COOPERATIVE OF
AMERICAN PHYSICIANS

Surpassing Challenges

MISSION STATEMENT

We are leaders and innovators in the healthcare community.

STATEMENT OF PRINCIPLES

Through its core products, Mutual Protection Trust and the CAPAssurance, a Risk Purchasing Group, the Cooperative of American Physicians, Inc. 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.

A MESSAGE TO OUR MEMBERS

Twenty-twenty was no doubt frustrating for so many in the health care profession. Physicians up and down the state battled a virus that seemed determined to counter their Herculean efforts at every turn.

With a health care delivery system scrambling to keep a populace healthy amid an economy largely upended, it was all the more important that the Cooperative of American Physicians and the Mutual Protection Trust respond in ways that addressed both immediate needs and long-term goals. Fortunately, we believe that many of the innovations implemented in 2020 in response to the pandemic will bring lasting efficiencies to CAP operations.

The impact of COVID-19 was not yet fully revealed when CAP built a multi-faceted – and constantly updated – COVID-19 Resource Center. Our members rushed to the COVID-19 Resource Center to get fresh information on topics from PPE to patient safety strategies during the pandemic.

CAP then launched a series of webinars curated specifically for physicians practicing during the pandemic. Implementing telehealth, understanding legal immunity issues, and learning about small business relief financing were some of the topics of webinars attended by hundreds of our members. CAP continues to develop new webinars as we receive feedback from our members and monitor developments in the area.

Meanwhile CAP's dedicated risk management e-newsletter, the Patient Safety Advocate, spread the word on organized medicine's efforts to distribute PPE to physicians and kept members apprised of the latest updates from the CDC, CMA, and other organizations.

CAP's response to the health crisis wasn't limited to getting out information critical to physicians treating patients or dealing with closed offices. Beginning with a company-wide move to keep CAP staff safe through working at home, CAP developed new remote-access competencies that will make our members' connections to services not only safer today but more efficient and less costly in the months and years to come.

For example, rather than inviting members to physically attend meetings in the office, CAP implemented remote protocols for nearly every kind of business gathering. Another success was the ability to conduct virtual member office visits by our risk management representatives. Presenting the Litigation Education Retreat remotely and conducting the Public Affairs Symposium in webinar format provided greater flexibility for physicians to participate in the organization. Going forward, our members can expect to save time and resources through these kinds of personalized remote-access opportunities.

And in recognition of the pandemic's effect on claims activities and other operations, CAP and MPT were pleased to announce in April the return to members of $4.7 million in assessment funds.

Successfully responding to emergent events requires more than just taking unique actions to meet immediate needs. It also requires staying attentive to the regular, day-to-day operations necessary to conduct an enterprise such as CAP and MPT. Significant in that regard was a further reduction in claims frequency, growth in membership over the previous year, no overall increase in the assessment, and MPT's recognition yet again by the A.M. Best Company as an A+ (Excellent)-rated provider of medical professional liability protection.

It's commonly said that 2020 was a year like no other. It's probably also safe to say that the future will bring similar challenges. Under such circumstances, the ultimate test is one's ability to adapt to circumstances not just to get along, but to move forward. We hope you agree that 2020 was a year in which CAP found new ways to be vital to our members.

Thank you for keeping CAP close to you.

Wayne Kleinman, MD
President and Chair
Cooperative of American Physicians, Inc.

Sarah E. Scher, JD
Chief Executive Officer

Charles P. Steinmann, MD
Chair
Mutual Protection Trust

Board of Directors

COOPERATIVE OF AMERICAN PHYSICIANS

Wayne Kleinman, MD
President and Chair

Paul Weber, MD, PhD
Vice Chair and Vice President

Sheilah Clayton, MD

Roger S. Eng Jr., MD, MPH, FACR

Dennis T. Jordanides, MD

Gregory Lizer, MD, FAAP

Graham A. Purcell, MD

Board of Trustees

MUTUAL PROTECTION TRUST

Charles P. Steinmann, MD, FACA
Chair

Phillip Unger, MD
Vice Chair

Othella T. Owens, MD, FACS

Stewart L. Shanfield, MD

Lisa Thomsen, MD, FAAFP

COOPERATIVE OF AMERICAN PHYSICIANS, INC.

CAP 2020 Financial Reports

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, 2020 and 2019 have been audited by Ernst & Young LLP, independent auditors, as set forth in their reports appearing on pages 7 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 CAP or MPT, 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 management.

This report will be filed with the California Department of Business Oversight.

Graham A. Purcell, MD
Chair
CAP and MPT Audit Committee
March 19, 2021

Report of Independent Auditors

THE BOARD OF DIRECTORS
COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

We have audited the accompanying consolidated financial statements of Cooperative of American Physicians, Inc. and Subsidiaries (the Company), which comprise the consolidated balance sheets as of December 31, 2020 and 2019, 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 consolidated 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 of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit 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 qualified audit opinion.

BASIS FOR QUALIFIED OPINION

The Company has omitted certain disclosures for short-duration insurance contracts that provide information regarding the Company's reserves for losses and loss adjustment expenses. As such, the short-duration insurance contract disclosures do not contain the nature, amount, timing, or uncertainty of future cash flows relating to short-duration insurance contract liabilities as required under U.S. generally accepted accounting principles.

QUALIFIED OPINION

In our opinion, except for the incomplete disclosure of the information referred to in the Basis for Qualified Opinion paragraph, the financial statements present fairly, in all material respects, the consolidated financial position of the Company at December 31, 2020 and 2019, 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.

REQUIRED SUPPLEMENTARY INFORMATION

Management has omitted information related to incurred and paid claims development and the average annual percentage payout of incurred claims that U.S. generally accepted accounting principles require to be presented to supplement the financial statements. Such missing information, although not a part of the financial statements, is required by the Financial Accounting Standards Board who considers it to be an essential part of financial reporting for placing the financial statements in an appropriate operational, economic, or historical context. Our opinion on the financial statements is not affected by this missing information.

San Francisco, California
March 19, 2021

Ernst & Young LLP

Consolidated Balance Sheets

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

	December 31	
	2020	2019
ASSETS		
Cash and cash equivalents	**$ 17,547,000**	$12,617,000
Restricted cash	**11,035,000**	3,215,000
Fixed income securities, at fair value	**53,888,000**	46,694,000
Equity securities, at fair value	**4,024,000**	4,432,000
Income taxes receivable	**62,000**	161,000
Premium receivable	**8,761,000**	15,689,000
Receivables from affiliated entities	**1,616,000**	1,766,000
Receivables for claims and risk management services	**2,885,000**	2,429,000
Deferred acquisition costs	**293,000**	554,000
Other assets	**1,928,000**	2,728,000
	$102,039,000	$90,285,000
LIABILITIES AND MEMBERS' EQUITY		
Liabilities:		
Reserves for losses and loss adjustment expenses	**$ 31,447,000**	$28,809,000
Payables to affiliated entities	**383,000**	657,000
Dues received in advance	**1,203,000**	1,142,000
Deferred tax liabilities, net	**365,000**	304,000
Unearned premiums	**1,563,000**	2,449,000
Unearned claims and risk management services	**4,870,000**	3,880,000
Premiums payable	**20,133,000**	17,858,000
Accounts payable and other liabilities	**9,625,000**	5,393,000
	69,589,000	60,492,000
Contingencies and commitments *(see Note 8)*		
Members' equity:		
Members' equity	**29,793,000**	28,477,000
Accumulated other comprehensive income	**2,657,000**	1,316,000
	32,450,000	29,793,000
	$102,039,000	$90,285,000

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	
	2020	2019
Revenues		
Member and participant dues	**$ 3,356,000**	$ 3,374,000
Claims and risk management service revenues	**41,772,000**	42,982,000
Premiums earned	**17,141,000**	15,187,000
Commissions earned	**2,303,000**	1,982,000
Investment income, net	**1,658,000**	2,211,000
Other revenues	**40,000**	38,000
Total revenues	**66,270,000**	65,774,000
Expenses		
Salaries and related expenses	**32,059,000**	31,285,000
Other operating costs	**17,935,000**	19,637,000
Losses and loss adjustment expenses	**15,019,000**	13,850,000
Total expenses	**65,013,000**	64,772,000
Gain on extinguishment of debt	**1,004,000**	—
Income before income taxes	**2,261,000**	1,002,000
Income tax expense	**(434,000)**	(375,000)
Net income	**1,827,000**	627,000
Other comprehensive income, net		
Net unrealized gains on securities available-for-sale, net of taxes	**830,000**	1,080,000
Comprehensive income	**$ 2,657,000**	$ 1,707,000

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, 2019	$27,869,000	$ 217,000	$28,086,000
Net income	627,000	—	627,000
Cumulative effect of adoption of ASU 2016-01 for equity financial instruments at January 1, 2019	(19,000)	19,000	—
Other comprehensive gains (net of deferred income taxes of $287,000)	—	1,080,000	1,080,000
Balance at December 31, 2019	28,477,000	1,316,000	29,793,000
Net income	**1,827,000**	**—**	**1,827,000**
Other comprehensive gains (net of deferred income taxes of $221,000)	**—**	**830,000**	**830,000**
Balance at December 31, 2020	**$30,304,000**	**$2,146,000**	**$32,450,000**

