2014 and 2013, and the results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying supplementary information is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Ernst + Young LLP

Los Angeles, California
March 19, 2015

Balance Sheets

MUTUAL PROTECTION TRUST

	December 31 2014	December 31 2013
ASSETS		
Trust Fund Corpus, restricted:		
Fixed income securities, available-for-sale, at fair value	$143,020,000	$141,887,000
Cash and cash equivalents	1,124,000	1,775,000
Accrued interest receivable	955,000	964,000
Deferred tax liability	(1,210,000)	(776,000)
	143,889,000	143,850,000
Trust Fund Operating Accounts:		
Fixed income securities, available-for-sale, at fair value	65,462,000	63,011,000
Cash and cash equivalents	13,431,000	11,657,000
Assessments, dues and other coverages receivable	91,366,000	93,917,000
Fixed assets, net	2,768,000	3,454,000
Deferred tax asset, net	16,321,000	13,537,000
Income taxes receivable	—	125,000
Other assets	20,388,000	21,191,000
	209,736,000	206,892,000
	$353,625,000	$350,742,000
LIABILITIES		
Trust Fund Operating Accounts:		
Non-assessable former members' liability	$ 33,265,000	$ 37,664,000
Unpaid claims and expenses	13,452,000	16,254,000
Deferred assessments, dues and other coverages	110,010,000	110,323,000
Payable to affiliated entity	1,531,000	1,672,000
Income taxes payable	254,000	—
Other liabilities	29,546,000	24,560,000
	188,058,000	190,473,000
Contingencies and commitments (see Notes 5 and 9)		
MEMBERS' EQUITY		
Trust Fund Corpus, including accumulated other comprehensive income of $2,246,000 and $1,441,000 for 2014 and 2013, respectively	143,889,000	143,850,000
Trust Fund Operations	21,678,000	16,419,000
	165,567,000	160,269,000
	$353,625,000	$350,742,000

The accompanying notes are an integral part of these financial statements.

Statements of Operations and Net Increase (Decrease) in Members' Equity

MUTUAL PROTECTION TRUST

	Years Ended December 31 2014	2013
Assessments and Dues	$108,640,000	$114,144,000
Revenues		
Investment income:		
Interest income, net	5,655,000	5,854,000
Realized gains	153,000	130,000
Investment income, net	5,808,000	5,984,000
Other coverage fees	15,984,000	15,154,000
Total Assessments, Dues and Revenues	130,432,000	135,282,000
Expenses		
Claims costs:		
Indemnity expense	42,278,000	48,066,000
Defense and investigative services	35,184,000	35,064,000
Salaries and related expenses	6,165,000	6,533,000
Other operating costs	11,580,000	13,352,000
	95,207,000	103,015,000
General and administrative:		
Salaries and related expenses	15,771,000	12,336,000
Other operating costs	19,973,000	19,592,000
	35,744,000	31,928,000
Total Expenses	130,951,000	134,943,000
(Deficit) Excess of Assessments, Dues and Revenues Over Expenses Before Income Taxes	(519,000)	339,000
Income Tax Benefit (Expense)	5,154,000	(33,000)
Net Excess of Assessments, Dues and Revenues Over Expenses	4,635,000	306,000
Other Comprehensive Income (Loss), Net		
Net unrealized gains (losses) on securities available-for-sale, net of taxes	1,429,000	(5,116,000)
Net Increase (Decrease) in Members' Equity	$ 6,064,000	$ (4,810,000)

The accompanying notes are an integral part of these financial statements.

Statements of Changes in Members' Equity

MUTUAL PROTECTION TRUST

	Trust Fund Operations	Trust Fund Corpus: Active Members	Trust Fund Corpus: Accumulated Other Comprehensive Income	Trust Fund Corpus: Members' Deferred Contract Receivable	Trust Fund Corpus: Retired Members and Voluntary Terminations	Trust Fund Corpus: Total Trust Fund Corpus	Total Members' Equity
Balance at January 1, 2013	$17,719,000	$140,408,000	$ 4,951,000	$(14,048,000)	$13,933,000	$145,244,000	$162,963,000
Corpus Activity:							
Additions	—	5,934,000	—	(5,934,000)	—	—	—
Payments on deferred contracts receivable	—	—	—	7,481,000	—	7,481,000	7,481,000
Repayments	—	—	—	—	(4,752,000)	(4,752,000)	(4,752,000)
Contributions relinquished	—	(613,000)	—	—	—	(613,000)	(613,000)
Transfers of Corpus	—	(5,006,000)	—	—	5,006,000	—	—
Net Excess of Assessments, Dues and Revenues over Expenses	306,000	—	—	—	—	—	306,000
Other Comprehensive Loss (net of deferred income taxes of $2,754,000)	(1,606,000)	—	(3,510,000)	—	—	(3,510,000)	(5,116,000)
Balance at December 31, 2013	16,419,000	140,723,000	1,441,000	(12,501,000)	14,187,000	143,850,000	160,269,000
Corpus Activity:							
Additions	—	6,189,000	—	(6,189,000)	—	—	—
Payments on deferred contracts receivable	—	—	—	6,888,000	—	6,888,000	6,888,000
Repayments	—	—	—	—	(6,773,000)	(6,773,000)	(6,773,000)
Contributions relinquished	—	(881,000)	—	—	—	(881,000)	(881,000)
Transfers of Corpus	—	(7,141,000)	—	—	7,141,000	—	—
Net Excess of Assessments, Dues and Revenues over Expenses	4,635,000	—	—	—	—	—	4,635,000
Other Comprehensive Income (net of deferred income taxes of $769,000)	624,000	—	805,000	—	—	805,000	1,429,000
Balance at December 31, 2014	$21,678,000	$138,890,000	$ 2,246,000	$(11,802,000)	$14,555,000	$143,889,000	$165,567,000

The accompanying notes are an integral part of these financial statements.

