

**A Physician's Advocate
for 25 Years**

Table of Contents

Chairman's Letter	2
President's Report	4
Milestones of Our First 25 Years	8
Condensed Financial Highlights	13
Board of Directors	14
Senior Management	15

Mission Statement

To provide high-quality insurance products and technology-based business solutions to enhance the strength and security of the health care community.

Vision Statement

To become the most trusted business partner of health care providers.



G. Richard Geier, M.D.

Board Chairman

Letter to Shareholders

In the March 1980 issue of *Minnesota Medicine*, then Minnesota Medical Association President Frank E. Johnson, M.D., reported that the MMA's Professional Liability Committee continued to negotiate with the St. Paul Companies on behalf of Minnesota physicians. By May 22, 1980, advocacy had turned into action when the MMA House of Delegates approved the committee's recommendation to form the organization that would become Midwest Medical Insurance Company (MMIC). In the 25 years since, MMIC has grown to be an advocate, in words and actions, for physicians in six Upper Midwest states.

Early on MMIC made its insurance available in North and South Dakota, states without enough physicians to start their own companies. Later, MMIC embraced companies formed by the Iowa Medical Society and by physicians in Nebraska—the Iowa Physician Mutual Insurance Trust and Medical Liability Mutual of Nebraska, respectively. More recently, MMIC has grown nicely by responding to insurance requests from physician colleagues in Wisconsin.

We have testified before legislatures in Iowa and Minnesota within the past year and have participated in many tort reform forums, both locally and nationally. Our risk management staff advocates within the profession to improve patient care and to reduce the number and size of claims. We formed our subsidiaries, MMIC Technology Solutions and the MMIC Agency Inc., to provide additional services to support physicians, clinics and hospitals.

Commercial insurers, most of whom are now out of the medical professional liability business, once mocked MMIC as “a bedpan mutual.” Now after a quarter century, MMIC is recognized nationally as one of the most successful and respected physician-owned medical professional liability insurance companies in the industry.

Our 25th Year Was a Very Good One

A continued decrease in claim frequency offset the moderating increase in claim severity to provide excellent financial results. Depressed interest rates kept investment returns low, as most of our investments are required to be in bonds. However, our managers have beaten the benchmarks handily. While the subsiding malpractice crisis has led to some stability, there has not been a general roll back in prices in the industry, just less severe premium increases. We are simply adjusting to a new level of pain.

MMIC was able to reduce 2006 premiums for many Iowa physicians and to provide a modest dividend for its physicians in Minnesota. If present medical

malpractice trends continue, premiums should stabilize and policyholder dividends could be more frequent. Unfortunately, the improving situation will attract competitors who will offer unrealistically low premiums for a time. In a few years, these companies will then likely raise premiums dramatically or will disappear when the cycle tightens.

MMIC remains focused on the long-term welfare and best interests of its insured physician shareholders, clinics and hospitals. Our new three-year strategic plan emphasizes our commitment in the updated mission statement: *“To provide high-quality insurance products and technology-based business solutions to enhance the strength and security of the health care community.”* Already the market leader in our six-state territory, our emphasis is not on our continued gradual growth, but on enhancing customer service and our value.

Last year, we added two new board members: Dr. Paul Matson and Darrell Tukua, CPA. Dr. Matson replaced Dr. Terence Cahill, whom we thank for five and a half years of service. Dr. Matson is an orthopedic surgeon practicing in Mankato, Minn. He is a former president and board chair of the MMA and currently serves as an alternate American Medical Association delegate. Maintaining close relationships with our sponsoring medical associations is very important to MMIC. About half our board members are leaders in organized medicine.

Darrell Tukua joined the board's Audit and Budget Committee in 2004. Adding his financial expertise worked out so well in the committee that in 2005 we elected him to our holding company board of directors.

On a sad note, Dr. Robert S. Flom died July 20, 2005, at the age of 80. Dr. Flom chaired the MMA Professional Liability Committee that recommended the formation of MMIC. He also chaired the MMIC board of directors, steering the company through its first nine formative years until he retired in 1989. Perhaps we can pay tribute best to this visionary physician advocate by following his advice at the end of his first annual report to the MMA, which was published in the October 1981 *Minnesota Medicine*: “Meanwhile – practice carefully!”