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 2020	2019
Operating activities		
Net income	**$ 1,827,000**	$ 627,000
Adjustments to reconcile net income to net cash provided by operating activities:		
Net amortization on fixed income securities	**236,000**	164,000
Net realized investment gains	**(87,000)**	(674,000)
Gain on extinguishment of debt	**(1,004,000)**	—
Forgiven interest on Paycheck Protection Program loan	**6,000**	—
Deferred income taxes	**(160,000)**	(72,000)
Changes in operating assets and liabilities:		
Income taxes	**99,000**	333,000
Premiums receivable	**6,928,000**	(223,000)
Receivable from affiliated entities	**150,000**	(192,000)
Receivable for claims and risk management services	**(456,000)**	62,000
Deferred acquisition costs	**261,000**	27,000
Other assets	**800,000**	(953,000)
Reserves for losses and loss adjustment expenses	**2,638,000**	7,348,000
Payable to affiliated entities	**(274,000)**	237,000
Dues received in advance	**61,000**	(46,000)
Unearned premiums	**(886,000)**	(354,000)
Unearned claims and risk management services	**990,000**	905,000
Premiums payable	**2,275,000**	630,000
Accounts payable and other liabilities	**1,338,000**	209,000
Net cash provided by operating activities	**14,742,000**	8,028,000
Investing activities		
Purchases of fixed income and equity securities	**(18,879,000)**	(10,064,000)
Proceeds from sales or maturities of fixed income and equity securities	**12,995,000**	6,054,000
Net cash used in investing activities	**(5,884,000)**	(4,010,000)
Financing activity		
Paycheck Protection Program loans	**3,892,000**	—
Net cash provided by financing activity	**3,892,000**	—
Net change in cash, cash equivalents and restricted cash	**12,750,000**	4,018,000
Cash, cash equivalents and restricted cash at beginning of year	**15,832,000**	11,814,000
Cash, cash equivalents and restricted cash at end of year	**$ 28,582,000**	$ 15,832,000

The following table summarizes the Company's cash, cash equivalents and restricted cash within the consolidated balance sheets:

	December 31 2020	2019
Cash and cash equivalents	**$17,547,000**	$12,617,000
Restricted cash	**11,035,000**	3,215,000
Cash, cash equivalents and restricted cash	**$28,582,000**	$15,832,000

Supplemental disclosure of noncash financing activities:
The Paycheck Protection Program loan was forgiven by the U.S. Small Business Administration in 2020. The amounts forgiven were $998,000 in principal and $6,000 in interest.

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. Members of CAP consist 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 received 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 business trust governed by its Board of Trustees and is not included in the consolidation of CAP and its wholly owned subsidiaries. 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 (former CAPAssurance insurer), 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 CAPAssurance. 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 original purpose of CAPIC was to offer supplemental reinsurance and insurance coverage to its affiliate, MPT, and supplemental insurance coverage to CAP. Over the years, CAPIC changed its licensing status as part of an effort to broaden its product offerings. 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 CAPAssurance insurer and thereby participates in the underwriting results of the CAPAssurance Program. Effective October 2020, the arrangement with the former CAPAssurance insurer was terminated and they were replaced by another national medical professional liability insurance company (CAPAssurance insurer). The terms under the new arrangement did not change. CAPIC has expanded its product offerings to include assumed reinsurance of large physician groups, hospitals, and medical facilities that purchase their medical professional liability insurance through the CAPAssurance Program. Effective December 1, 2015, CAPIC entered into another pro rata reinsurance agreement with the former CAPAssurance insurer that covers policies issued to large physician groups, hospitals, and medical facilities that are not purchased through CAPAssurance. The terms are similar to the original pro rata reinsurance agreement that covers policies purchased through CAPAssurance. Under these reinsurance agreements, 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 former CAPAssurance insurer on these policies are also reimbursed by CAPIC on the same pro rata basis per the terms of these reinsurance agreements. CAPIC amortizes these expenses over the related policy term. These expenses include certain claims administration and other policy services provided by CAP to the former CAPAssurance insurer under the CAPAssurance Program. CAPIC is consolidated in the operations of CAP.

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, 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. CAP Agency is consolidated in the operations of CAP.

Effective January 1, 2010, CAP and MPT entered into an administrative and management services agreement whereby CAP provides membership, claim, risk management, financial, legal 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

NOTE 1: ORGANIZATION *(continued)*

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 10).*

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 CAP State Independent Expenditure Committee and the CAP 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 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, disclosure of assets and liabilities at the date of the financial statements and the reported amounts 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. 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, and funds held in a loss fund pursuant to a claims servicing agreement. 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, excise surplus lines taxes to taxing authorities, and approved loss payments under the claims servicing agreement.

INVESTMENTS

Investments are classified as available-for-sale and are carried at fair value. Unrealized gains and losses for fixed income securities are accounted for, net of tax, as a component of accumulated other comprehensive income in members' equity. Unrealized gains and losses for equity securities are accounted for in operations as a component of investment income, net. 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. 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 are reported as a write-down of cost or amortized cost to fair value.

CONCENTRATIONS 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 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.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

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, income taxes receivable, premiums receivable, receivables from affiliated entities, receivables for claims and risk management services, payables 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 a fair value hierarchy, 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 states and municipalities, corporate bonds, residential mortgage-backed securities, commercial mortgage-backed securities, asset-backed securities and redeemable preferred stocks are based on the observable market information and as such, are included in Level 2 of the hierarchy. Level 1 is limited to unadjusted quoted prices in active markets for identical instruments and includes U.S. Treasury securities and equity securities.

The equity securities are measured at fair value with changes in fair value being recognized in net income.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

The following table presents investments in the accompanying consolidated balance sheets that are stated at fair value and the fair value measurements used as of December 31, 2020 and 2019 *(see Note 3):*

	Total	Level 1	Level 2
DECEMBER 31, 2020			
Fixed income securities:			
States and municipalities	**$19,948,000**	**$ —**	**$19,948,000**
U.S. Treasury obligations	**254,000**	**254,000**	**—**
Corporate bonds	**9,408,000**	**—**	**9,408,000**
Residential mortgage-backed securities	**12,040,000**	**—**	**12,040,000**
Commercial mortgage-backed securities	**8,318,000**	**—**	**8,318,000**
Asset-backed securities	**3,587,000**	**—**	**3,587,000**
Redeemable preferred stock	**333,000**	**—**	**333,000**
Total fixed income securities	**$53,888,000**	**$254,000**	**$53,634,000**
DECEMBER 31, 2019			
Fixed income securities:			
States and municipalities	$15,608,000	$ —	$15,608,000
U.S. Treasury obligations	251,000	251,000	—
Corporate bonds	9,794,000	—	9,794,000
Residential mortgage-backed securities	8,477,000	—	8,477,000
Commercial mortgage-backed securities	5,022,000	—	5,022,000
Asset-backed securities	7,224,000	—	7,224,000
Redeemable preferred stock	318,000	—	318,000
Total fixed income securities	$46,694,000	$251,000	$46,443,000

There were no securities at December 31, 2020 or 2019, whose fair value measurements were based on Level 3: Unobservable inputs.

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 the CAPAssurance insurer *(see Notes 1 and 10).* 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 and corporate legal services, revenues are determined based on actual expenses incurred plus a margin. Services to MPT related solely to membership administration and claim management services are directly charged to MPT after reductions for claims services provided to the CAPAssurance insurer. For all other services provided to MPT under the agreements, the calculation of service revenues 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 and corporate legal service revenues are determined based on actual costs incurred and represent claims legal services provided by CAPIC to MPT physicians and corporate legal defense services provided by CAP to MPT.

The claims and risk management services under the CAPAssurance Program are derived from agreements with the CAPAssurance insurer that became effective in 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 CAPAssurance insurer 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 CAPAssurance insurer 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. These other agreements include pro rata reinsurance agreements between CAPIC and the CAPAssurance insurer. This enables the Company to participate in the

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

underwriting results on insurance policies issued by the CAPAssurance insurer. Accordingly, the Company will not only generate claims and risk management service revenues on policies issued by the CAPAssurance insurer, but will also recognize premiums earned through the reinsurance agreements and dues revenue for any physician and medical facility Participants who purchase benefits from CAP.

CAP recognizes the marketing services revenues under the CAPAssurance Program 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 since 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, which in many cases extends beyond the expiration of the insurance policy. The allocation of service fees between claims administration and policy services is based on the premium percentages for such services as provided for in the underlying agreements. The Company determined these rates to be reasonable by comparing these percentages to the recent historical experience of the CAPAssurance insurer and found such rates comparable. The CAPAssurance insurer 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 or reinsurance contract terms. Premiums under extended reported endorsements are recognized on the effective date of the endorsement.

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 achieving favorable 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.

DEFERRED ACQUISITION COSTS

Costs that vary with and are directly related to the successful production of new and renewal insurance and reinsurance premiums are deferred to the extent they are recoverable against unearned premiums and are amortized as related premiums are earned. These acquisition costs consist mainly of commissions, premium taxes, claims administration costs and other policy administration costs of the ceding company. Future investment income attributable to related premiums is considered in measuring the recoverability of the carrying value of this asset. The amortization of deferred acquisition costs related to claim administration costs is included in losses in the consolidated Statements of Comprehensive Income. All other amortization is included in other operating expenses *(see Note 7).*

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

Under ASU 2015-09, *Financial Services — Insurance (Topic 944): Disclosures about Short-Duration Contracts,* all insurance entities that issue short-duration contracts are required to provide expanded disclosures about the liability for unpaid claims and claim adjustment expenses. These disclosures relate entirely to CAPIC, which is regulated by the Insurance Commissioner of the State of Hawaii.