Statements of Cash Flows

MUTUAL PROTECTION TRUST

	Years Ended December 31 2014	2013
Operating Activities		
Net excess of assessments, dues and revenues over expenses	$ 4,635,000	$ 306,000
Adjustments to reconcile net excess of assessments, dues and revenues over expenses to net cash provided by (used in) operating activities:		
Depreciation	925,000	742,000
Amortization on fixed income securities	1,080,000	1,167,000
Net realized investment gains	(153,000)	(130,000)
Deferred income taxes	(3,119,000)	(90,000)
Increase in lease incentive obligation	740,000	—
Changes in operating assets and liabilities:		
Accrued interest receivable	9,000	184,000
Assessments, dues and other coverages receivable	2,551,000	(3,533,000)
Income taxes receivable	379,000	852,000
Other assets	803,000	(4,877,000)
Non-assessable former members' liability	(4,399,000)	2,470,000
Unpaid claims and expenses	(2,802,000)	3,089,000
Deferred assessments, dues and other coverages	(313,000)	(3,248,000)
Payable to affiliated entity	(141,000)	1,672,000
Other liabilities	4,246,000	341,000
Net Cash Provided by (Used in) Operating Activities	4,441,000	(1,055,000)
Investing Activities		
Fixed income securities available-for-sale:		
Purchases	(31,830,000)	(54,301,000)
Sales and maturities	29,517,000	48,312,000
Net increase in short-term investments	—	2,562,000
Purchases of fixed assets	(239,000)	(321,000)
Net Cash Used in Investing Activities	(2,552,000)	(3,748,000)
Financing Activities		
Additions to Trust Fund Corpus	6,888,000	7,481,000
Repayments of Trust Fund Corpus	(7,654,000)	(5,365,000)
Net Cash (Used in) Provided by Financing Activities	(766,000)	2,116,000
Net Change in Cash and Cash Equivalents	1,123,000	(2,687,000)
Cash and Cash Equivalents at Beginning of Year		
Trust Fund Corpus	1,775,000	2,012,000
Trust Fund Operations	11,657,000	14,107,000
	13,432,000	16,119,000
Cash and Cash Equivalents at End of Year		
Trust Fund Corpus	1,124,000	1,775,000
Trust Fund Operations	13,431,000	11,657,000
	$ 14,555,000	$ 13,432,000

The accompanying notes are an integral part of these financial statements.

Notes to Financial Statements

MUTUAL PROTECTION TRUST

Note 1: Organization

The Mutual Protection Trust (MPT) was organized in 1977 for the purpose of providing its member physicians with medical professional liability protection and related claims administration, including defense and investigative services. Only physicians licensed to practice medicine in the state of California are eligible for membership. MPT is an interindemnity arrangement structured so that its members share the cost of medical professional liability protection. California legislation enacted in 1976 permitted the formation of a trust fund, with specific provisions including the requirement to accumulate a minimum Trust Fund Corpus of $10 million. The Cooperative of American Physicians, Inc. (CAP) sponsored the organization of MPT and the initial accumulated contributions from the members were transferred to the Trust Fund Corpus. MPT is governed by a Board of Trustees.

Each member is required to pay an Initial Trust Contribution based upon the member's risk classification and other factors. These contributions are accumulated into the Trust Fund Corpus. MPT members are allowed to pay Initial Trust Contributions in installments. The amount of Trust Fund Contributions unpaid is reported as a deferred contract receivable from members and is reported as a reduction in members' equity.

In accordance with the Mutual Protection Trust Agreement (the MPT Agreement), the Trust Fund Corpus may be utilized by the Board of Trustees only for (1) investment in qualified securities, (2) return of contributions to qualified members in connection with death, retirement or termination, (3) payment of claims in an amount not exceeding 10% of the Trust Fund Corpus, with such amounts being promptly repaid to the Trust Fund Corpus by levying assessments against MPT members, (4) collateral for bonds or deposits in court necessary for the appeal of judgments in an amount not exceeding 15% of the Trust Fund Corpus, (5) distribution to MPT members in the event of the dissolution of MPT, and (6) other lawful purposes approved in accordance with the MPT Agreement. The use of the Trust Fund Corpus for any other purpose is strictly prohibited.

Initial Trust Contributions are repaid to the member on the 10th anniversary of the membership effective date to members who have retired or who have voluntarily terminated membership in accordance with California Insurance Code Section 1280.7 and the MPT Agreement. Members must be in compliance with all terms and conditions of the MPT Agreement, including the payment of all amounts due to MPT, to be entitled to the repayment of initial trust contributions. All repayments of initial trust contributions require the written authorization of at least two-thirds of the Board of Trustees. Members who have voluntarily terminated membership through December 31, 2014 will receive the return of their Initial Trust Contributions aggregating $14,555,000, in accordance with the provisions of the MPT Agreement through the year 2024. The Initial Trust Contributions of members who have been involuntarily terminated pursuant to the provisions of the MPT Agreement that provide for no return of the Initial Trust Contribution, are recognized in operations in the year of termination since these members have relinquished the right to the return of their Initial Trust Contributions.

Assessments are determined by the Board of Trustees in accordance with California Insurance Code Section 1280.7 and the MPT Agreement and are used to fund estimated operating needs through the succeeding fiscal year. The Board of Trustees has the ability to levy additional assessments, should there be an operating shortfall in a given year (see Note 5). Assessments become an obligation of active members on the date of levy by the Board of Trustees. Results from operations may vary from year to year since actual amounts may differ from the estimates used to levy assessments.

Revenues are primarily comprised of other coverage fees and net investment income. Assessments and revenues are used to pay legally binding final judgments and settlements against MPT members, claims defense and investigative expenses and administrative expenses, and are used to fund MPT's actuarially estimated future liability for claims against non-assessable former members in accordance with the MPT Agreement and resolution of the Board of Trustees (see Note 4).

Note 2: Summary of Significant Accounting Policies

BASIS OF FINANCIAL STATEMENT PRESENTATION

The financial statements have been prepared in accordance with U.S. generally accepted accounting principles (GAAP). This basis of accounting necessarily requires the use of management estimates that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of assessments, revenues and expenses during the reporting period. Actual results may differ from those estimates.

Notes to Financial Statements

MUTUAL PROTECTION TRUST

Note 2: Summary of Significant Accounting Policies (continued)

ASSESSMENTS AND DUES

Member assessments are levied by the Board of Trustees annually and recognized over the period in which membership services are rendered. Member assessments levied in advance of the fiscal year to which they apply are deferred and recognized in operations in the subsequent year. In November 2014 and 2013, MPT levied $103,539,000 and $105,813,000 in member assessments, respectively. The November 2013 assessment included a $2,000,000 increase in assessments relating to operating requirements of fiscal year 2013 and $103,813,000 in assessments related to the 2014 fiscal year. The following table reconciles the assessments levied in November 2013 and 2012 to the assessments recognized in the Statements of Operations:

	Years Ended December 31	
	2014	2013
Assessment levied in November of the preceding year	**$103,813,000**	$111,388,000
Increase in 2013 assessments included in November of the preceding year	**—**	2,000,000
Net adjustments to member assessments during the year	**(336,000)**	256,000
Dues recognized	**5,163,000**	500,000
Assessments and dues recognized in the Statement of Operations	**$108,640,000**	$114,144,000

