ProMutualGroup®

FINANCIAL INTEGRITY, PHYSICIAN LOYALTY

2007 ANNUAL REPORT

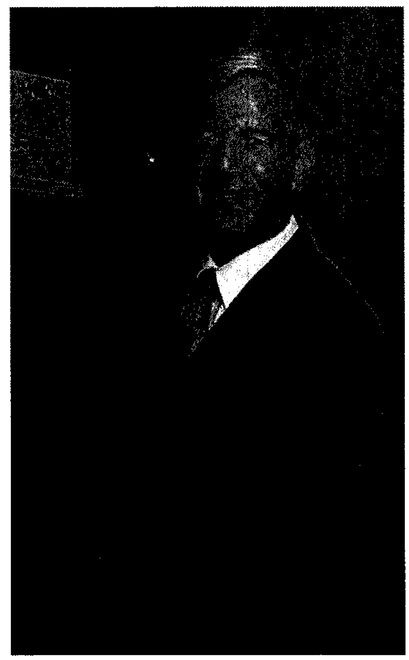
a tradition of Commitment

ENDUREPERFORMSUSTAIN

Chairman's Letter

Kenneth A. Heisler, MD, FACS
Chairman of the Board

"...we remain in the top 10 medical liability insurance writers in the United States... and having broken into the top five on the list of specialty medical liability insurance companies in the nation."



As a fellow healthcare professional, I understand the importance of choosing a medical liability provider that offers a variety of coverage options, excellent services, and has the financial wherewithal to be there in the long run. I rely on the protection and dependability that ProMutual Group provides and I am proud to be the Chairman of such an organization. For more than 30 years, ProMutual Group and its predecessors have been providing protection to the healthcare community, and our commitment to maintaining this in the long-term is the subject of this year's annual report.

I am pleased to report that our financial strength remained solid in 2007. This year marked the 12th consecutive year our A.M. Best rating of A- (Excellent) was reaffirmed. In addition we remain in the top 10 medical liability insurance writers in the United States based on direct written premium and have broken into the top five on the list of specialty medical liability insurance companies in the nation with a ranking of fourth, as reported by both Conning Research and the National Association of Insurance Commissioners.

ProMutualGroup

While last year was profitable and the industry more stable than we have seen in the past decade, we are cognizant of the extreme volatility of the medical liability business. In 2007 we continued our commitment to pricing appropriately and selecting only the best customers in each territory as allowed by state requirements. We look for those healthcare professionals who have a record of practicing safe medicine and are committed to using risk management techniques to avoid losses. Further, we continue to set our rates based on historical trends and anticipated payouts for many years in the future. For we realize that in this business, it can take many years for an incident to develop into a claim and ultimately reach a legal conclusion.

The primary service we provide to our policyholders is to protect them when they are faced with a claim. In 2007, we continued our strategy of aggressive claims management and efforts to help control the cost of malpractice claims. Our track record of defending our policyholders this year remained impressive. Nearly 75 percent of claims were closed without an indemnity payment and for those that went to a verdict at trial, we won 90 percent. This record comes from our philosophy of tenaciously investigating all claims, resolving those with merit quickly, and vigorously defending good medicine.

To continue to provide outstanding claim management support in the future, we are building upon several successful initiatives that help us provide the best defense possible. Such initiatives include the use of alternative dispute resolution techniques, an online database of legal expert testimony, and a defense counsel mentoring program to ensure there's a talented pool of experienced defense attorneys well into the future.

Although healthcare providers may face a claim at some point in their professional career, we believe that the best claim is the one that doesn't occur. Our function is to not only defend, but to reduce lawsuits, and for this we provide risk management training and protocols for individual physicians, groups and hospitals that will help them avoid a lawsuit in the first place. Over time, the results of our risk management efforts will be realized in the reduced number of claims our insureds experience, a reduction in our defense costs and ideally, more stable premiums for all.

Lastly, I would like to recognize the commitment and hard work of my fellow members of the Board of Directors and the seasoned management team of ProMutual Group. Their knowledge, experience and, most of all, dedication has allowed this company to persevere, prosper and maintain its quality given changing economic conditions and changes in healthcare. That is our commitment to you now, as it has been for the past three decades, and as it will be tomorrow.