CAPIC requested permission from the Insurance Commissioner to omit these disclosures from its financial statements as of and for the year ended December 31, 2020. The Insurance Commissioner approved CAPIC's request; therefore, the Company is not including the disclosures as required by ASU 2015-09.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

PREMIUMS RECEIVABLE AND PREMIUMS PAYABLE

CAP Agency and CAP record premiums receivable and payable under its agency billed business 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 are recognized based on billing date as a premium receivable from the physician group or medical facility and a premium payable to the CAPAssurance insurer. Cash received from CAP Agency or CAP billings reduce the premiums receivable and cash payments to the insurance companies reduce the premiums payable. For business where CAP Agency is not obligated to perform billing services, accounts are settled on a cash basis. CAPIC records premiums receivable under insurance policies issued to certain medical group entities or under reinsurance contracts entered into with MPT or the CAPAssurance insurer based on the effective date of the policy or reinsurance contract.

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 services 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 represent the amount of these services fees that relate to either the unexpired policy periods or the unexpired claim payout periods 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 Insurance Commissioner of the State of Hawaii (Insurance Commissioner). At December 31, 2020 and 2019, 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, 2020 or 2019.

INCOME TAXES

CAP and its wholly owned subsidiaries file a consolidated federal income tax return. 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.

COMPREHENSIVE INCOME

Comprehensive income consists of net income and other comprehensive income, net. For the years ended December 31, 2020 and 2019, other comprehensive income, net consists solely of net unrealized gains, net of tax, on fixed income securities classified as available-for-sale. Reclassification adjustments related to those securities for the years ended December 31, 2020 and 2019, were as follows:

	2020	2019
Net realized investment gains included in the calculation of investment income	**$ 4,000**	$ 6,000
Tax effect at 21%	**(1,000)**	(1,000)
Net realized investment gains reclassified from other comprehensive income	**$ 3,000**	$ 5,000

Notes to Consolidated Financial Statements

COOPERATIVE OF AMERICAN PHYSICIANS, INC. AND SUBSIDIARIES

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

NEW ACCOUNTING STANDARDS

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842),* as modified by ASU 2017-03, *Transition and Open Effective Date Information.* Under ASU 2016-02, an entity will be required to recognize assets and liabilities for the rights and obligations created by leases on the entity's balance sheet for both finance and operating leases. For leases with a term of 12 months or less, an entity can elect to not recognize lease assets and lease liabilities and expense the lease over a straight-line basis for the term of the lease. ASU 2016-02 will require new disclosures that depict the amount, timing, and uncertainty of cash flows pertaining to an entity's leases. In June 2020, the FASB issued ASU 2020-05 which postponed the effective date of ASU 2016-02. These updates will be effective for annual reporting periods beginning after December 15, 2021, and may be adopted earlier. The Company has not yet adopted this guidance and has not yet finalized its analysis of how adopting this guidance will impact its financial statements.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments — Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments.* Rather than generally recognizing credit losses when it is probable that the loss has been incurred, the revised guidance requires companies to recognize an allowance for credit losses for the difference between the amortized cost basis of a financial instrument and the amount of amortized cost that the company expects to collect over the instrument's contractual life. In November 2019, the FASB issued ASU 2019-10 which postponed the effective date of ASU 2016-13. This update will be effective for annual reporting periods beginning after December 15, 2022, and may be adopted earlier. The Company has not yet adopted this guidance. The Company is evaluating the effect to its financial statements.

In December 2019, the FASB issued ASU 2019-12, *Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes.* The updated guidance for the accounting of income taxes is intended to simplify the accounting by removing several exceptions contained in existing guidance and amending other existing guidance to simplify several income tax accounting matters. The updated guidance is effective beginning after December 15, 2021. Early adoption is permitted. The adoption of this guidance is not expected to have a material effect on the Company's financial statements.

RECLASSIFICATIONS

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

SUBSEQUENT EVENTS

The Company has completed an evaluation of all subsequent events through March 19, 2021, which is the date the consolidated financial statements were available for issuance, and has concluded that no subsequent events occurred which would require recognition or disclosure.

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, 2020				
Fixed income securities:				
States and municipalities	**$18,761,000**	**$1,189,000**	**$ (2,000)**	**$19,948,000**
U.S. Treasury obligations	**250,000**	**4,000**	**—**	**254,000**
Corporate bonds	**8,953,000**	**455,000**	**—**	**9,408,000**
Residential mortgage-backed securities	**11,710,000**	**334,000**	**(4,000)**	**12,040,000**
Commercial mortgage-backed securities	**7,708,000**	**611,000**	**(1,000)**	**8,318,000**
Asset-backed securities	**3,514,000**	**73,000**	**—**	**3,587,000**
Redeemable preferred stocks	**299,000**	**34,000**	**—**	**333,000**
Total fixed income securities	**$51,195,000**	**$2,700,000**	**$ (7,000)**	**$53,888,000**
DECEMBER 31, 2019				
Fixed income securities:				
States and municipalities	$14,721,000	$ 888,000	$ (1,000)	$15,608,000
U.S. Treasury obligations	250,000	1,000	—	251,000
Corporate bonds	9,523,000	271,000	—	9,794,000
Residential mortgage-backed securities	8,237,000	240,000	—	8,477,000
Commercial mortgage-backed securities	4,869,000	172,000	(19,000)	5,022,000
Asset-backed securities	7,153,000	73,000	(2,000)	7,224,000
Redeemable preferred stocks	299,000	19,000	—	318,000
Total fixed income securities	$45,052,000	$1,664,000	$(22,000)	$46,694,000

The amortized cost and fair value of fixed income securities available-for-sale as of December 31, 2020, 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	$ 2,897,000	$ 2,932,000
Due after one year through five years	8,861,000	9,381,000
Due after five years through ten years	8,380,000	8,996,000
Due after ten years	8,125,000	8,634,000
	28,263,000	29,943,000
Mortgage-backed and asset-backed securities	22,932,000	23,945,000
	$51,195,000	$53,888,000

For the years ended December 31, 2020 and 2019, proceeds from sales of investments were $1,560,000 and $1,509,000, respectively.

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, 2020						
Fixed income securities:						
States and municipalities	**$ 830,000**	**$ (2,000)**	**$ —**	**$ —**	**$ 830,000**	**$ (2,000)**
U.S. Treasury obligations	**—**	**—**	**—**	**—**	**—**	**—**
Corporate bonds	**250,000**	**—**	**—**	**—**	**250,000**	**—**
Residential mortgage-backed securities	**612,000**	**(4,000)**	**—**	**—**	**612,000**	**(4,000)**
Commercial mortgage-backed securities	**960,000**	**(1,000)**	**—**	**—**	**960,000**	**(1,000)**
Asset-backed securities	**—**	**—**	**—**	**—**	**—**	**—**
Redeemable preferred stocks	**—**	**—**	**—**	**—**	**—**	**—**
Total fixed income securities	**$2,652,000**	**$ (7,000)**	**$ —**	**$ —**	**$2,652,000**	**$ (7,000)**
DECEMBER 31, 2019						
Fixed income securities:						
States and municipalities	$ —	$ —	$ 81,000	$(1,000)	$ 81,000	$ (1,000)
U.S. Treasury obligations	—	—	—	—	—	—
Corporate bonds	—	—	—	—	—	—
Residential mortgage-backed securities	206,000	—	—	—	206,000	—
Commercial mortgage-backed securities	1,022,000	(19,000)	56,000	—	1,078,000	(19,000)
Asset-backed securities	1,056,000	(1,000)	849,000	(1,000)	1,905,000	(2,000)
Redeemable preferred stocks	—	—	—	—	—	—
Total fixed income securities	$2,284,000	$(20,000)	$986,000	$(2,000)	$3,270,000	$(22,000)

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, 2020 and 2019, none of the Company's investments, whose estimated fair values were less than amortized cost, were considered to be other-than-temporarily impaired given the severity and duration of the impairment and the credit quality of the issuers. 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.

NOTE 3: INVESTMENTS *(continued)*

Investment income, net is summarized as follows:

	Years Ended December 31	
	2020	2019
Interest and dividend income	**$1,866,000**	$1,747,000
Net realized gains, fixed income securities	**20,000**	7,000
Net realized gains, equity securities	**640,000**	5,000
Change in unrealized (losses) gains, equity securities	**(573,000)**	662,000
Investment management fees and expenses	**(59,000)**	(46,000)
Net amortization of premium on fixed income securities	**(236,000)**	(164,000)
Investment income, net	**$1,658,000**	$2,211,000

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	
	2020	2019
Reserves for losses and loss adjustment expenses net of reinsurance recoverables at beginning of year	**$ 28,459,000**	$21,461,000
Incurred related to:		
Current year	**18,858,000**	15,684,000
Prior years	**(3,839,000)**	(1,834,000)
Total incurred	**15,019,000**	13,850,000
Paid related to:		
Current year	**(2,947,000)**	(1,825,000)
Prior years	**(8,134,000)**	(5,027,000)
Total paid	**(11,081,000)**	(6,852,000)
Unpaid claims liability and reserves for losses and loss adjustment expenses net of reinsurance recoverables at end of year	**32,397,000**	28,459,000
Less: Unpaid claims liability	**(1,300,000)**	—
Add: Reinsurance recoverables on unpaid losses and loss adjustment expenses at end of year	**350,000**	350,000
Reserves for losses and loss adjustment expenses gross of reinsurance recoverables on unpaid losses and loss adjustment expenses at end of year	**$ 31,447,000**	$28,809,000

$1,300,000 of the $15,019,000 in incurred losses was for a claim on a claims-paid policy form. As such, $1,300,000 is reclassified out of Reserves for losses and loss adjustment expenses and booked as Other liabilities.