In addition to the assessments levied in November 2014 and 2013, the Board of Trustees also established annual dues of $190 per active member. In the November 2014 assessment, substantially all of the annual dues were contributed, based on an election made by the member, to the CAP State Political Action Committee or to another political action committee established to support medical liability reform. Amounts contributed to these political action committees are not recognized in assessments and dues, and any contributions to these funds are not recognized as expenses. These funds are included in other liabilities as a payable to CAP's political action committees. In the November 2013 assessment and dues, the Board of Trustees directed that $250,000 of annual dues remain in MPT and was used to offset operating costs in fiscal 2014. The remaining dues were contributed to the political action committees. In addition to the annual dues of $190, the November 2014 and 2013 assessments and dues also included a special dues amount totaling $4,984,000 and $4,913,000, respectively, intended to replace $5,000,000 in operating cash used in 2014 and 2013 for certain public affairs activities. These expenses, which are included in general and administrative other operating costs, were incurred to support activities that preserve medical professional liability tort limits in California. Similar to annual dues, these special dues were recognized in operations in the subsequent year. Total annual and special dues recognized in fiscal 2014 is $5,163,000 and is included in the table above. Included in deferred assessments, dues and other coverages as of December 31, 2014 and 2013, is $4,921,000 and $5,214,000, respectively, in annual and special dues that are deferred and will be recognized in operations in the subsequent year.

REVENUES

Other coverage fees are recognized when billed and earned as revenue over the period in which services are rendered. The billing for other coverage fees typically occurs in the first quarter of the calendar year.

NET INCREASE (DECREASE) IN MEMBERS' EQUITY

Net increase (decrease) in members' equity consists of net excess of assessments, dues and revenues over expenses and other comprehensive income (loss). MPT does not report total comprehensive income (loss) since its statutory authority precludes the Board of Trustees from assessing MPT's members for anything other than operating needs. Assessments are not revenues as they are levied by the Board of Trustees solely to support such operating needs. Accordingly, there is no net (loss) income, or total comprehensive income (loss). Any excess of assessments, dues and revenues over expenses are the property of MPT members (see Note 1). Other comprehensive income (loss) refers to gains and losses that are not included in net excess of assessments, dues and revenues over expenses, but rather are recorded directly in members' equity. For the years ended December 31, 2014 and 2013, the net increase (decrease) in members' equity consists of net excess of assessments, dues and revenues over expenses and unrealized gains (losses) on securities classified as available-for-sale.

Notes to Financial Statements

MUTUAL PROTECTION TRUST

Note 2: Summary of Significant Accounting Policies (continued)

Reclassification adjustments related to available-for-sale securities for the years ended December 31, 2014 and 2013 were as follows:

	2014	2013
Net realized investment gains included in the calculation of investment income, net	$ 66,000	$ 77,000
Tax effect (at 35%)	(23,000)	(27,000)
Net realized investment gains reclassified from other comprehensive income	$ 43,000	$ 50,000

CASH AND CASH EQUIVALENTS

Cash and cash equivalents include cash and short-term highly liquid investments with maturities of 90 days or less at acquisition and are principally stated at amortized cost.

INVESTMENTS

Investments are limited to those qualifying under California law as defined in Section 16430 of the Government Code.

Investments are classified as available-for-sale and are carried at fair value. Transfers between fair value hierarchy levels 1, 2, or 3 are recognized on the actual date of the circumstances that caused the transfer to occur. Unrealized gains and losses are accounted for, net of tax, as a component of other comprehensive income in members' equity.

Investments in the Trust Fund Corpus and Trust Fund Operating accounts are designated as available-for-sale and are carried at fair value.

Investment income is recorded as earned. Premiums and discounts on investment securities are primarily amortized using the interest method over the estimated lives of the investments. Realized gains and losses from sales transactions occurring during the year, are recognized in operations using the specific identification method. Unrealized gains and losses are determined using the specific identification method. Adjustments for other-than-temporary market declines are recorded when determination of loss is probable and is reported as a write-down of amortized cost to fair value.

FIXED ASSETS

Fixed assets are stated at cost, less accumulated depreciation of $8,907,000 and $7,982,000 as of December 31, 2014 and 2013, respectively. Included in this category is capitalized software costs, which represent costs directly related to obtaining, developing or upgrading internal-use software. Depreciation and amortization are computed using the straight-line method over the estimated useful lives of the assets, which are generally as follows:

Asset Description	Asset Life
Software	5 years
Computer equipment	5 years
Document imaging	5 years
Leasehold improvements	5 years
Furniture and equipment	8 years

CONCENTRATION OF CREDIT RISK

Financial instruments which potentially subject MPT to concentrations of credit risk consist principally of temporary cash investments and fixed income securities; assessments, dues and other coverages receivable; and other assets. MPT places its temporary cash investments with high credit quality financial institutions. Concentrations of credit risk with respect to fixed income securities are limited due to the large number of such investments and their distribution across many different industries and geographic regions. MPT's investments in federal agency securities are considered to have an implicit guarantee as to principal from the U.S. government and are considered to have minimal credit risk. Credit risk concentration in assessments, dues and other coverages receivable is considered minimal due to the large number of physicians totaling approximately 11,700 that comprise the total receivable.

Notes to Financial Statements

MUTUAL PROTECTION TRUST

Note 2: Summary of Significant Accounting Policies (continued)

Within other assets, financial instruments that potentially subject MPT to concentrations of credit risk are assets that support MPT's employee benefit plan obligations. Substantially all of these employee benefit plan assets are comprised of mutual funds and cash values in company-owned life insurance policies. Such cash values are also invested in mutual funds. Concentrations of credit risk are mitigated through both the large number of mutual funds used, and the diversification within each mutual fund among many different equity and fixed income positions across many companies and security issuers (see Note 7).

FAIR VALUE OF FINANCIAL INSTRUMENTS

Estimated fair value amounts, defined as the price that would be received to sell an asset or paid to transfer a liability (i.e., the "exit price") in an orderly transaction between market participants at the measurement date, have been determined using available market information and other appropriate valuation methodologies. However, considerable judgment is required in developing the estimates of fair value where quoted market prices are not available. Accordingly, these estimates are not necessarily indicative of the amounts that could be realized in a current market exchange. The use of different market assumptions or estimating methodologies may have an effect on the estimated fair value amounts.

The following methods and assumptions were used by MPT in estimating the fair value disclosures for financial instruments in the accompanying financial statements and in these notes:

Cash and cash equivalents, assessments, dues and other coverages receivable. The carrying amounts for these financial instruments as reported in the accompanying balance sheets approximate their estimated fair values.