Sincerely,

Kenneth A. Heisler, M.D.

Kenneth A. Heisler, MD, FACS
Chairman of the Board

President's Letter

ProMutual Group's commitment to you – our policyholders – is the cornerstone of our mission. Whether you are a solo practitioner or part of a large group or institution, providing protection to healthcare providers has been our sole business for more than three decades. Our goal has always been to do one thing, *and to do it well.* We have been successful not only in 2007, but throughout our history, in being able to provide you with protection you can rely upon.

The reason we have been able to maintain our commitment is primarily through our ability to remain financially strong, even through fluctuating cycles in the marketplace. To deal with inevitable market cycles we must anticipate that there is going to be change and prepare for it. We do this by sticking to our core competencies. As a niche company, our focus is well-defined, that is, the protection of healthcare providers like yourself. In comparison to companies that do not enjoy such focus, we have been able to build strong, enduring relationships with our customers. This is due to our size, specialty, experience and, most importantly, our financial strength.

Generally, the medical liability industry as a whole is reporting excellent results for 2007. We find that our year-end numbers are very much in line with the industry and, once again, ProMutual Group ended the year in strong financial standing. This is evidenced by key indicators, such as total assets in excess of $2.2 billion and surplus of more than $600 million. These numbers indicate that we will be able to continue to pay any current and future claims since we maintain strong reserves against future liabilities. In short, we can say that we have the means to be here for our policyholders for years to come.

The return to profitability the medical liability industry has experienced over the past few years has resulted in a more competitive marketplace. Despite this, our renewal rate remained relatively steady in 2007 with the number of existing policies decreasing only slightly for physicians while remaining essentially stable for institutions. Clearly, the proven financial strength and the professional level of services we deliver continued to earn us the loyalty of our policyholders.

With a competitive marketplace, it is even more important that we are vigilant in managing our expenses. We were successful at this task and it contributed to a very satisfying combined ratio of 83.4 percent. We are committed to maintaining our dedication to prudent fiscal management, which along with our conservative investment strategy, assures that our assets will be managed wisely.

Given the climate of the marketplace, we are cognizant that we need to be concerned about the future, which looks to have its own challenges. With the possibility that we may experience a decrease in market share we must look for other opportunities to remain profitable. This has led us from a tactical approach to one that is more strategic, which we anticipate will allow us to grow without compromising the quality of our business.

As for our future plans to maintain this core business, we will continue to build upon what has proven well for us in the past. That is, we will select only the best risks, aggressively defend non-meritorious claims against our policyholders and work with each of you to reduce risk in the clinical setting, to prevent claims from occurring in the first place.

While commitment may be hard to measure, we feel that the proof of our commitment to you is in our experience. In turn, we would like to thank you for your commitment to us as evidenced by your loyalty over the years.

Sincerely,

Richard W. Brewer

Richard W. Brewer
President & CEO

Richard W. Brewer
President & CEO

ProMutual Group's commitment to our policyholders is the cornerstone of our operations.

Endure

A commitment to defending good medicine and advocating patient safety.

For more than three decades, ProMutual Group, together with its predecessors, has been a reliable and trusted provider of medical liability insurance. We've successfully endured, navigated, and responded to turbulent market cycles, evolving social and economic drivers, and rapid advances in medical technology to create the lasting stability our policyholders require.

Disciplined

Throughout our history, we have maintained a long-term vision and have consistently applied a measured, careful response to changes in the market, enabling development of a strong asset base and adequate reserves against future liabilities. In addition, by insuring those healthcare professionals that meet our underwriting standards in each state, we maintain a superior quality of business. This financial and underwriting discipline allows us to pay any current and future claims regardless of how long it takes for those claims to settle or arise.