NOTE 4: RESERVES FOR LOSSES AND LOSS ADJUSTMENT EXPENSES *(continued)*

For the years ended December 31, 2020 and 2019, the provision for losses and loss adjustment expenses for the prior years decreased by $3,839,000 and $1,834,000, respectively. The claims-made years impacted by the provision for losses and loss adjustment expenses for prior years are as follows:

	Prior Claims-Made Years' Provision for Losses and Loss Adjustment Expense for Years Ended December 31	
Claims-Made Year	**2020**	2019
2019	**$(2,194,000)**	$ —
2018	**504,000**	(1,427,000)
2017	**(1,869,000)**	(289,000)
2016	**(240,000)**	(44,000)
2015	**86,000**	140,000
2014	**(93,000)**	(79,000)
2013	**(33,000)**	40,000
2012	**—**	(6,000)
2011	**—**	(19,000)
2010	**—**	(150,000)
	$(3,839,000)	$(1,834,000)

For the year ended December 31, 2020, CAPIC experienced favorable development of $4,429,000 due to lower than expected claims severity from 2013 through 2019, with the exception of claims-made years 2015 and 2018 where CAPIC experienced adverse development amounting to $86,000 and $504,000, respectively. For the year ended December 31, 2019, CAPIC recognized favorable development of $2,014,000 due to lower than expected claims severity from 2010 through 2012, 2014, and from the 2016 through 2018 claims-made years. This was offset by adverse development due to higher than expected claims frequency from the 2013 and 2015 claims-made years.

NOTE 5: PAYCHECK PROTECTION PROGRAM

In April 2020, CAP and CAPIC entered into a $2,894,000 and $998,000 note payable with the Bank of Hawaii pursuant to the Paycheck Protection Program under the Coronavirus Aid, Relief, and Economic Security Act. Both, CAP and CAPIC, applied for loan forgiveness. CAPIC's loan was forgiven in December 2020 and CAP's loan is still under review by the Small Business Administration (SBA). The interest rate on the note payable is 1%. CAP has been informed by the lender that no repayments are due until the SBA has made a determination about loan forgiveness. As such, it is difficult to determine what amounts, if any, will have to be repaid to the lender in 2021 and 2022. The balance outstanding, along with the accrued interest, is $2,914,000.

NOTE 6: REINSURANCE

CAPIC is involved in the assumption of reinsurance to share risk with insureds. CAPIC also purchases reinsurance from non-affiliated insurers to reduce its net exposure to losses. The following table presents the effect of reinsurance on short-duration insurance premiums written and earned:

	Years Ended December 31	
	2020	2019
Premiums written:		
Direct	**$ 2,923,000**	$ 2,601,000
Assumed	**13,368,000**	12,295,000
Ceded	**(45,000)**	(69,000)
Total written	**$16,246,000**	$14,827,000
Premiums earned:		
Direct	**$ 2,987,000**	$ 2,593,000
Assumed	**14,227,000**	12,657,000
Ceded	**(73,000)**	(63,000)
Total earned	**$17,141,000**	$15,187,000

CAPIC assumes reinsurance on a pro rata basis with the CAPAssurance insurer as part of the CAPAssurance Program *(see Note 1).* Under the agreements, CAPIC participates on a pro rata basis in the first $1,000,000 of exposure on medical professional liability policies at rates that vary based on the type of insured covered by the policies *(see Note 8).*

Effective January 1, 2016, CAPIC entered into a reinsurance agreement with HAPI relating to physician medical professional liability coverage. Under the agreement, CAPIC assumes a 10% share of up to $4,700,000 in loss and defense costs in excess of $300,000 on a per claim basis. CAPIC's participation begins after the application of an aggregate deductible calculated at 12% of developed reinsurance premium.

Effective July 1, 2016, CAPIC entered into a reinsurance contract with the former CAPAssurance insurer on a pro rata basis that covers certain direct policies of medical professional liability coverage issued by CAPIC to healthcare facilities owned by physicians who are also members of HAPI. The receivable from the reinsurer on unpaid losses and loss adjustment expenses represents management's estimate of amounts that will be recoverable under this agreement. Given the uncertainty of the ultimate amounts of losses, management's estimates of losses and loss adjustment expenses recoverable may vary materially from the eventual outcome. Reinsurance contracts do not relieve CAPIC from its obligations to policyholders and CAPIC remains liable to its policyholders whether or not the reinsurer honors its contractual obligations. CAPIC recognized reinsurance recoveries of $10,000 and $350,000 under this contract for years ended December 31, 2020 and 2019, respectively. As of December 31, 2020 and 2019, the total amounts due to the reinsurer under this contract for reinsurance premiums were $0 and $28,000, respectively. For the years ended December 31, 2020 and 2019, no reinsurance balances were written off for credit reasons.

NOTE 7: AMORTIZATION OF DEFERRED ACQUISITION COSTS

Acquisition costs under reinsurance and insurance contracts are deferred to the extent they are recoverable against unearned premiums and are amortized as related premiums are earned. The amortization of deferred acquisition costs that is included in other operating expenses totals $164,000 and $583,000 for the years ended December 31, 2020 and 2019, respectively *(see Note 2).*

NOTE 8: CONTINGENCIES AND COMMITMENTS

The Company is subject to other 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 consolidated financial position.

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 $3,107,000 and $3,030,000 for the years ended December 31, 2020 and 2019, respectively. The future minimum rental commitments under these operating leases are as follows:

Years Ending December 31	Amount
2021	$2,329,000
2022	2,421,000
2023	2,436,000
2024	598,000
2025 and after	581,000
	$8,365,000

Effective in January 2018, CAPIC established a standby letter of credit facility with a major bank that allows for letters of credit to be issued to designated persons or entities. The purpose of the facility is to secure certain reinsurance obligations of CAPIC to the former CAPAssurance insurer under reinsurance agreements established as part of the CAPAssurace Program *(see Notes 1, 2 and 6).* The maximum amount available under the facility for all standby letters of credit issued collectively is $15,208,000. The facility is collateralized by CAPIC's investment portfolio and an annual fee is charged to maintain the facility. Any drawings made under issued and active letters of credit bear interest at the bank's prime rate plus a margin. As of December 31, 2020, no drawings under this letter of credit have been made. Accordingly, there was no interest expense incurred under this facility for the year ended December 31, 2020.

NOTE 9: INCOME TAXES

The components of the income tax expense are as follows:

	Years Ended December 31	
	2020	2019
Current	**$(594,000)**	$(447,000)
Deferred	**160,000**	72,000
Total	**$(434,000)**	$(375,000)

NOTE 9: INCOME TAXES *(continued)*

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 2020	2019
Federal income tax expense at 21%	**$(475,000)**	$(211,000)
Adjustments in taxes resulting from:		
State income tax expense (net of federal effect)	**(187,000)**	(175,000)
Paycheck Protection Program loan forgiveness	**212,000**	—
Employee benefit plan	**3,000**	2,000
Tax effect of PAC Committee's reimbursement for taxes	**(36,000)**	(38,000)
Non-deductible lobbying and political expenses	**(6,000)**	—
Tax-exempt investment income	**62,000**	63,000
Meals, entertainment and club dues exclusion	**(5,000)**	(9,000)
Employer paid parking	**(8,000)**	(13,000)
Preferred stock: eligible dividends received deduction	**6,000**	6,000
Total income tax expense	**$(434,000)**	$(375,000)

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

	December 31 2020	2019
Deferred tax assets:		
Discounting of reserves for losses and loss adjustment expenses	**$ 425,000**	$ 373,000
Discounting transition adjustment pursuant to the Tax Cuts and Jobs Act	**22,000**	26,000
Employee benefit obligations	**199,000**	150,000
Charitable contributions carryovers	**—**	48,000
State taxes	**37,000**	36,000
Unearned premiums	**66,000**	103,000
Other items	**4,000**	6,000
Deferred tax assets	**753,000**	742,000
Deferred tax liabilities:		
Unrealized gains on fixed income securities	**(565,000)**	(345,000)
Unrealized gains on equity securities	**(19,000)**	(139,000)
State tax on unremitted earnings of subsidiaries	**(271,000)**	(254,000)
Accretion of bond discount	**(146,000)**	(133,000)
Deferred acquisition costs	**(117,000)**	(175,000)
Deferred tax liabilities	**(1,118,000)**	(1,046,000)
Deferred tax liabilities, net	**$ (365,000)**	$ (304,000)

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.

As of December 31, 2020, there remain no federal net operating loss carryforwards.

Income taxes paid for the years ended December 31, 2020 and 2019 were $495,000 and $289,000, respectively. There were no penalties on tax amounts paid in either year ended December 31, 2020 or 2019.