G. Richard Geier, M.D.
Chairman of the Board



David P. Bounk

President and
Chief Executive Officer,
The MMIC Group

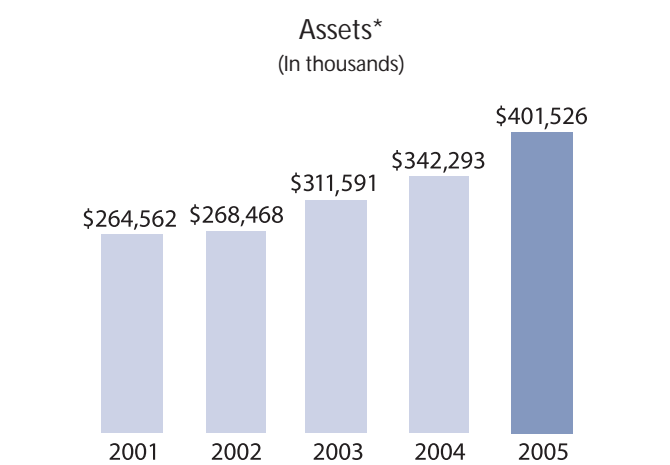
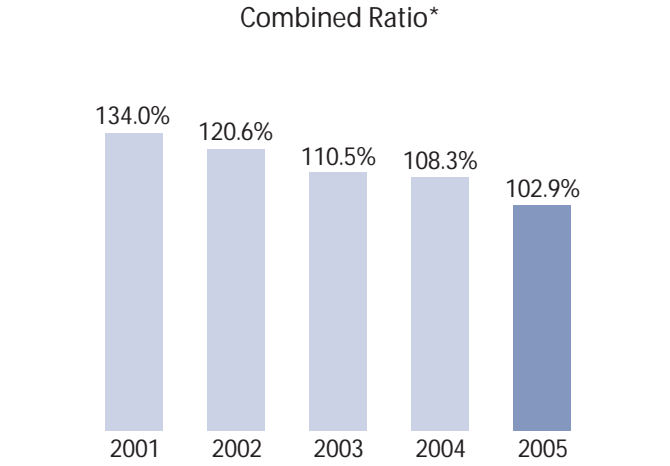
President's Report

Twenty-five years of unwavering support and advocacy for its policyholders and other health care providers has allowed MMIC to become one of the most effective physician-owned companies in the country.

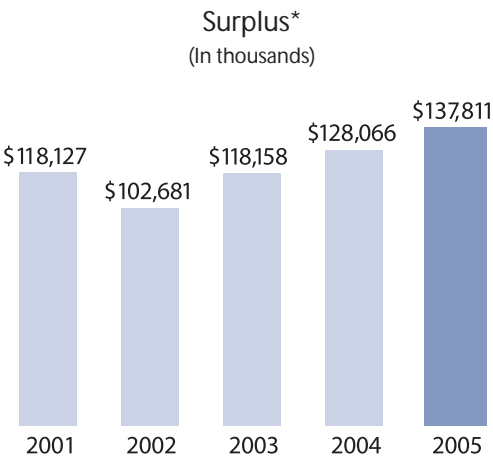
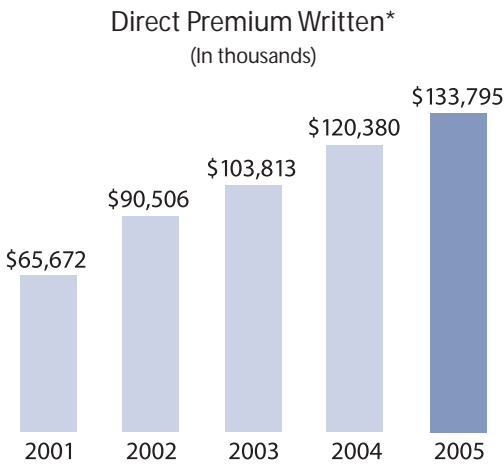
In this year's annual report, numerous charts and financial statements will illustrate that 2005 was a successful year for MMIC. We had a respectable increase in written premiums, assets and policyholder surplus. And perhaps most significantly, we saw the fourth consecutive decrease in our combined ratio.

Rate adequacy, control of administrative expenses and a significant drop in claim frequency, the lowest level in MMIC history, drove the 5.4 points improvement in the combined ratio. However, a continued rise in claim severity along with late development of claims from prior years, especially in Minnesota, partially offset these positive results.