Innovative

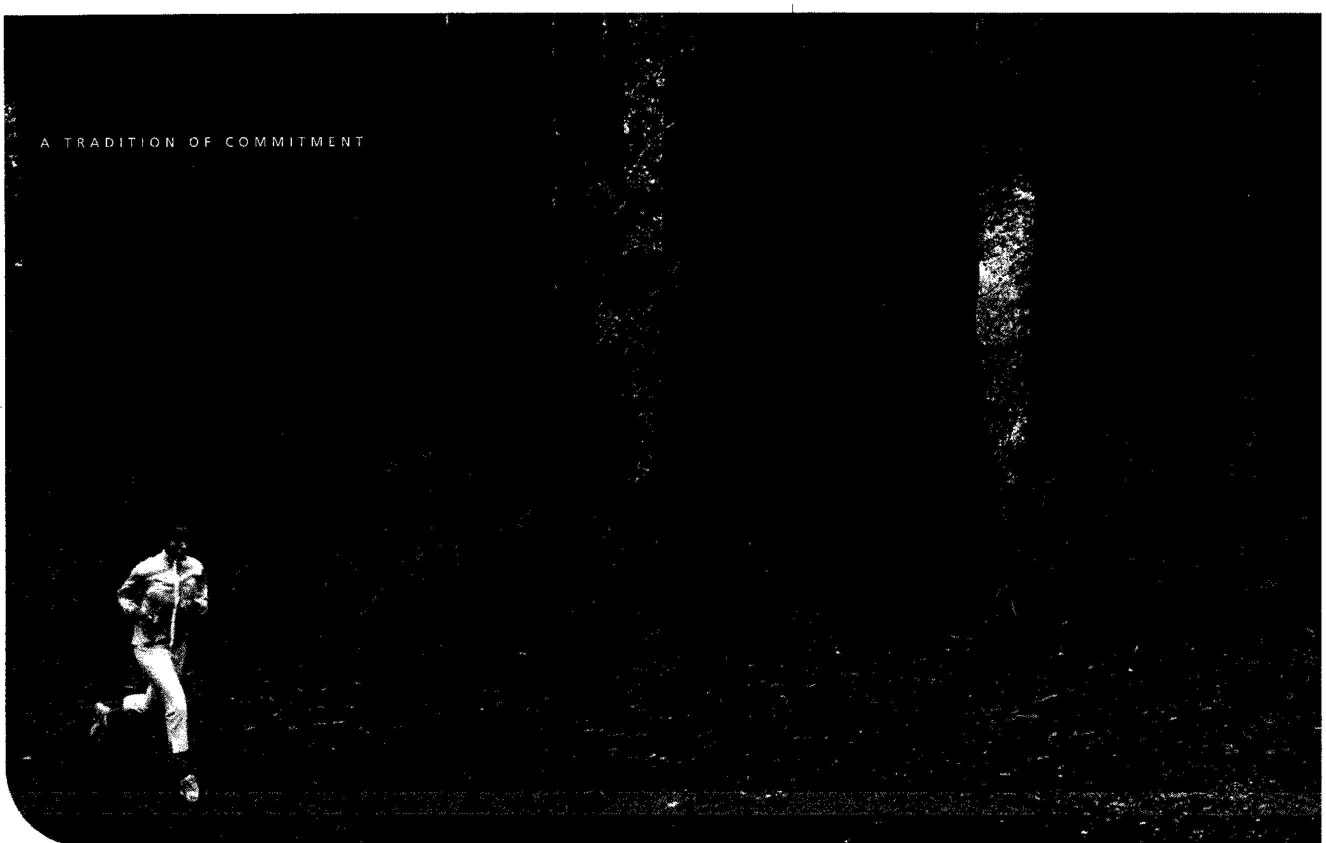
Over the years, we have witnessed the appearance of countless new sources of liability risk. In response, ProMutual Group has remained committed to the identification and understanding of emerging risks and to the development and implementation of strategies to minimize the exposure of policyholders. We have a heritage of providing innovative, proactive risk management programs, educating doctors, hospitals and clinics on ways to increase patient safety, reduce the incidence of negative outcomes, and, ultimately, decrease the incidence of lawsuits.

Gregg L. Hanson
Senior Vice President, Underwriting

"As we respond to trends in healthcare and medical liability, we always have the best interest of our policyholders in mind. Keeping a steady course for policyholders is of utmost importance to ProMutual Group."

Dedicated

Since our founding, ProMutual Group has been dedicated to aggressively defending good medicine and protecting the hard-earned reputations and assets of our policyholders. Our claim staff of experienced nurses, attorneys, and industry professionals has always been counted on to provide exceptional support and protection when one of our policyholders faces a claim.