NOTE 9: INCOME TAXES *(continued)*

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, 2020 and 2019, the Company had no uncertain tax positions.

Tax years 2017 through 2019 and tax years 2016 through 2019 are subject to examination by the federal and California taxing authorities, respectively.

NOTE 10: RELATED-PARTY TRANSACTIONS

CAP and MPT operate under an administrative and management services agreement whereby CAP provides membership, claims, risk management, financial, legal 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. The margin applies to all services, except corporate legal, whose services are provided to MPT at cost. For the years ended December 31, 2020 and 2019, CAP agreed to waive the margin. Total revenues of $24,251,000 and $23,575,000 for the years ended December 31, 2020 and 2019, respectively, recognized from MPT for administrative and management services under the agreement are included in claims and risk management service revenues in the consolidated statements of comprehensive income. Expenses related to these agreements are included in salaries and related expenses totaling $17,572,000 and $16,967,000 for the years ended December 31, 2020 and 2019, respectively, and in other operating costs totaling $6,279,000 and $6,608,000 for the years ended December 31, 2020 and 2019, respectively.

Effective January 1, 2013, CAPIC and MPT entered into a services agreement whereby CAPIC provides claims legal defense services to MPT physicians. Under the CAPAssurance Program, claims legal defense services are also provided to the CAPAssurance insurer. CAPIC receives monthly fees for these services that are based on actual costs incurred. Claims services fees recognized under this agreement were $15,889,000 and $17,886,000 for the years ended December 31, 2020 and 2019, respectively. Included in the receivable from affiliated entities is $1,725,000 and $1,853,000 due from MPT for these services as of December 31, 2020 and 2019, respectively.

In 2020 and 2019, CAPIC had reinsurance contracts with MPT. These contracts principally provide per claim excess of loss reinsurance coverage on a claims-made form for claims reported in 2020 and 2019. 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 $5,500,000 and $4,000,000 for the years ended December 31, 2020 and 2019, 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 $230,000 and $228,000 for the years ended December 31, 2020 and 2019, respectively. For the years ended December 31, 2020 and 2019, total affiliate reinsurance premium income under all reinsurance contracts with MPT was $5,707,000 and $4,206,000, respectively.

CAP provides its Members and Participants defense coverage for medical board actions with a $25,000 limit and employment practice defense coverage with a $50,000 limit. CAPIC provides insurance coverage to CAP for these benefits. MPT reimburses CAP for a significant portion of the cost of this coverage. CAP paid CAPIC $2,887,000 and $2,521,000 for the years ended December 31, 2020 and 2019, respectively, for this coverage, of which MPT reimbursed CAP $2,830,000 and $2,462,000 for the same respective years.

NOTE 10: RELATED-PARTY TRANSACTIONS *(continued)*

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 $817,000 and $767,000 for the years ended December 31, 2020 and 2019, 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.

MUTUAL PROTECTION TRUST

MPT 2020 Financial Reports

Report of Independent Auditors

THE 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, 2020 and 2019, and the related statements of operations, 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 of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit 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, 2020 and 2019, 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 financial 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, except for that portion marked "unaudited," has been subjected to the auditing procedures applied in the audits 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 of America. In our opinion, the information, except for that portion marked "unaudited" on which we express no opinion, is fairly stated, in all material respects, in relation to the financial statements as a whole.

San Francisco, California
March 19, 2021

Ernst + Young LLP

Balance Sheets

MUTUAL PROTECTION TRUST

	December 31 2020	December 31 2019
ASSETS		
Trust fund corpus, restricted:		
Fixed income securities, available-for-sale, at fair value	$141,851,000	$139,174,000
Cash and cash equivalents	4,392,000	2,798,000
Accrued interest receivable	646,000	867,000
Deferred tax liability	(1,482,000)	(654,000)
	145,407,000	142,185,000
***Trust fund operating accounts*:**		
Fixed income securities, available-for-sale, at fair value	74,002,000	71,502,000
Cash and cash equivalents	32,238,000	23,545,000
Assessments, dues and other coverages receivable	87,940,000	89,782,000
Fixed assets and intangibles, net	1,544,000	1,597,000
Deferred tax asset, net	4,328,000	7,754,000
Income taxes receivable	760,000	403,000
Other assets	29,364,000	28,230,000
	230,176,000	222,813,000
	$375,583,000	$364,998,000
LIABILITIES		
Trust fund operating accounts:		
Non-assessable former members' liability	$ 38,332,000	$ 36,994,000
Unpaid claims and expenses	18,318,000	16,701,000
Deferred assessments, dues and other coverages	122,343,000	117,647,000
Payable to affiliated entity	1,613,000	1,749,000
Other liabilities	24,916,000	25,295,000
	205,522,000	198,386,000
Contingencies and commitments *(see Notes 5 and 9)*		
MEMBERS' EQUITY		
Trust fund corpus, including accumulated other comprehensive gain of $5,577,000 and $2,462,000 for 2020 and 2019, respectively	145,407,000	142,185,000
Trust fund operations	24,654,000	24,427,000
	170,061,000	166,612,000
	$375,583,000	$364,998,000

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

Statements of Operations

MUTUAL PROTECTION TRUST

	Years Ended December 31	
	2020	2019
Assessments and dues	$102,986,000	$114,739,000
Revenues		
Investment income:		
Interest income, net	5,249,000	6,473,000
Realized gains (losses)	358,000	(466,000)
Investment income, net	5,607,000	6,007,000
Other coverage fees	13,738,000	13,893,000
Total assessments, dues and revenues	122,331,000	134,639,000
Expenses		
Claims costs:		
Indemnity expense	46,932,000	49,274,000
Defense and investigative services	27,217,000	35,738,000
Salaries and related expenses	5,237,000	5,185,000
Other operating costs	14,472,000	13,044,000
	93,858,000	103,241,000
General and administrative:		
Salaries and related expenses	14,156,000	12,769,000
Other operating costs	12,686,000	13,348,000
	26,842,000	26,117,000
Total expenses	120,700,000	129,358,000
Excess of assessments, dues and revenues over expenses before income taxes	1,631,000	5,281,000
Income tax (expense) benefit	(2,720,000)	370,000
Net (deficit) excess of assessments, dues and revenues over expenses	(1,089,000)	5,651,000
Other comprehensive gain, net		
Net unrealized gains on securities available-for-sale, net of taxes	4,431,000	5,615,000
Net change in members' equity through operations	$ 3,342,000	$ 11,266,000

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 (Loss)	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, 2019	$16,890,000	$140,282,000	$(1,267,000)	$(14,414,000)	$13,760,000	$138,361,000	$155,251,000
Corpus activity:							
Additions	—	8,418,000	—	(8,418,000)	—	—	—
Payments on deferred contracts receivable	—	—	—	7,031,000	—	7,031,000	7,031,000
Repayments	—	—	—	—	(6,049,000)	(6,049,000)	(6,049,000)
Contributions relinquished	—	(887,000)	—	—	—	(887,000)	(887,000)
Transfers of corpus	—	(6,443,000)	—	—	6,443,000	—	—
Net excess of assessments, dues and revenues over expenses	5,651,000	—	—	—	—	—	5,651,000
Other comprehensive gains (net of deferred income taxes of $1,493,000)	1,886,000	—	3,729,000	—	—	3,729,000	5,615,000
Balance at December 31, 2019	24,427,000	141,370,000	2,462,000	(15,801,000)	14,154,000	142,185,000	166,612,000
Corpus activity:							
Additions	**—**	**7,511,000**	**—**	**(7,511,000)**	**—**	**—**	**—**
Payments on deferred contracts receivable	**—**	**—**	**—**	**7,520,000**	**—**	**7,520,000**	**7,520,000**
Repayments	**—**	**—**	**—**	**—**	**(6,535,000)**	**(6,535,000)**	**(6,535,000)**
Contributions relinquished	**—**	**(878,000)**	**—**	**—**	**—**	**(878,000)**	**(878,000)**
Transfers of corpus	**—**	**(6,481,000)**	**—**	**—**	**6,481,000**	**—**	**—**
Net deficit of assessments, dues and revenues over expenses	**(1,089,000)**	**—**	**—**	**—**	**—**	**—**	**(1,089,000)**
Other comprehensive gains (net of deferred income taxes of $1,178,000)	**1,316,000**	**—**	**3,115,000**	**—**	**—**	**3,115,000**	**4,431,000**
Balance at December 31, 2020	**$24,654,000**	**$141,522,000**	**$ 5,577,000**	**$(15,792,000)**	**$14,100,000**	**$145,407,000**	**$170,061,000**