Direct written premium increased 15 percent in 2005. With our deliberate and controlled growth strategy, we wrote \$4.9 million in new business. Most of that growth came from new opportunities in Iowa and Wisconsin. Our insurance agents and brokers submitted



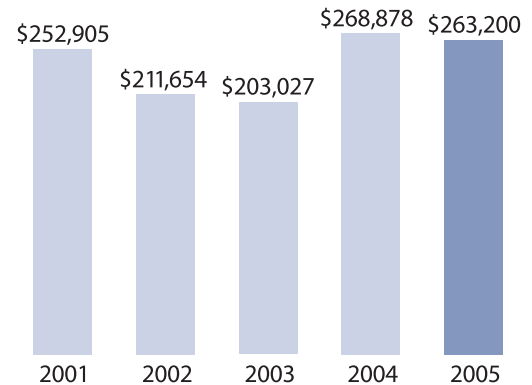
the majority of new business. They were successful in helping MMIC retain many accounts. We lost a few accounts due to aggressive underpricing by competitors, however, a few returned when they did not find the level of service to which they were accustomed.



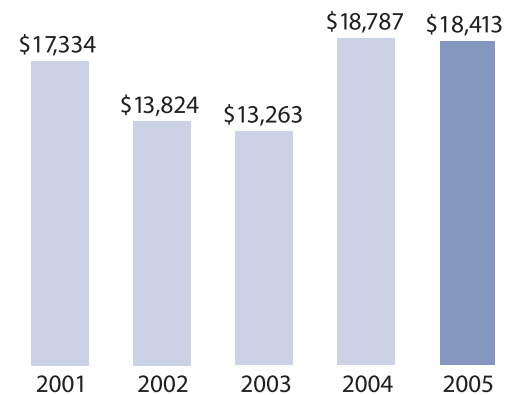
The average paid claim decreased slightly to \$263,200, nearly \$5,700 less than 2004, even though we continued to handle a number of high valued cases.

Averaged allocated loss adjustment expense in 2005 improved to \$18,413, two percent better than 2004 and significantly lower than the average ALAE of \$21,306** for Physician Insurers Associations of America companies.

Average Indemnity Paid
(Physician and Clinic Professional Liability Closed Cases)
(In dollars)



Average Allocated Loss Adjustment Expense (ALAE)
(Physician and Clinic Professional Liability Closed Cases)
(In dollars)



Outstanding Claim Results

One fundamental reason we have remained an industry leader the past 25 years is our unending commitment to a well-structured, defense-minded claim management philosophy that protects the interests of policyholders.

MMIC claim results were very positive and showed improvement over last year.

* Derived from stand-alone Midwest Medical Insurance Company audited financial statements prepared on a statutory basis.

MMIC Base Rates are Among the Lowest in Country

While improving our financial security, we also were able to hold down the cost of coverage for policyholders. Our physician base rates continue to be some of the lowest in the country. Last year our board voted not to increase base rates for 2006 in five of our six states.