Investments. MPT determines the fair value of its investments based on the fair value hierarchy established in Accounting Standards Codification (ASC) 820, which requires an entity to disclose the use of observable inputs and minimize the use of unobservable inputs for measuring fair value. Estimates of fair value measurements for these securities are estimated using relevant inputs, including available relevant market information, benchmark curves, benchmarking of like securities, sector groupings, and matrix pricing. Additionally, an Option Adjusted Spread model is used to develop prepayment and interest rate scenarios. Industry standard models are used to analyze and value securities with embedded options or prepayment sensitivities.

Each asset class is evaluated based on relevant market information, relevant credit information, perceived market movements and sector news. The market inputs utilized in the pricing evaluation include: benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, reference data, and industry and economic events. The extent of the use of each market input depends on the asset class and the market conditions.

This method of valuation will only produce an estimate of fair value if there is objectively verifiable information to produce a valuation. If objectively verifiable information is not available, MPT would be required to produce an estimate of fair value using some of the same methodologies, but would have to make assumptions for market-based inputs that are unavailable due to market conditions. Depending on the security, the priority of the use of inputs may change or some market inputs may not be relevant. For some securities, additional inputs may be necessary.

Because the fair value estimates of most fixed income securities are determined by evaluations that are based on observable market information rather than market quotes, most estimates of fair value for fixed income securities are based on estimates using objectively verifiable information and are included in the amount disclosed in Level 2 of the hierarchy. The value of U.S. agencies, states and municipalities, corporate bonds, residential mortgage-backed securities and commercial mortgage-backed securities is based on the observable market information and as such, is included in the Level 2 hierarchy. Level 1 is limited to unadjusted quoted prices in active markets for identical instruments.

All investments on the accompanying balance sheet are stated at fair value and are considered Level 2 investments as of December 31, 2014 and 2013.

There were no transfers in and out of Level 1 and Level 2 fair value measurements during the years ended December 31, 2014 and 2013. There were no securities at December 31, 2014 or 2013 whose fair value measurements were based on Level 3: Unobservable inputs.

Notes to Financial Statements

MUTUAL PROTECTION TRUST

Note 2: Summary of Significant Accounting Policies (continued)

UNPAID CLAIMS AND EXPENSES AND NON-ASSESSABLE FORMER MEMBERS' LIABILITY

MPT reports its liability consistent with California Insurance Code Section 1280.7 and the MPT Agreement. Such liability at each year-end, as detailed in Note 4, represents the unpaid amount of the following items:

1. Accrued liability for claims defense and investigative expenses for all open claims under MPT management;

2. Total liability for legally binding final settlements and judgments against members who are current in the payment of all amounts due under the MPT Agreement and former members who have met the requirements for retirement, termination with tail coverage, transfer of membership or who are deceased; and

3. Actuarially estimated future liability for claims reported and claims incurred but not reported against former MPT members who are no longer assessable because of retirement, transfer of membership, voluntary or involuntary termination with tail coverage or death (collectively referred to as non-assessable former members' liability). Also included in this liability is an estimate for claims administration and other adjusting expenses that will be incurred in administering the claims for such non-assessable former members.

INCOME TAXES

MPT files its federal income tax return as a mutual insurance company and files its California income tax return under the provision of the California Bank and Corporation Tax Law as a business trust. Income taxes are provided on the basis of items included in the determination of income for financial reporting purposes regardless of the period when such items are reported for tax purposes. Deferred tax assets and liabilities are recorded to reflect the tax consequences in future years of temporary differences between the tax bases of assets and liabilities and the corresponding bases used for the financial statements. A valuation allowance is recorded to reduce deferred tax assets to an amount that represents management's best estimate of the amount that more likely than not will be realized. The income tax effect on unrealized investment gains and losses on the Trust Fund Corpus investments is accounted for as deferred income taxes and is included as a separate component of the Trust Fund Corpus. Interest and penalties on tax amounts paid or received are included in investment income, net and general and administrative other operating costs, respectively (see Note 8).

NEW ACCOUNTING STANDARDS

In February 2013, the FASB issued an update to clarify the scope and applicability of a particular disclosure to nonpublic entities that resulted from the issuance of Accounting Standards Update No. 2011-04, *Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs.* This update clarifies that nonpublic entities that have total assets of $100 million or more or that have one or more derivatives are not exempted from the requirement to disclose "the level of the fair value hierarchy within which the fair value measurements are categorized in their entirety (Level 1, 2, or 3)" for items that are not measured at fair value in the statement of financial position but for which fair value is disclosed. The adoption of this update did not have a material impact on MPT's financial statements.

In February 2013, the FASB issued an update to improve the reporting of reclassifications out of accumulated other comprehensive income. The amendments in this update require an entity to report the effect of significant reclassifications out of accumulated other comprehensive income on the respective line items in net income if the amounts being reclassified are required under U.S. GAAP to be reclassified in their entirety to net income in the same reporting period. An entity is required to cross-reference other disclosures required under U.S. GAAP that provide additional detail about those amounts. The amendments do not change the current requirements for reporting net income or other comprehensive income in financial statements. This update is effective prospectively for reporting periods beginning after December 15, 2013, and may be adopted earlier. MPT adopted this guidance effective January 1, 2014. The adoption of this update did not have a material impact on MPT's financial statements.

In July 2013, the FASB issued an update regarding the financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. The objective of this update is to reduce diversity in practice by providing guidance on the presentation of unrecognized tax benefits in order to better reflect the manner in which an entity would settle at the reporting date any additional income taxes that would result from the

Notes to Financial Statements

MUTUAL PROTECTION TRUST

Note 2: Summary of Significant Accounting Policies (continued)

disallowance of a tax position when net operating loss carryforwards, similar tax losses, or tax credit carryforwards exist. This update will be effective for reporting periods beginning after December 15, 2014, and may be adopted earlier. The adoption of this update is not expected to have a material impact on MPT's financial statements.

SUBSEQUENT EVENTS

MPT has completed an evaluation of all subsequent events through March 19, 2015, which is the date the financial statements were available for issuance, and has concluded that no subsequent event occurred which would require recognition or disclosure.