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

Statements of Cash Flows

MUTUAL PROTECTION TRUST

	Years Ended December 31	
	2020	2019
Operating activities		
Net (deficit) excess of assessments, dues and revenues over expenses	**$ (1,089,000)**	$ 5,651,000
Adjustments to reconcile net (deficit) excess of assessments, dues and revenues over expenses to net cash provided by operating activities:		
Depreciation and amortization	**440,000**	446,000
Amortization on fixed income securities	**1,418,000**	1,067,000
Net realized investment (gains) losses	**(358,000)**	466,000
Deferred income taxes	**3,076,000**	712,000
Decrease in lease incentive obligation	**(448,000)**	(361,000)
Changes in operating assets and liabilities:		
Accrued interest receivable	**221,000**	(30,000)
Assessments, dues and other coverages receivable	**1,842,000**	(1,619,000)
Income taxes receivable	**(357,000)**	(367,000)
Other assets	**(1,134,000)**	(7,835,000)
Non-assessable former members' liability	**1,338,000**	3,389,000
Unpaid claims and expenses	**1,617,000**	4,145,000
Deferred assessments, dues and other coverages	**4,696,000**	(830,000)
Payable to affiliated entity	**(136,000)**	188,000
Other liabilities	**69,000**	2,113,000
Net cash provided by operating activities	**11,195,000**	7,135,000
Investing activities		
Fixed income securities available-for-sale:		
Purchases	**(68,541,000)**	(75,523,000)
Sales and maturities	**67,913,000**	71,547,000
Net additions to fixed assets and intangibles	**(387,000)**	(1,035,000)
Net cash used in investing activities	**(1,015,000)**	(5,011,000)
Financing activities		
Additions to Trust fund corpus	**7,520,000**	7,031,000
Repayments of Trust fund corpus	**(7,413,000)**	(6,936,000)
Net cash provided by financing activities	**107,000**	95,000
Net change in cash and cash equivalents	**10,287,000**	2,219,000
Cash and cash equivalents at beginning of year		
Trust fund corpus	**2,798,000**	3,078,000
Trust fund operations	**23,545,000**	21,046,000
	26,343,000	24,124,000
Cash and cash equivalents at end of year		
Trust fund corpus	**4,392,000**	2,798,000
Trust fund operations	**32,238,000**	23,545,000
	$ 36,630,000	$ 26,343,000

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 a business trust 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, 2020, will receive the return of their Initial trust contributions aggregating $14,100,000, in accordance with the provisions of the MPT Agreement through the year 2030. 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 and dues 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 and dues 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 and dues.

Revenues are primarily comprised of other coverage fees, finance charges and net investment income. Assessments, dues and revenues are used to pay legally binding final judgments and settlements against MPT members, claims defense and investigative expenses, 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, 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.

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 2020 and 2019, MPT levied $112,635,000 and $112,410,000 in member assessments, respectively. The following table reconciles the assessments levied in November 2019 and 2018 to the assessments recognized in the Statements of Operations:

	Years Ended December 31	
	2020	2019
Assessment levied in November of the preceding year	**$112,410,000**	$110,829,000
Assessment refund	**(4,701,000)**	—
November 2018 assessments transferred to 2019	**—**	6,000,000
November 2019 assessments transferred to 2020	**3,000,000**	(3,000,000)
November 2020 assessments transferred to 2021	**(9,000,000)**	—
Net adjustments to member assessments during the year	**94,000**	(274,000)
Dues recognized	**1,183,000**	1,184,000
Assessments and dues recognized in the Statements of Operations	**$102,986,000**	$114,739,000

In April 2020, the Board of Trustees approved a return of $4,701,000 in assessment funds to the members of record as of April 15, 2020. In addition to the assessments levied in November 2020 and 2019, the Board of Trustees also established annual dues of $190 per active member. In the November 2020 and 2019 assessment, approximately $544,000 and $1,113,000, respectively, 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. From the dues levied in 2020, the Board of Trustees directed that the residual dues of $1,750,000 be used for reimbursement to MPT for the advance made to Californians Allied for Patient Protection (CAPP). From the dues levied in 2019, the Board of Trustees directed that the residual dues remain in MPT and be used to offset operating costs in 2020. Total residual dues of $1,159,000 were included in deferred assessments, dues, and other coverages as of December 31, 2019, and none for December 31, 2020. Amounts contributed to the 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 and totaled $544,000 and $1,113,000 as of December 31, 2020 and 2019, respectively.

REVENUES

Other coverage fees and finance charges 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 IN MEMBERS' EQUITY

Net increase in members' equity consists of net (deficit) excess of assessments, dues and revenues over expenses and other comprehensive gain. MPT does not report total comprehensive income or loss since its statutory authority precludes the Board of Trustees from assessing MPT's members for anything other than operating needs. Assessments and dues are not revenues as they are levied by the Board of Trustees solely to support such operating needs. Accordingly, there is no net income or loss, or total comprehensive income or loss. Any excess of assessments, dues and revenues over expenses are the property of MPT members *(see Note 1).* Other comprehensive gain refers to gains and losses that are not included in net (deficit) excess of assessments, dues and revenues over expenses, but rather are recorded directly in members' equity. For the years ended December 31, 2020 and 2019, the net increase in members'

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

equity consists of net (deficit) excess of assessments, dues and revenues over expenses and unrealized gains on securities classified as available-for-sale.

Reclassification adjustments related to available-for-sale securities for the years ended December 31, 2020 and 2019 were as follows:

	2020	2019
Net realized investment gains included in the calculation of investment income, net	$107,000	$227,000
Tax effect (at 21%)	(23,000)	(48,000)
Net realized investment gains reclassified from other comprehensive gain (loss)	$ 84,000	$179,000

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. 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 on an accrual basis. Premiums and discounts on investment securities are 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 are reported as a write-down of amortized cost to fair value.

CONCENTRATIONS 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 12,000 that comprise the total receivable.

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)*.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

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, Income Taxes Receivable, Payable to Affiliated Entity. 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 a fair value hierarchy, 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 values of states and municipalities, corporate bonds, residential mortgage-backed securities and commercial mortgage-backed securities are based on the observable market information and as such, are included in Level 2 of the hierarchy. Level 1 is limited to unadjusted quoted prices in active markets for identical instruments and includes, for example, U.S. Treasury securities.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

The following table presents investments in the accompanying balance sheets that are stated at fair value and the fair value measurements used as of December 31, 2020 *(see Note 3):*

	Total	Level 1	Level 2
DECEMBER 31, 2020			
Trust Fund Corpus, restricted:			
Fixed income securities			
States and municipalities	$ 40,845,000	$—	$ 40,845,000
Corporate bonds	30,223,000	—	30,223,000
Residential mortgage-backed securities	61,342,000	—	61,342,000
Commercial mortgage-backed securities	9,441,000	—	9,441,000
Total fixed income securities	$141,851,000	$—	$141,851,000
Trust Fund Operating:			
Fixed income securities			
States and municipalities	$ 15,081,000	$—	$ 15,081,000
Corporate bonds	18,603,000	—	18,603,000
Residential mortgage-backed securities	34,851,000	—	34,851,000
Commercial mortgage-backed securities	5,467,000	—	5,467,000
Total fixed income securities	$ 74,002,000	$—	$ 74,002,000

All investments on the accompanying balance sheet as of December 31, 2019, are stated at fair value and are considered Level 2 investments.

There were no securities at December 31, 2020 or 2019, whose fair value measurements were based on Level 1 or Level 3 inputs.

Other Assets. Included in other assets are mutual fund investments used to fund SERP and NDCP obligations *(see Note 7).* The carrying amounts for these mutual fund investments in the accompanying balance sheets are stated at fair value, totaling $4,254,000 and $3,914,000 at December 31, 2020 and 2019, respectively.

ASSESSMENTS, DUES AND OTHER COVERAGES RECEIVABLE

Assessments, dues and other coverages receivable is primarily composed of assessments and dues levied by the Board of Trustees. Assessments and dues are recorded as a receivable at the time the MPT member becomes legally obligated to pay such assessments and dues under the MPT Agreement. This occurs at the time assessments and dues are levied by the Board of Trustees, which traditionally occurs in November.

FIXED ASSETS AND INTANGIBLES, NET

Fixed assets and intangibles consist of the following:

	December 31	
	2020	2019
Software	$ 1,417,000	$ 1,290,000
Computer equipment	4,692,000	4,474,000
Document imaging	620,000	620,000
Leasehold improvements	3,851,000	3,851,000
Furniture and equipment	4,293,000	4,251,000
	14,873,000	14,486,000
Accumulated amortization and depreciation	(13,329,000)	(12,889,000)
Fixed assets and intangibles, net	$ 1,544,000	$ 1,597,000

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

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

The costs incurred with respect to the preliminary project stage are expensed in the period incurred. Costs related to application development stages are tracked separately and capitalized. Finally, costs related to the post-implementation stage are expensed in the period incurred unless such costs are incurred to modify the software's functionality significantly.

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 2016, the FASB issued ASU 2016-02, *Leases (Topic 842),* as modified by ASU 2017-03, *Transition and Open Effective Date Information.* Under ASU 2016-02, an entity will be required to recognize assets and liabilities for the rights and obligations created by leases on the entity's balance sheet for both finance and operating leases. For leases with a term of 12 months or less, an entity can elect to not recognize lease assets and lease liabilities and expense the lease over a straight-line basis for the term of the lease. ASU 2016-02 will require new disclosures that depict the amount, timing, and uncertainty of cash flows pertaining to an entity's leases. In June 2020, the FASB issued ASU 2020-05 which postponed the effective date of ASU 2016-02. These updates will be effective for annual reporting periods beginning after December 15, 2021 and may be adopted earlier. MPT has not yet adopted this guidance and has not yet finalized its analysis of how adopting this guidance will impact its financial statements.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments — Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments.* Rather than generally recognizing credit losses when it is probable that the loss has been incurred, the revised guidance requires companies to recognize an allowance for credit losses for the difference between the amortized cost basis of a financial instrument and the amount of amortized cost that the company expects to collect over the instrument's contractual life. In November 2019, the FASB issued ASU 2019-10 which postponed the effective date of ASU 2016-13. This update will be effective for annual reporting periods beginning after December 15, 2022, and may be adopted earlier. MPT has not yet adopted this guidance. MPT is evaluating the effect to its financial statements.