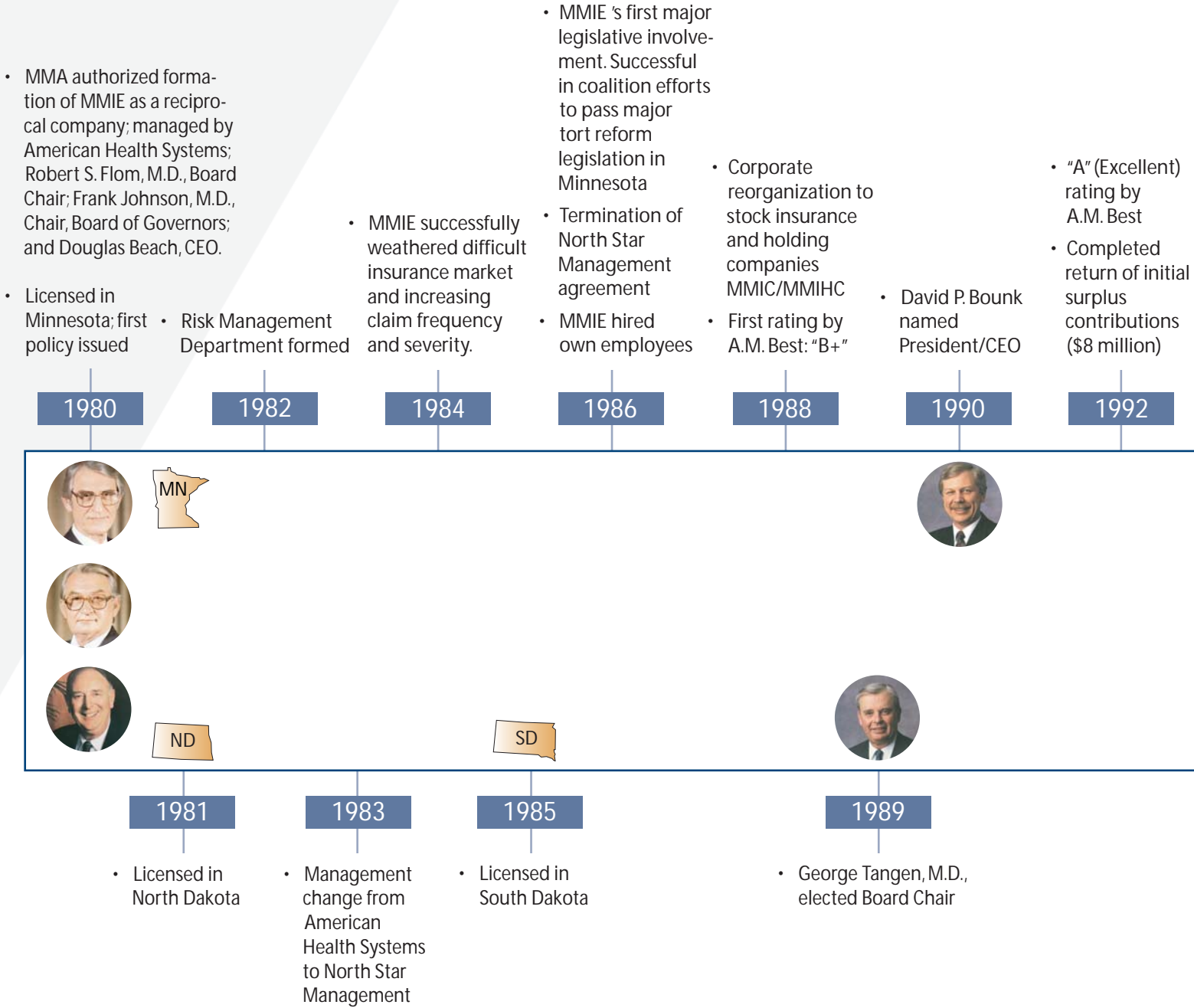
The chart below depicts a comparison of MMIC physician rates to the rates of the largest medical liability insurers in other selected states. All rates are for \$1 million/\$3 million limits.

2005 MMIC Base Rates			
	Internal Medicine	General Surgery	OB/GYN
Iowa	\$6,401	\$23,171	\$47,173
Minnesota	\$4,286	\$12,857	\$19,643
North Dakota ⁺	\$6,681	\$20,044	\$30,623
Nebraska ⁺	\$4,245	\$18,086	\$27,680
South Dakota ⁺	\$4,619	\$13,858	\$21,172
Wisconsin ⁺	\$5,147	\$18,015	\$23,677

2005 Other States			
	Internal Medicine	General Surgery	OB/GYN
Colorado ⁺	\$14,912	\$52,828	\$47,212
Florida	\$38,388 – 74,855	\$153,549 – 299,420	\$153,549 – 299,420
Illinois ⁺	\$19,740 – 38,424	\$51,500 – 101,940	\$72,048 – 143,040
Michigan	\$14,019 – 38,942	\$58,544 – 162,623	\$60,966 – 169,350
Texas ⁺	\$16,982 – 36,018	\$59,253 – 125,672	\$71,260 – 151,138

⁺ State has tort reform, including a cap on pain and suffering. Source for other states: *Medical Liability Monitor*, October 2005