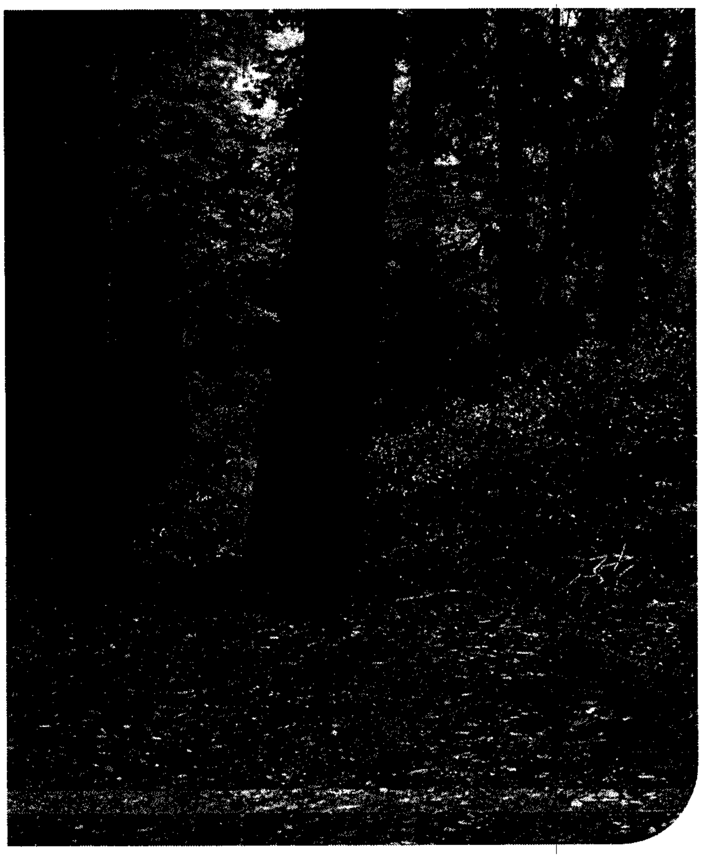
Perform

Furthering our commitment with a strong performance in 2007.

In 2007, we continued to strengthen our financial position and maintained profitability during a period of significant volatility. We supported our policyholders through a variety of risk management and patient safety initiatives. And when claims did arise, we continued to provide policyholders with the best possible defense.

Financial

- In 2007, strong operating gains further enhanced policyholder surplus which was over $602 million at year-end. We were able to retain quality accounts which resulted in an improved combined ratio of 83.4%, compared to 98.6% the prior year.
- Our risk-based capital margin of safety increased to 446% of the required level of risk-based capital.
- In response to the highly leveraged financial markets and the housing market contraction, we reallocated nearly 20% of investment and equities to treasury inflation protected securities (TIPS) which had very positive results for us in 2007, and we decreased our allowed allocation of Fannie Mae and Freddie Mac mortgage-backed securities.
- We had no material exposure to sub-prime, or so-called "toxic," securities.
- Given that we were subject to federal income tax, we increased our allocation to investment grade municipal bonds from 25% to 40%.
- Investment income exceeded our expectations by 3.2%.