In August 2018, the FASB issued ASU 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework — Changes to the Disclosure Requirements for Fair Value Measurement.* In this update, the FASB issued guidance that eliminates and modifies certain disclosure requirements related to fair value measurements. The new guidance eliminates the requirements to disclose the transfers between Level 1 and Level 2 of the fair value hierarchy, the policy for the timing of transfers between levels of the fair value hierarchy, the valuation processes for Level 3 fair value measurements and the changes in unrealized gains and losses for the period included in earnings for recurring Level 3 fair value measurements held at the end of the reporting period while it modifies existing disclosure requirements related to measurement uncertainty, the requirement to disclose the timing of liquidation of an investee's assets for investments in certain entities that calculate net asset value and the requirement to disclose transfers into and out of Level 3 of the fair value hierarchy and purchases and issues of Level 3 assets and liabilities. ASU 2018-13 is effective for reporting periods beginning after December 15, 2019. Adopting this guidance did not have a material effect on MPT's financial statements.

In December 2019, the FASB issued ASU 2019-12, *Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes.* The updated guidance for the accounting of income taxes is intended to simplify the accounting by removing several exceptions contained in existing guidance and amending other existing guidance to simplify several income tax accounting matters. The updated guidance is effective beginning after December 15, 2021. Early adoption is permitted. The adoption of this guidance is not expected to have a material effect on MPT's financial statements.

SUBSEQUENT EVENTS

MPT has completed an evaluation of all subsequent events through March 19, 2021, 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, 2020				
Trust Fund Corpus, restricted:				
Fixed income securities, available-for-sale				
States and municipalities	$ 38,357,000	$2,490,000	$ (2,000)	$ 40,845,000
Corporate bonds	28,424,000	1,800,000	(1,000)	30,223,000
Residential mortgage-backed securities	58,839,000	2,514,000	(11,000)	61,342,000
Commercial mortgage-backed securities	9,172,000	302,000	(33,000)	9,441,000
Total fixed income securities	$134,792,000	$7,106,000	$(47,000)	$141,851,000
Trust Fund Operating:				
Fixed income securities, available-for-sale				
States and municipalities	$ 14,233,000	$ 848,000	$ —	$ 15,081,000
Corporate bonds	17,675,000	929,000	(1,000)	18,603,000
Residential mortgage-backed securities	33,516,000	1,335,000	—	34,851,000
Commercial mortgage-backed securities	5,327,000	150,000	(10,000)	5,467,000
Total fixed income securities	$ 70,751,000	$3,262,000	$(11,000)	$ 74,002,000

NOTE 3: INVESTMENTS *(continued)*

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
DECEMBER 31, 2019				
Trust Fund Corpus, restricted:				
Fixed income securities, available-for-sale				
States and municipalities	$ 31,076,000	$ 859,000	$ (94,000)	$ 31,841,000
Corporate bonds	34,587,000	1,117,000	(5,000)	35,699,000
Residential mortgage-backed securities	68,361,000	1,245,000	(119,000)	69,487,000
Commercial mortgage-backed securities	2,034,000	113,000	—	2,147,000
Total fixed income securities	$136,058,000	$3,334,000	$(218,000)	$139,174,000
Trust Fund Operating:				
Fixed income securities, available-for-sale				
States and municipalities	$ 10,632,000	$ 263,000	$ (18,000)	$ 10,877,000
Corporate bonds	17,105,000	514,000	(3,000)	17,616,000
Residential mortgage-backed securities	41,163,000	812,000	(40,000)	41,935,000
Commercial mortgage-backed securities	1,017,000	57,000	—	1,074,000
Total fixed income securities	$ 69,917,000	$1,646,000	$ (61,000)	$ 71,502,000

The amortized cost and fair value of fixed income securities available-for-sale as of December 31, 2020, 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
Trust Fund Corpus, restricted:		
Due in one year or less	$ 7,886,000	$ 8,081,000
Due after one year through five years	23,405,000	24,482,000
Due after five years through ten years	26,822,000	29,021,000
Due after ten years	8,668,000	9,484,000
	66,781,000	71,068,000
Residential mortgage-backed securities	58,839,000	61,342,000
Commercial mortgage-backed securities	9,172,000	9,441,000
	$134,792,000	$141,851,000
Trust Fund Operating:		
Due in one year or less	$ 1,596,000	$ 1,610,000
Due after one year through five years	13,037,000	13,527,000
Due after five years through ten years	13,003,000	13,945,000
Due after ten years	4,272,000	4,602,000
	31,908,000	33,684,000
Residential mortgage-backed securities	33,516,000	34,851,000
Commercial mortgage-backed securities	5,327,000	5,467,000
	$ 70,751,000	$ 74,002,000

For the years ended December 31, 2020 and 2019, proceeds from sales of investments were $25,646,000 and $47,004,000, respectively.

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, 2020						
Trust Fund Corpus, restricted:						
Fixed income securities						
States and municipalities	**$1,664,000**	**$ (2,000)**	**$ —**	**$ —**	**$1,664,000**	**$ (2,000)**
Corporate bonds	**1,325,000**	**(1,000)**	**—**	**—**	**1,325,000**	**(1,000)**
Mortgage-backed securities	**5,246,000**	**(44,000)**	**—**	**—**	**5,246,000**	**(44,000)**
Total fixed income securities	**$8,235,000**	**$(47,000)**	**$ —**	**$ —**	**$8,235,000**	**$(47,000)**
Trust Fund Operating:						
Fixed income securities						
States and municipalities	**$ —**	**$ —**	**$ —**	**$ —**	**$ —**	**$ —**
Corporate bonds	**1,641,000**	**(1,000)**	**—**	**—**	**1,641,000**	**(1,000)**
Mortgage-backed securities	**3,079,000**	**(10,000)**	**—**	**—**	**3,079,000**	**(10,000)**
Total fixed income securities	**$4,720,000**	**$(11,000)**	**$ —**	**$ —**	**$4,720,000**	**$(11,000)**
DECEMBER 31, 2019						
Trust Fund Corpus, restricted:						
Fixed income securities						
States and municipalities	$ 7,397,000	$ (94,000)	$ —	$ —	$ 7,397,000	$ (94,000)
Corporate bonds	897,000	(5,000)	—	—	897,000	(5,000)
Mortgage-backed securities	5,574,000	(53,000)	8,166,000	(66,000)	13,740,000	(119,000)
Total fixed income securities	$13,868,000	$(152,000)	$8,166,000	$(66,000)	$22,034,000	$(218,000)
Trust Fund Operating:						
Fixed income securities						
States and municipalities	$ 2,778,000	$ (18,000)	$ —	$ —	$ 2,778,000	$ (18,000)
Corporate bonds	522,000	(3,000)	—	—	522,000	(3,000)
Mortgage-backed securities	2,889,000	(24,000)	2,622,000	(16,000)	5,511,000	(40,000)
Total fixed income securities	$ 6,189,000	$ (45,000)	$2,622,000	$(16,000)	$ 8,811,000	$ (61,000)

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, 2020 and 2019, none of the investments whose estimated fair values were less than amortized cost were considered to be other-than-temporarily impaired given the severity and duration of the impairment and the credit quality of the issuers.

NOTE 3: INVESTMENTS *(continued)*

MPT does not intend to sell its investments whose fair values are less than amortized cost 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	
	2020	2019
Interest income	**$ 6,800,000**	$ 7,784,000
Gross gains on sales of investments	**358,000**	142,000
Gross loss on sales of investments	**—**	(608,000)
Investment management fees and expenses	**(133,000)**	(244,000)
Net amortization of premium on fixed income securities	**(1,418,000)**	(1,067,000)
Investment income, net	**$ 5,607,000**	$ 6,007,000

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	
	2020	2019
Accrued indemnity	**$16,361,000**	$13,749,000
Accrued defense and investigative services	**1,957,000**	2,952,000
	$18,318,000	$16,701,000

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 shown on the following page.

NOTE 4: UNPAID CLAIMS AND EXPENSES AND NON-ASSESSABLE FORMER MEMBERS' LIABILITY *(continued)*

	December 31 2020	December 31 2019
Claims reported:		
Members retired	**$ 8,336,000**	$ 8,671,000
Members voluntarily terminated, transferred and deceased	**7,921,000**	8,474,000
Members involuntarily terminated	**13,314,000**	11,854,000
Claims incurred but not reported	**7,151,000**	6,341,000
Claims administration and other adjusting expenses	**1,610,000**	1,654,000
	$38,332,000	$36,994,000

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
2021	$14,125,000
2022	7,795,000
2023	5,297,000
2024	3,543,000
2025	2,481,000
2026 and after	5,091,000
	$38,332,000

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 $38,332,000 at December 31, 2020. 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.

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 $143,523,000 and $139,997,000 as of December 31, 2020 and 2019, 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 for assessable members. 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 16 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.