Milestones of Our First 25 Years



- Purchased MedPower Information Resources
- Licensed in Wisconsin and Illinois
- Merged with Medical Liability Mutual Insurance Company of Nebraska
- Andrew J.K. Smith, M.D., elected Board Chair
- Communications and Law and Health Policy departments formed
- Underwriting functions for all states centralized in Minnesota
- Stock restructure Class A to Class C
- Purchased ownership interest in Partners Healthcare Consulting
- G. Richard Geier, M.D., elected Board Chair
- \$75 million refunded to policyholders to date
- Jack Kleven retired
- David Bounk reassumed Presidency of MMIC

1996 1998 2000 2002 2004



1993 1995 1997 1999 2001 2003 2005

- Merged with Iowa Physicians Mutual Insurance Trust
- SEC listing
- MMIHC Insurance Services (Agency) incorporated
- Practice Resources (Midwest Medical Solutions) incorporated
- Significant growth in nontraditional accounts; first self-insured retention account written
- Jack L. Kleven named President of MMIC
- Johnson-McCann Benefits purchased
- MMIC MedPortal and MMIC Consulting launched
- Purchased ownership interest in Langan & Flynn
- Business Office Solutions (BOS) began
- Began more actively writing in Wisconsin
- MMIC Benefits book of business sold; name change to MMIC Agency
- SEC delisting
- The MMIC Group turns 25

The board also approved returning \$2.5 million in unanticipated profits to our Minnesota physician policyholders in 2006. Checks will be mailed to Minnesota policyholders who were insured with us in 1999 and are still insured when we make quarterly payments in 2006. This is the first time in four years we are able to return unanticipated profits. MMIC has returned \$77 million to policyholders over the past 14 years, including \$10 million from the stock restructure.

Using Technology to Control Expenses and Enhance Services

We continued to make it easier for policyholders to access information and services last year. We redesigned and expanded our web site (www.mmicgroup.com) to include a Policyholder Service Center. Policyholders can review their policy and claim information, and make automatic premium payments online. We added to our online risk management services to include more resources for physicians, clinics and hospitals. Using technology to enhance services and internal work processes has allowed MMIC to continue to hold the administrative expense per physician to \$878 per year, which is one of the lowest in the country.

We made further refinements to our rate-making processes to help keep our premiums at a competitive level while maintaining financial security. These improvements will allow us to more selectively rate accounts based on their own claim experience. We also automated the underwriting renewal process and expanded agent and broker access to MMIC's web site resources. In 2006, we will begin replacing our paper files with a complete imaging system, which will continue to allow staff to improve their efficiency.

2005 Legislative Advocacy

We believe advocating for physicians has to include more than effective risk management and claim handling. It must also involve working closely with medical societies in legislative activity, especially when the results can improve the fairness of the litigation process. MMIC continued to support state medical associations in tort reform efforts last year. We also participated in legislative and regulatory activities of the PIAA and the Health Coalition on liability and access. Listed below by state is a brief list of the outcomes of some of our 2005 legislative activities:

North Dakota: The Legislature broadened the expert affidavit requirement to apply to actions of clinics, ambulatory care centers and nursing homes and to informed consent cases.

Iowa: We provided significant information and testified at hearings of the Iowa Legislature Interim Commission on Medical Malpractice. A part of that testimony was correcting the flawed data presented by tort reform opponents. An outcome of the committee hearings is there will be tort reform legislative proposals in 2006. MMIC also participated in meetings facilitated by the Iowa Medical Society that included plaintiff and defense attorneys, and other insurance companies. Discussions centered on ways to make the litigation process more efficient and less costly.

South Dakota: South Dakota Legislature passed the "Apology Law," which prohibits the use of statements of apology by health care providers to prove negligence medical malpractice actions.

Wisconsin: In 2005, the Wisconsin cap on non-economic damages was overturned. The 2006 Legislature will address bills proposing a new cap that can withstand constitutional challenge.

Minnesota: Efforts to pass a statute of repose and a cap on noneconomic damages were unsuccessful.

Because the litigation environment is much better in MMIC's territory than in other parts of the country, significant tort reform will be difficult to achieve. Lobbyists for plaintiff attorneys have produced a number of misleading studies that suggest insurance reform and pricing controls are necessary, but tort reform is not. No matter how simplistic it may sound, artificially trying to control such things as insurance rates, dividends and surplus will hurt physicians by weakening the financial stability of the companies that are providing medical malpractice coverage.