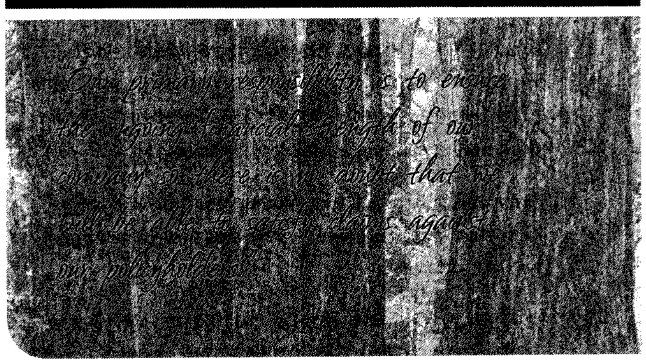
Risk Management

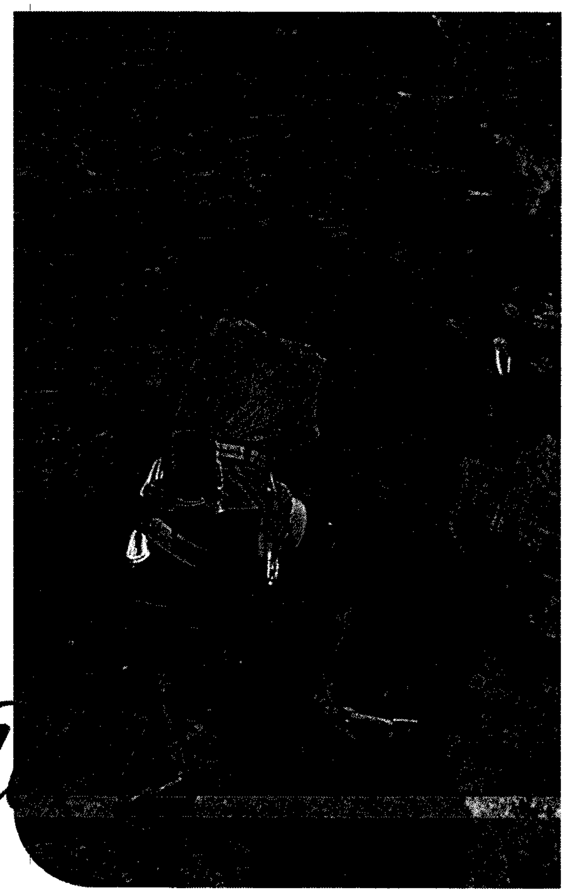
- Our risk management team completed more than 1,000 on-site office and hospital appraisals and provided recommendations tailored to each practice and/or group.
- We developed a risk management module for physician office appraisals focused on electronic medical records.
- We published four issues of *Perspectives on Clinical Risk Management* focusing on EMRs, MRSA, Frequently Asked Questions, and A Sampling of Best Practices.
- We co-authored a paper entitled, "Patient Safety and Telephone Medicine: Some Lessons from Closed Claim Case Review," for publication in the *Journal of General Internal Medicine.*
- We presented a number of seminars to national risk management groups, specialty medical societies, group practices and hospital departments.
- We continued our joint sponsorship of ACCME-accredited programs, including ones that specifically focused on communication.

Claim Services

- We closed nearly 75% of claims without an indemnity payment.
- One-hundred cases went to a trial with a total of 156 defendants. Of those, 101 went to a verdict, 91 of which resulted in a defense verdict. This gave us a verdict win rate of 90% for 2007.
- Policyholders who experienced a claim were surveyed on their satisfaction with the legal services provided to them. For this, we achieved a response rate of 25% and an average score of 4.6/5.0 which translates to a rating of "excellent" in terms of communication skills, representation at scheduled events and at trial.

John J. Donahue
Senior Vice President & Chief Financial Officer





Susta

A commitment to what lies ahead.