Note 3: Investments

Fixed income securities, exclusive of cash and cash equivalents are comprised of the following:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
DECEMBER 31, 2014				
Trust Fund Corpus, restricted:				
Fixed income securities, available-for-sale				
States and municipalities	$ 24,199,000	$1,864,000	$ —	$ 26,063,000
Corporate bonds	43,170,000	772,000	(120,000)	43,822,000
Residential mortgage-backed securities	70,968,000	1,431,000	(511,000)	71,888,000
Commercial mortgage-backed securities	1,226,000	21,000	—	1,247,000
Total fixed income securities	$139,563,000	$4,088,000	$ (631,000)	$143,020,000
Trust Fund Operating:				
Fixed income securities, available-for-sale				
Corporate bonds	$ 21,538,000	$ 493,000	$ (31,000)	$ 22,000,000
Residential mortgage-backed securities	43,200,000	603,000	(341,000)	43,462,000
Total fixed incomes securities	$ 64,738,000	$1,096,000	$ (372,000)	$ 65,462,000
DECEMBER 31, 2013				
Trust Fund Corpus, restricted:				
Fixed income securities, available-for-sale				
U.S. Agencies	$ 3,985,000	$ 81,000	$ —	$ 4,066,000
States and municipalities	24,291,000	2,368,000	—	26,659,000
Corporate bonds	37,792,000	949,000	(256,000)	38,485,000
Residential mortgage-backed securities	71,875,000	1,000,000	(1,952,000)	70,923,000
Commercial mortgage-backed securities	1,726,000	28,000	—	1,754,000
Total fixed income securities	$139,669,000	$4,426,000	$(2,208,000)	$141,887,000
Trust Fund Operating:				
Fixed income securities, available-for-sale				
U.S. Agencies	$ 505,000	$ 10,000	$ —	$ 515,000
Corporate bonds	19,734,000	693,000	(41,000)	20,386,000
Residential mortgage-backed securities	43,006,000	352,000	(1,248,000)	42,110,000
Total fixed income securities	$ 63,245,000	$1,055,000	$(1,289,000)	$ 63,011,000

The amortized cost and fair value of fixed income securities available-for-sale as of December 31, 2014, by contractual repayment date of principal, are shown on the following page. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Notes to Financial Statements

MUTUAL PROTECTION TRUST

Note 3: Investments (continued)

	Amortized Cost	Fair Value
Trust Fund Corpus, restricted		
Due in one year or less	$ 7,519,000	$ 7,577,000
Due after one year through five years	50,823,000	52,487,000
Due after five years through 10 years	9,027,000	9,821,000
	67,369,000	69,885,000
Residential mortgage-backed securities	70,968,000	71,888,000
Commercial mortgage-backed securities	1,226,000	1,247,000
	$139,563,000	$143,020,000
Trust Fund Operating		
Due in one year or less	$ 4,094,000	$ 4,170,000
Due after one year through five years	12,911,000	13,113,000
Due after five years through 10 years	4,533,000	4,717,000
	21,538,000	22,000,000
Residential mortgage-backed securities	43,200,000	43,462,000
	$ 64,738,000	$ 65,462,000

For the years ended December 31, 2014 and 2013, proceeds from sales of investments were $10,575,000 and $8,627,000, respectively.

The following table shows the gross unrealized losses and fair value aggregated by investment category and length of time those securities have been in a continuous unrealized loss position:

	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
DECEMBER 31, 2014						
Trust Fund Corpus, restricted:						
Fixed income securities						
Corporate bonds	$ 7,754,000	$(27,000)	$ 6,704,000	$ (93,000)	$14,458,000	$(120,000)
Residential mortgage-backed securities	3,200,000	(7,000)	25,720,000	(504,000)	28,920,000	(511,000)
Total fixed income securities	$10,954,000	$(34,000)	$32,424,000	$(597,000)	$43,378,000	$(631,000)
Trust Fund Operating:						
Fixed income securities						
Corporate bonds	$ 2,846,000	$(16,000)	$ 1,043,000	$ (15,000)	$ 3,889,000	$ (31,000)
Residential mortgage-backed securities	4,163,000	(19,000)	17,543,000	(322,000)	21,706,000	(341,000)
Total fixed income securities	$ 7,009,000	$(35,000)	$18,586,000	$(337,000)	$25,595,000	$(372,000)

Notes to Financial Statements

MUTUAL PROTECTION TRUST

Note 3: Investments (continued)

	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
DECEMBER 31, 2013						
Trust Fund Corpus, restricted:						
Fixed income securities						
Corporate bonds	$11,571,000	$ (256,000)	$ —	$ —	$11,571,000	$ (256,000)
Residential mortgage-backed securities	42,556,000	(1,858,000)	877,000	(94,000)	43,433,000	(1,952,000)
Total fixed income securities	$54,127,000	$(2,114,000)	$877,000	$(94,000)	$55,004,000	$(2,208,000)
Trust Fund Operating:						
Fixed income securities						
Corporate bonds	$ 3,030,000	$ (41,000)	$ —	$ —	$ 3,030,000	$ (41,000)
Residential mortgage-backed securities	28,561,000	(1,150,000)	877,000	(98,000)	29,438,000	(1,248,000)
Total fixed income securities	$31,591,000	$(1,191,000)	$877,000	$(98,000)	$32,468,000	$(1,289,000)

MPT reviews at least quarterly its investment portfolio for securities that may have an other-than-temporary impairment. In its impairment analysis, MPT takes into consideration numerous criteria, including the duration and extent of any decline in estimated fair value, industry factors, downgrades by rating agencies, liquidity and fundamental factors of the issuers, as well as its ability and intent to retain its investment in the issuer to allow for any anticipated recovery in market value or maturity. If the decline is determined to be other than temporary, the investment's amortized cost is written down to estimated fair value with the unrealized loss recognized in operations as a realized loss on investments.

As of December 31, 2014 and 2013, none of the investments whose estimated fair values were less than amortized costs were considered to be other-than-temporarily impaired given the severity and duration of the impairment and the credit quality of the issuers.

MPT does not intend to sell its investments whose fair values are less than amortized costs and it is not more likely than not that MPT will be required to sell the investments before recovery of the amortized cost bases, which may be maturity.

Investment income, net is summarized as follows:

	Years Ended December 31	
	2014	2013
Interest income	**$ 7,058,000**	$ 7,333,000
Gross gains on sales of investments	**153,000**	130,000
Investment management fees and expenses	**(324,000)**	(312,000)
Net amortization of premium on fixed income securities	**(1,079,000)**	(1,167,000)
Investment income, net	**$ 5,808,000**	$ 5,984,000

Notes to Financial Statements

MUTUAL PROTECTION TRUST

Note 4: Unpaid Claims and Expenses and Non-Assessable Former Members' Liability

Unpaid claims and expenses for assessable members are comprised of the following:

	December 31 2014	December 31 2013
Accrued indemnity	**$10,230,000**	$13,265,000
Accrued defense and investigative services	**3,222,000**	2,989,000
	$13,452,000	$16,254,000

MPT has assumed claims liability by providing tail coverage to certain former members who are no longer liable for assessments (non-assessable former members) including those who are retired, transferred, terminated or deceased. Members voluntarily terminating have no tail coverage from MPT unless they remain liable for assessments or pay a tail coverage fee.

Under California Insurance Code Section 1280.7, members involuntarily terminated by MPT's peer review process are entitled to receive tail coverage without liability for future assessments upon release of the right to a return of their Initial Trust Contributions.