Subsidiaries Had a Solid Year

Over the past several years, MMIC has been offering policyholders a variety of property and casualty insurance coverages and the latest technology products and services through the MMIC Agency and MMIC Technology Solutions. We diversified our product offerings because our policyholders continue to ask for our help in these areas. Helping physicians is why MMIC was created 25 years ago.

MMIC Agency Inc. continues to broaden its offerings to our direct written policyholders by partnering with some of the major insurance companies in the country. Agency net income in 2005 was \$263,432, an increase of 16.9 percent from 2004. A nice component of the Agency's success is that 123 of its clients

also purchased their medical professional liability coverage from MMIC. We are encouraged by the number of policyholders who are buying a variety of insurance products and services from The Agency. We also are encouraged that a number of our insurance agents are working with us to access markets for business that is difficult to place.

MMIC Technology Solutions Inc. had a strong year in 2005. Sales increased to more than \$3.2 million. The number of Technology Solutions clients reached an all time high of 93, representing more than 500 physicians. Operating expenses remained flat compared to 2004. Technology Solutions was able to reduce its operating loss before taxes, depreciation and interest by nearly \$400,000. These improved results positioned Technology Solutions for a strong start in 2006. The company has recurring revenue of \$2.1 million and late year sales will generate licensing revenue of nearly \$400,000 in 2006.

We are finding that more physicians are recognizing the need for technology in their practices. They are more accepting of electronic medical records. We believe that greater emphasis on efficiencies and quality patient care will accelerate the acceptance of electronic medical records in the near future.

Enhanced Customer Service

The 2005 results for the MMIC Group are encouraging; however, we will not rest on our laurels. The new 2006 to 2008 strategic plan emphasizes continuous improvement of customer service. The plan also includes expansion of our risk management activities to include broader patient safety and quality of care initiatives. We are also exploring whether MMIC

should play a more active role in broader health policy issues.

In today's health care environment, there is increased discussion about improving the quality of care as one means to achieve long-term stability of the health care system. You may have heard of initiatives such as the Bridges to Excellence, Leapfrog Group, Institute for Clinic Systems Improvement and the Iowa Health Collaborative. We believe that we can assist policyholders by engaging in some of these broader healthcare-related activities. The MMIC Law and Health Policy and Risk Management departments along with the board and its Strategic Planning Committee will analyze these and other opportunities. If appropriate, we will participate in a way that will be helpful to policyholders.

As previously stated, no organization can allow itself to become complacent based upon its past successes. It is impossible to predict the future, but we do know it will hold many changes, many challenges and many opportunities. Over the next few years, we

will see significant price competition from new entrants into the medical professional liability industry and from some of the larger commercial companies that have recently indicated a desire to compete in our territory.

We have never let competition cause us to make rash and unwise decisions. We believe that being a true physician advocate means providing outstanding customer service, maintaining a financially secure insurance company and participating in other areas important to policyholders. MMIC has been a consistent presence for 25 years. We will be your best advocate for the next 25 years.

Thank you for allowing the employees, and board and committee members of the MMIC Group to be your advocates over the past 25 years.

Midwest Medical Insurance Holding Company and Subsidiaries

Condensed Consolidated Financial Information

(Unaudited, In Thousands)

Balance Sheets

	December 31	
	2005	2004
Assets		
Invested assets	\$377,607	\$328,457
Other assets	50,785	47,956
Total assets	<u>\$428,392</u>	<u>\$376,413</u>
Liabilities and shareholders' equity		
Liabilities:		
Unpaid losses and loss adjustment expenses	\$219,912	\$188,946
Other liabilities	67,831	54,405
Total liabilities	<u>\$287,743</u>	<u>243,351</u>
Shareholders' equity	140,649	133,062
Total liabilities and shareholders' equity	<u>\$428,392</u>	<u>\$376,413</u>

Statements of Income

	Year Ended December 31	
	2005	2004
Revenues:		
Net premiums earned	\$113,141	\$ 96,026
Net investment income	13,436	11,883
Realized capital gains	1,822	4,532
Other	4,325	3,246
	<u>132,724</u>	<u>115,687</u>
Losses and expenses:		
Losses and loss adjustment expenses	101,529	90,173
Underwriting, acquisition and insurance expenses	14,652	13,548
Other operating expenses	6,180	5,978
	<u>122,361</u>	<u>109,699</u>
Income before income taxes	10,363	5,988
Income tax expense	2,662	1,752
Net income	<u>\$ 7,701</u>	<u>\$ 4,236</u>

The foregoing unaudited condensed consolidated financial information has been derived from the audited consolidated financial statements. These statements are available upon request from the Finance Department or on our Web site: www.mmigroup.com.