NOTE 5: CONTINGENCIES *(continued)*

MPT has entered into reinsurance contracts with major foreign and domestic reinsurance companies and its affiliate, Cooperative of American Physicians Insurance Company, Inc. (CAPIC, a wholly-owned subsidiary of CAP), which provides coverage on a claims-made basis for case losses and defense costs in excess of a $1,000,000 retention. 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 foreign and domestic reinsurance companies and CAPIC, which provides coverage on a claims-made basis for multiple claims arising out of one common, systemic event. Under these systemic event reinsurance contracts, limits of $7,000,000 are available to MPT on a claims-made basis over a $3,000,000 retention.

MPT is subject to other 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.

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, legal and other administrative and management services to MPT. Under the agreement, MPT pays CAP monthly fees for these services that are based on actual expenses incurred by CAP plus a margin. The margin applies to all services, except legal, whose services are provided to MPT at cost. CAP agreed to waive the margin for the years ended December 31, 2020 and 2019. Fees of $24,251,000 and $23,575,000 were incurred by MPT for administrative and management services under the agreement for the years ended December 31, 2020 and 2019, 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 $15,889,000 and $17,886,000 for the years ended December 31, 2020 and 2019, respectively. Included in the payable to affiliated entity is $1,725,000 and $1,853,000 payable to CAPIC for these services as of December 31, 2020 and 2019, respectively.

In 2020 and 2019, 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 2020 and 2019. These agreements can be terminated and commuted at the end of any calendar quarter prospectively by mutual agreement of MPT and CAPIC. Premiums paid by MPT under these agreements were $5,500,000 and $4,000,000 for the years ended December 31, 2020 and 2019, 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 from MPT to CAPIC under this contract were $230,000 and $228,000 for the years ended December 31, 2020 and 2019, respectively. For the years ended December 31, 2020 and 2019, total affiliate reinsurance premium expense under all reinsurance contracts with CAPIC was $5,707,000 and $4,206,000, respectively, and is included in Claims: Other Operating Costs.

CAP provides its Members and Participants defense coverage for medical board actions with a $25,000 limit and employment practice defense coverage with a $50,000 limit. CAPIC provides insurance coverage to CAP for these benefits. MPT reimburses CAP for a significant portion of the cost of this coverage. CAP paid CAPIC $2,887,000 and $2,521,000 for the years ended December 31, 2020 and 2019, respectively, for this coverage, of which MPT reimbursed CAP $2,830,000 and $2,462,000 for the same respective years.

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 $25,000 and $22,000 for the years ended December 31, 2020 and 2019, respectively. 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 $5,187,000 and $5,301,000 at December 31, 2020 and 2019, respectively. The benefit related to this program was $600,000 and $836,000 for the years ended December 31, 2020 and 2019, respectively. 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 $12,960,000 and $11,449,000 at December 31, 2020 and 2019, 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, totaled $21,653,000 and $18,307,000 at December 31, 2020 and 2019, respectively. The mutual fund assets are carried at fair value, totaled $4,254,000 and $3,914,000 at December 31, 2020 and 2019, respectively.

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 trust 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 the third-party trust. MPT made its final premium contribution in 2016.

NOTE 8: INCOME TAXES

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

	Years Ended December 31	
	2020	2019
Current	**$ 356,000**	$1,082,000
Deferred	**(3,076,000)**	(712,000)
Total	**$(2,720,000)**	$ 370,000

NOTE 8: INCOME TAXES *(continued)*

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

	Years Ended December 31	
	2020	2019
Federal income tax (expense) at 21%	$ (342,000)	$(1,109,000)
Adjustments in taxes resulting from:		
State income tax (net of federal benefit)	(140,000)	123,000
Change in valuation allowance	(2,161,000)	1,496,000
Employer paid parking	(61,000)	(80,000)
Employer benefit plans	(50,000)	(36,000)
Meals	(10,000)	(34,000)
Life insurance proceeds	35,000	—
Other items	9,000	10,000
Total federal income tax (expense) benefit	$(2,720,000)	$ 370,000

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

	December 31	
	2020	2019
Trust Fund Corpus, restricted:		
Deferred tax liability attributable to net unrealized investment gains	$ (1,482,000)	$ (654,000)
Trust Fund Operating:		
Deferred tax assets attributable to:		
Initial trust contributions	$ 28,132,000	$ 27,941,000
Discounting of non-assessable former members' claim and other liability	2,147,000	1,963,000
Net operating loss carryforward	9,553,000	7,392,000
AMT credit carryforward	—	357,000
Employee benefit obligations	2,954,000	3,521,000
Lease incentive obligations	534,000	783,000
Capital loss carryover	351,000	496,000
Other items	173,000	129,000
Deferred tax assets before valuation allowance	43,844,000	42,582,000
Valuation allowance	(9,553,000)	(7,392,000)
Deferred tax assets after valuation allowance	34,291,000	35,190,000
Deferred tax liabilities attributable to:		
Discounting of assessable members' contingent claim liability	(26,612,000)	(24,098,000)
Discounting transition adjustment pursuant to the Tax Cuts and Jobs Act	(846,000)	(1,016,000)
Accretion of bond discount	(1,209,000)	(1,150,000)
Unrealized gains on fixed income maturities	(683,000)	(333,000)
Internally developed software	(198,000)	(182,000)
Deferred state liability	(415,000)	(456,000)
Other items	—	(201,000)
Deferred tax liabilities	(29,963,000)	(27,436,000)
Deferred tax asset, net	$ 4,328,000	$ 7,754,000

NOTE 8: INCOME TAXES *(continued)*

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, dues 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, 2020, there remain federal net operating loss carryforwards totaling $33,007,000 which will expire beginning 2030, 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 for 2006 and subsequent tax years. As of December 31, 2020, there remains a state net operating loss carryforward totaling $29,645,000, which will expire beginning 2029 to be applied to future tax years.

Deferred tax assets are recognized only to the extent that it is more likely than not that future taxable income will be available, and a valuation allowance is established where deferred tax assets cannot be recognized. Based on an analysis of MPT's tax position, management believes that it is more likely than not that the benefit from certain federal and state net operating loss carryforwards will not be realized. As a result, MPT recognized a valuation allowance of $9,553,000 and $7,392,000 on the deferred tax assets relating to federal and state net operating loss carryforwards as of December 31, 2020 and 2019, respectively. The valuation allowance increased in 2020 and decreased in 2019 by $2,161,000 and $1,495,000, respectively.

MPT paid no income taxes and no tax penalties were recognized for the year ended December 31, 2020 or 2019.

Tax years 2017 through 2019 and tax years 2016 through 2019 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, 2020 and 2019, 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 $3,107,000 and $3,030,000 for the years ended December 31, 2020 and 2019, respectively. The future minimum rental commitments under these operating leases are as follows:

Years Ending December 31	Amount
2021	$2,329,000
2022	2,421,000
2023	2,436,000
2024	598,000
2025 and after	581,000
	$8,365,000

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. There were no amounts outstanding as of December 31, 2020 and 2019. Interest expense on the line of credit was $0 and $6,000 for the years ended December 31, 2020 and 2019. MPT's fixed income securities are pledged as collateral for amounts outstanding under the line of credit. 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, 2020 or 2019.

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, 2020 or 2019.

Supplementary Financial Information

MUTUAL PROTECTION TRUST

	As of and For the Years Ended December 31				
	2020	2019	2018	2017	2016
RESULTS OF OPERATIONS					
(In millions)					
Total assessments, dues and revenues	**$122.3**	$134.6	$123.3	$127.4	$141.1
Expenses					
Indemnity expense	**$ 46.9**	$ 49.3	$ 43.8	$ 42.6	$ 61.3
Defense and investigative	**27.2**	35.7	32.0	34.5	36.3
Other	**46.6**	44.4	44.6	43.8	47.6
Total expenses	**$120.7**	$129.4	$120.4	$120.9	$145.2
Excess (deficit) of assessments, dues and revenues over expenses, net of income taxes	**$ (1.1)**	$ 5.7	$ 4.3	$ 1.3	$ (5.6)
FINANCIAL POSITION					
Cash and invested assets	**$252.5**	$237.0	$225.2	$213.9	$212.9
Total assets	**$375.6**	$365.0	$345.0	$339.9	$344.5
Members' equity	**$170.1**	$166.6	$155.3	$153.4	$153.9
MEMBERSHIP AND CLAIMS (Unaudited)					
Active members at year end	**12,056**	11,970	11,867	11,746	11,809
Services for reported claims					
Cases opened	**637**	812	928	871	1,047
Cases closed	**609**	879	957	1,008	1,079
Cases under management	**1,194**	1,166	1,233	1,262	1,399
Per active member (In thousands)					
Total assessments, dues and revenues	**$ 10.1**	$ 11.2	$ 10.4	$ 10.8	$ 11.9
Indemnity expense	**3.9**	4.1	3.7	3.6	5.2
Defense and investigative	**2.3**	3.0	2.7	2.9	3.1
Other expenses	**3.9**	3.7	3.8	3.7	4.0
Total expenses	**$ 10.1**	$ 10.8	$ 10.2	$ 10.2	$ 12.3

COOPERATIVE OF
AMERICAN PHYSICIANS

333 S. Hope St., 8th Floor, Los Angeles, CA 90071 | 800-252-7706 | www.CAPphysicians.com

LOS ANGELES | ORANGE | SAN DIEGO | WALNUT CREEK