The liability for claims of non-assessable former members reflects an estimate of future payments for claims reported as of each year-end, an estimate of the related defense and investigative expenses, an estimate for claims administration and other adjusting expenses, and a provision for claims incurred but not reported. Since this liability is based upon estimates, and while management believes that amounts recorded are adequate, the ultimate liability may differ from the amounts provided in the financial statements. The methodologies for making such estimates and for establishing the resulting liabilities are continually reviewed by management and the independent actuaries of MPT. Adjustments to the estimates are included in operations in the period they are determined. The actuarially estimated liability for claims of non-assessable former members is as follows:

	December 31 2014	December 31 2013
Claims reported:		
Members retired	**$ 3,633,000**	$ 3,545,000
Members voluntarily terminated, transferred and deceased	**9,243,000**	5,952,000
Members involuntarily terminated	**11,838,000**	15,048,000
Claims incurred but not reported	**6,292,000**	10,471,000
Claims administration and other adjusting expenses	**2,259,000**	2,648,000
	$33,265,000	$37,664,000

The following summarizes the years in which the actuarially estimated liability for claims reported and claims incurred but not reported for non-assessable former members are estimated to be paid:

Years Ending December 31	Amount
2015	$ 9,820,000
2016	7,191,000
2017	5,196,000
2018	3,738,000
2019	2,891,000
2020 and after	4,429,000
	$33,265,000

Cash and investments in MPT's Trust Fund Operations accounts have been retained sufficient to fund the total estimated future liability for claims against non-assessable former members of $33,265,000 at December 31, 2014. Such funds may be used for other purposes only upon approval of the Trustees, and it is the Board's intention to replenish any such funds through the regular assessment process.

Notes to Financial Statements

MUTUAL PROTECTION TRUST

Note 5: Contingencies

MPT is liable for unpaid claims and expenses only as required by California Insurance Code Section 1280.7 and the MPT Agreement. Any future liability beyond the amount reported in the financial statements for unpaid claims and expenses of the MPT members will become the liability of MPT only to the extent that final settlements or judgments exist against MPT members who are current in all payments due to MPT, or when an MPT member becomes a former member and qualifies for non-assessable former member status.

MPT's independent actuaries have estimated the aggregate liability of the assessable members for all actual claims and expenses, which are not the current liability of MPT, to be $125,249,000 (net of reinsurance of $10,855,000 as discussed below) and $134,471,000 (net of reinsurance of $10,575,000 as discussed below) as of December 31, 2014 and 2013, respectively. This liability is MPT's estimate of future payments for all claims reported as of each year-end and the related defense and investigative expenses. Additional occurrences may become reported claims in subsequent periods. Actuarial studies have estimated that this liability for unpaid claims and expenses will require funding through future assessments, which are affected by the amount of investment earnings, over a period of up to eighteen years. In the highly unlikely event this contingent liability becomes due in its entirety within the next 12 months, management believes there will be sufficient available liquidity within its Trust Fund Operations' cash and cash equivalents, fixed income securities, reinsurance recoveries, and available lines of credit to fully fund this contingent liability prior to making any unanticipated assessment of the membership.

MPT has entered into reinsurance contracts with major global reinsurance companies and its affiliate, Cooperative of American Physicians Insurance Company, Inc. (CAPIC, a wholly-owned subsidiary of CAP), which provide coverage on a claims-made basis for case losses in excess of a $1,000,000 retention for which MPT is obligated. Coverage also has been purchased that applies to multiple cases arising from the same occurrence. MPT is contingently liable with respect to ceded reinsurance, if any, should any reinsurer be unable to meet its obligations under those agreements. MPT also has reinsurance contracts with major London-based reinsurance companies and CAPIC, which provides coverage on a claims-made basis for multiple claims arising out of one common, systemic event. Limits of $7,000,000 are available to MPT on a claims-made basis over a $3,000,000 retention. Premiums paid under this contract were $565,000 and $694,000 for the years ended December 31, 2014 and 2013, respectively (see Note 6). During 2013, MPT maintained a contract with a major reinsurance company that was designed to protect MPT from a sudden and unexpected level of loss, defense and investigative payments within a calendar year that could lead to an unanticipated assessment. Reinsurance protection was available in the event that calendar year loss and defense and investigative payments, net of underlying reinsurance recoveries, exceeded an actuarially determined attachment point. The initial adjustable premium of $5,000,000 was held by MPT on a contingent basis. The attachment point was set at a level where the likelihood of the reinsurance being triggered was remote. Due to the limited transfer of risk evident in the contract, in accordance with ASC 340-30, *Other Assets and Deferred Costs – Insurance Contracts that do not Transfer Insurance Risk,* the deposit method of accounting was used. The contingent adjustable premium of $5,000,000 was included in Trust Fund Operations fixed income securities as of December 31, 2013. This contract was terminated at January 1, 2014.

In December 2010, an audit was performed by a municipal taxing authority of certain business tax returns filed by MPT covering the tax years 2008, 2009, and 2010. In January 2011, the results of the audit indicated that the taxing authority objected to the method employed by MPT in preparing the tax returns. MPT objected to the audit's findings, and believed there are alternative methods allowed for under the regulations that more appropriately reflect MPT's business tax obligations. In September 2012, MPT exhausted its administrative remedies with the taxing authority and was unsuccessful in its protest to the audit's findings. The taxing authority closed its audit for the years in question and MPT paid the taxing authority $498,000 in additional taxes. In July 2013, the taxing authority audited MPT's business tax returns for tax years 2011, 2012, and 2013. The taxing authority adjusted these tax years using the same methodology used in the earlier audit, resulting in additional taxes of $288,000. MPT included in other liabilities an estimate of $319,000 as of December 31, 2013 in additional business tax expense for the 2011 and 2012 tax years and for additional legal expenses. In March and April 2014, MPT and the municipal taxing authority reached agreement on the two audits covering the 2008 through 2013 tax years and established a more appropriate method of preparing MPT's tax returns. As a result of these agreements, MPT received a refund of $515,000 in taxes previously paid on the 2008 through 2013 tax years and the audits for these tax years have been closed.

MPT is subject to legal proceedings arising from the normal conduct of its business. In the opinion of management, any ultimate liability that may arise from these proceedings will not have a material effect on MPT's financial position.

Notes to Financial Statements

MUTUAL PROTECTION TRUST

Note 6: Related Party Transactions

Effective January 1, 2010, MPT and CAP entered into an administrative and management services agreement whereby CAP provides membership, claims, risk management, financial, and other administrative and management services to MPT. Under the agreement, CAP receives monthly fees from MPT for these services that are based on actual expenses incurred by CAP plus a margin. Fees of $24,982,000 and $26,526,000 were incurred by MPT for administrative and management services under the agreement for the years ended December 31, 2014 and 2013, respectively.