Board of Directors

G. Richard Geier, Jr., M.D.
Chairman
Olmsted Medical Center
Rochester, Minnesota

Michael D. Abrams
Executive Director
Iowa Medical Society
West Des Moines, Iowa

John R. Balfanz, M.D.
Pediatrics & Young Adults Medicine
St. Paul, Minnesota

Robert W. Beattie, M.D.
University of North Dakota School
of Medicine and Health Science
Grand Forks, North Dakota

Gail P. Bender, M.D.
Oncologist, P.A.
St. Louis Park, Minnesota

James R. Bishop, M.D., Secretary
Director of Medical Affairs
Fairview Southdale Hospital
Edina, Minnesota

David P. Bounk
President and CEO
The MMIC Group and
MMIC Technology Solutions
Minneapolis, Minnesota

Mary S. Carpenter, M.D.
Family Practice Associates
of Winner
Winner, South Dakota

Kent E. Carr, M.D.
Mercy Clinics, Inc.
Des Moines, Iowa

Peter J. Daly, M.D.
Summit Orthopedics, Ltd.
St. Paul, Minnesota

Michael G. Del Core, M.D.
Creighton Cardiac Center
Omaha, Nebraska

Anthony C. Jaspers, M.D.
Lake Crystal Clinic
Lake Crystal, Minnesota

Eugene L. Kerns, M.D.
Obstetrics and Gynecology
Specialist, P.C.
Davenport, Iowa

Wayne F. Leebaw, M.D., Vice Chair
Endocrinology Clinic of Minneapolis
Edina, Minnesota

Mark O. Liaboe, M.D.
Dubuque Internal Medicine, P.C.
Dubuque, Iowa

Patricia J. Lindholm, M.D.
Fergus Falls Medical Group
Fergus Falls, Minnesota

Paul C. Matson, M.D.
Orthopaedic & Fracture Clinic, P.A.
Mankato, Minnesota

Stephen A. McCue, M.D.
Metropolitan Obstetrics &
Gynecology P.A.
St Paul, Minnesota

Robert K. Meiches, M.D.
Chief Executive Officer
Minnesota Medical Association
Minneapolis, Minnesota

Mark D. Odland, M.D.
Hennepin County Medical Center
Minneapolis, Minnesota

T. Michael Tedford, M.D.
The Ear, Nose and Throat Clinic
Minneapolis, Minnesota

Tom D. Throckmorton, M.D.
Northwest Iowa Surgeons
Spencer, Iowa

Darrell R. Tukua, CPA
Retired Partner, KPMG LLP
Blaine, Minnesota

William L. Youmans, M.D.
Camden Physicians, Ltd.
Minneapolis, Minnesota

Senior Management

David P. Bounk
President and CEO
The MMIC Group and
MMIC Technology Solutions Inc.

Niles A. Cole
Chief Financial Officer/Vice President – Finance
The MMIC Group

Jay A. Koepsell
Controller/Assistant Vice President – Finance
The MMIC Group

Stephanie A. Kroeger
Assistant Vice President – Human Resources
The MMIC Group

Elizabeth S. Lincoln
Vice President – Law and Health Policy
General Counsel
The MMIC Group

Gerald M. O'Connell
Vice President – Sales and Marketing
The MMIC Group and MMIC Agency Inc.

Julie J. Stafford
Vice President – Underwriting
Midwest Medical Insurance Company

Peggy A. Wagner
Vice President – Risk Management
Midwest Medical Insurance Company

Thomas M. Youngblom
Assistant Vice President – Information Services
The MMIC Group

Jerry A. Zeitlin
Vice President – Claim
Midwest Medical Insurance Company

Rosalind M. Miller
Communications Manager
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Auditors

Ernst & Young LLP

Actuarial Consultant

Bickerstaff, Whatley, Ryan & Burkhalter
Consulting Actuaries

Headquartered in Minneapolis, Minn., the MMIC Group provides medical liability insurance, property and casualty insurance products and a range of technology, human resources and strategic health care consulting products and services to physicians, clinics and hospitals in the Upper Midwest.