Effective January 1, 2013, MPT and CAPIC entered into a services agreement whereby CAPIC provides legal defense services to MPT physicians. MPT pays CAPIC monthly fees for these services that are based on actual costs incurred. Fees incurred under this agreement were $16,672,000 and $16,266,000 for the year ended December 31, 2014 and 2013, respectively. Included in the payable to affiliated entity is $1,786,000 and $1,672,000 payable to CAPIC for these services as of December 31, 2014 and 2013, respectively.

In 2014 and 2013, MPT had reinsurance contracts with CAPIC. These contracts principally provide per claim excess of loss reinsurance coverage on a claims-made form for MPT for claims reported in 2014 and 2013. Aggregate stop-loss coverage was also provided to MPT in 2013 on a claims-made basis. The aggregate stop-loss coverage provided for a limit of $11,000,000 in excess of an aggregate attachment of $115,200,000. These agreements can be terminated and commuted at the end of any calendar quarter prospectively by mutual agreement of CAPIC and MPT. Premiums paid by MPT under these agreements were $2,500,000 and $3,100,000 for the years ended December 31, 2014 and 2013, respectively. MPT also maintains reinsurance coverage on a claims-made basis for multiple claims arising out of one common event. CAPIC participates in this contract along with other non-affiliated reinsurance companies. Premiums paid by MPT to CAPIC under this contract were $204,000 and $243,000 for the years ended December 31, 2014 and 2013, respectively. For the years ended December 31, 2014 and 2013, total affiliate reinsurance premium expense under all reinsurance contracts with CAPIC was $2,679,000 and $3,343,000, respectively, and is included in Claims: Other Operating Costs.

Note 7: Employee Benefits

MPT sponsors a 401(k) savings plan for its employees. Employees' contributions are matched by MPT at a level that is determined by the Board of Trustees. The contribution expense for the 401(k) savings plan was $21,000 for the years ended December 31, 2014 and 2013. Eligible employees vest in MPT's contribution over a four-year vesting schedule. MPT also sponsors a supplemental employee retirement program (SERP) for certain employees. Participants vest, on average, over a 10-year period. SERP liabilities, which are included in other liabilities, totaled $5,722,000 and $5,518,000 at December 31, 2014 and 2013, respectively. The expense (benefit) related to this program was $301,000 and ($774,000) for the years ended December 31, 2014 and 2013, respectively. The significant increase in expense in 2014 was due primarily to a decrease in the discount rate to 3% from 3.38% in 2014 and 2013, respectively. These rates were used to determine the present value of SERP obligations for the respective years. MPT maintains a non-qualified deferred compensation program (NDCP) for eligible employees and Board members. Under the plan, participants can defer compensation or Board fees based on an annual election. Amounts deferred are credited with notional investment earnings on a tax deferred basis until such amounts are distributed to participants. Liabilities of the NDCP, which are included in other liabilities, totaled $11,134,000 and $10,942,000 at December 31, 2014 and 2013, respectively.

MPT funds its SERP and NDCP obligations principally through life insurance policies on the participants and eligible participants. Mutual fund investments are also used to fund these obligations. The life insurance policy assets supporting these benefit plan obligations are carried at their cash surrender value, which approximates fair value, and are included in other assets, totaling $13,660,000 and $13,113,000 at December 31, 2014 and 2013, respectively. The mutual fund assets are carried at fair value, totaling $4,846,000 and $4,611,000 at December 31, 2014 and 2013, respectively.

Notes to Financial Statements

MUTUAL PROTECTION TRUST

Note 7: Employee Benefits (continued)

MPT maintains a post-retirement medical benefit plan for certain employees. Beginning at the age of 62, participants can use amounts contributed to a separate post-retirement account held on their behalf (by a third party trust) to fund eligible medical expenses. Amounts paid to the trust by MPT are not refundable and become the property of the trustee on behalf of participants. The trust invests funds received from MPT in universal life insurance policies covering participants, which includes a death benefit funded by MPT until the participant reaches the vesting age of 62. While the plan establishes targeted post-retirement benefit levels for participants, there is no obligation for MPT to fully fund these levels and the employees are only eligible to receive the benefits accumulated in their account. Amounts contributed to the trust by MPT were $21,000 for the years ended December 31, 2014 and 2013.

Note 8: Income Taxes

The components of the income tax benefit (expense) are as follows:

	Years Ended December 31	
	2014	2013
Current	$2,035,000	$(123,000)
Deferred	3,119,000	90,000
Total	$5,154,000	$ (33,000)

A reconciliation of income tax benefit (expense) computed at the federal statutory tax rate to total income tax benefit (expense) is summarized as follows:

	Years Ended December 31	
	2014	2013
Federal income tax benefit (expense) at 35%	$ 182,000	$ (119,000)
Decrease (increase) in taxes resulting from:		
State income tax benefit (expense) (net of federal benefit/expense)	1,542,000	(417,000)
Non-deductible public affairs activities	(1,801,000)	(1,769,000)
Change in valuation allowance	4,890,000	2,283,000
Return-to-provision adjustments	361,000	—
Other	(20,000)	(11,000)
Total federal income tax benefit (expense)	$ 5,154,000	$ (33,000)

Notes to Financial Statements

MUTUAL PROTECTION TRUST

Note 8: Income Taxes (continued)

The significant components of deferred income tax assets and liabilities are as follows:

	December 31 2014	2013
Trust Fund Corpus, restricted:		
Deferred tax liability attributable to net unrealized investment gains	$ (1,210,000)	$ (776,000)
Trust Fund Operating:		
Deferred tax assets attributable to:		
Initial trust contributions	46,543,000	46,169,000
Discounting of non-assessable former members' claim and other liability	1,897,000	2,326,000
Net operating loss carryforward	10,504,000	15,393,000
Employee benefit obligations	8,370,000	7,846,000
Lease incentive obligations	1,388,000	—
California EZ credit	129,000	129,000
Capital loss carryover	215,000	282,000
Deferred tax asset attributable to net unrealized investment losses	—	82,000
Other	—	328,000
Deferred tax assets before valuation allowance	69,046,000	72,555,000
Valuation allowance	(10,504,000)	(15,393,000)
Deferred tax assets after valuation allowance	58,542,000	57,162,000
Deferred tax liabilities attributable to:		
Discounting of assessable members' contingent claim liability	(40,096,000)	(42,253,000)
Deferred tax liability attributable to net unrealized investment gains	(253,000)	—
Accretion of bond discount	(1,442,000)	(1,372,000)
Other	(430,000)	—
Deferred tax liabilities	(42,221,000)	(43,625,000)
Deferred tax asset, net	$ 16,321,000	$ 13,537,000

ASC 740, *Income Taxes,* requires that deferred tax assets be reduced by a valuation allowance if it is more likely than not that some portion or all of the deferred tax asset will not be realized. Realization of the deferred income tax asset is dependent on MPT generating sufficient taxable excess of assessments and revenues over expenses in future years as the deferred income tax charges become currently deductible for tax reporting purposes. MPT evaluates the need for a valuation allowance taking into consideration all available evidence, both positive and negative, including future sources of income, tax planning strategies, future contractual cash flows and reversing temporary differences.

As of December 31, 2014 there remains federal net operating loss carryforwards totaling $24,082,000 which will expire beginning 2026, to be applied to future tax years. The net operating loss carryforward resulted primarily from a change in accounting method for incurred losses that was permitted by the Internal Revenue Service in 2008 on 2006 and subsequent tax years. As of December 31, 2014 there remains a state net operating loss carryforward totaling $23,475,000 which will expire beginning 2028 to be applied to future tax years. MPT has determined that it is not more likely than not that the deferred tax assets related to the net operating losses will be recognized. Accordingly, MPT has established a valuation allowance against these deferred tax assets. The valuation allowance decreased by $4,889,000 and $2,283,000 in 2014 and 2013, respectively.

Notes to Financial Statements

MUTUAL PROTECTION TRUST

Note 8: Income Taxes (continued)

MPT believes that it is more likely than not that the results of future operations and various tax planning strategies will generate sufficient taxable income in the periods necessary to realize the remaining $16,321,000 in deferred tax assets, net. Additional valuation allowance benefits or charges could be recognized in the future due to changes in management's expectations regarding the realization of tax benefits.

On December 8, 2014, MPT was granted its request to the California taxing authority to be treated as a cooperative as defined under Revenue and Taxation Code 24405. Under this section, an eligible cooperative is entitled to a special deduction generally equal to taxable income. Through an additional agreement, MPT was allowed to amend prior tax returns covering 2008 through 2012 tax years to apply this special deduction. As a result of this agreement, MPT received a refund of prior income taxes totaling $2,324,000 and interest of $171,000.

Income taxes refunded for the years ended December 31, 2014 and 2013 was $2,413,000 and $729,000, respectively. There was no tax penalties recognized for the years ended December 31, 2014 or 2013.

Tax years 2011 through 2013 and tax years 2010 through 2013 are subject to examination by the federal and California taxing authorities, respectively. There are no income tax examinations currently in progress.

MPT's income tax returns are subject to audit by the Internal Revenue Service and state tax authorities. Significant disputes may arise with these tax authorities involving issues of the timing and amount of deductions and allocations of income among various tax jurisdictions because of differing interpretations of tax laws and regulations. MPT periodically evaluates its exposures associated with tax filing positions.

As of December 31, 2014 and 2013, MPT had no uncertain tax positions.

Note 9: Commitments

MPT and CAP occupy their home office and regional office facilities under operating leases which provide for adjustments to the lease payments based upon contractual commitments and inflationary factors. Both companies are lessees under these operating leases. Rent expense is apportioned between MPT and CAP based primarily on the number of employees. The total rent expense under these leases was $2,442,000 and $3,312,000 for the years ended December 31, 2014 and 2013, respectively. The total rent expense apportioned to MPT was $759,000 and $48,000 for the years ended December 31, 2014 and 2013, respectively. The future minimum rental commitments under these operating leases are as follows:

Years Ending December 31	Amount
2015	$ 2,032,000
2016	1,673,000
2017	1,696,000
2018	1,751,000
2019 and after	9,120,000
	$16,272,000

MPT maintains a line of credit in the amount of $20,000,000, which bears interest at the bank prime rate or a borrowing rate based upon the London Interbank Offered Rates plus a margin for any portion outstanding. The line of credit includes a sub-feature for letters of credit which may be used to collateralize appeal bonds obtained by MPT. There were no letters of credit outstanding under this sub-feature at December 31, 2014 or 2013.

MPT obtains surety bonds for use as collateral for judgments on appeal. MPT indemnifies the surety company for any recoveries made against the appeal bond. Fees are paid based upon the amount and duration of the appeal bond. No amounts were outstanding on appeal bonds at December 31, 2014 or 2013.

Supplementary Financial Information

MUTUAL PROTECTION TRUST

	As of and For the Years Ended				
	2014	2013	2012	2011	2010
RESULTS OF OPERATIONS					
(In millions)					
Total Assessments, Dues and Revenues	**$130.4**	$135.3	$127.1	$118.0	$118.0
Expenses					
Indemnity Expense	**$ 42.3**	$ 48.1	$ 51.0	$ 43.4	$ 50.7
Defense and Investigative	**35.2**	35.1	31.9	30.7	30.6
Other	**53.5**	51.8	46.5	44.7	42.6
Total Expenses	**$131.0**	$135.0	$129.4	$118.8	$123.9
(Deficit) Excess of Assessments, Dues and Revenues Over Expenses, net of income taxes	**$ (0.5)**	$ 0.3	$ (2.0)	$ 1.8	$ (5.4)
FINANCIAL POSITION					
Cash and Invested Assets	**$223.0**	$218.3	$226.5	$226.1	$216.4
Total Assets	**$353.6**	$350.7	$346.7	$340.3	$327.3
Members' Equity	**$165.6**	$160.3	$163.0	$162.5	$154.5
MEMBERSHIP AND CLAIMS (Unaudited)					
Active Members at Year End	**11,688**	11,789	11,726	11,533	11,067
Services for Reported Claims					
Cases Opened	**1,142**	1,234	1,198	1,291	1,139
Cases Closed	**1,113**	1,170	1,190	1,228	1,209
Cases Under Management	**1,522**	1,493	1,429	1,421	1,358
Per Active Member (In thousands)					
Total Assessments, Dues and Revenues	**$ 11.2**	$ 11.5	$ 10.8	$ 10.2	$ 10.7
Indemnity Expense	**3.6**	4.1	4.3	3.8	4.6
Defense and Investigative	**3.0**	3.0	2.7	2.7	2.8
Other Expenses	**4.6**	4.4	4.0	3.8	3.8
Total Expenses	**$ 11.2**	$ 11.5	$ 11.0	$ 10.3	$ 11.2

Cooperative of American Physicians, Inc. is licensed as a property and casualty broker-agent and surplus line broker (California license No. 0B72723).
Insurance purchased by CAPAssurance, a Risk Purchasing Group, is from a "non-admitted" or "surplus line" insurer that is not licensed by the state of California.

CAP Physicians Insurance Agency, Inc. is authorized under California license No. 0F97719.

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