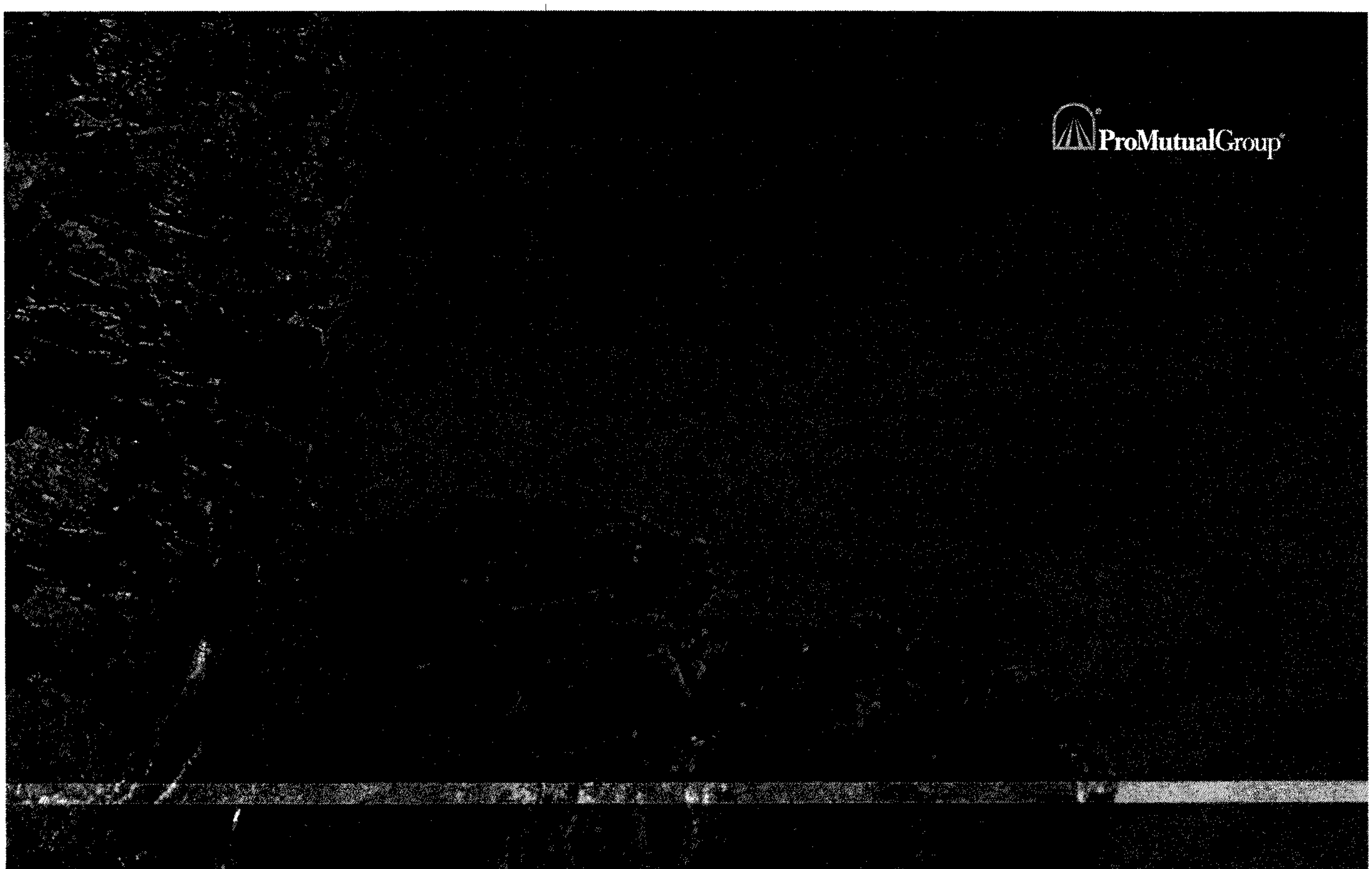
As the future unfolds, we expect change to be constant: market cycles, shifting social and economic conditions, new channels for the delivery of healthcare, and incredible advances in medicine and information technology – all of which bring complex challenges and new risks.

ProMutual Group will remain committed to delivering the best possible underwriting, risk management, and claim services to our policyholders amidst this volatility.

To sustain our strong financial position, we will continue to take a conservative approach to growing investments and we will seek new ways to control costs and enhance operational efficiencies.

Our claim services will continue to evolve, keeping pace with emerging sources of risk and new trends in claim activity.

- When appropriate, we will continue to use alternative dispute resolution on behalf of our policyholders in order to facilitate a trial or the settlement of a claim. This includes arbitration to resolve a claim or mediation to effect a reasonable settlement.
- We will continue to expand our Online Legal Expert database to support defense counsel in more effective and efficient ways to cross-examine plaintiff experts. The database now offers more than 90,000 pages of depositions and transcripts of past testimony of plaintiff experts.
- Our in-depth screening and interview process ensures we will always offer our policyholders superior defense counsel with expertise in defending healthcare providers. In preparation for the future, our mentoring program enables less-experienced attorneys to gain the necessary experience needed to lead a malpractice defense.



Michael R. Kubik
Vice President, Marketing

"Creating and sustaining stability for policyholders stems from our deep understanding of the concerns of healthcare providers and our ability to effectively respond."

ProMutual Group has steadfastly worked on addressing failure to diagnose issues for policyholders and their patients. We have developed risk management approaches based on our analysis of claims data associated with this important area of medical malpractice.

In 2007, we approached the Institute for Healthcare Improvement (IHI) with a goal of developing improved strategies to help prevent the diagnostic errors which plague the healthcare industry. The process by which these errors occur is being researched as are the best practices that can contribute to developing a reliable diagnostic process.

REPORT OF INDEPENDENT AUDITORS

To the Board of Directors of
Medical Professional Mutual Insurance Company, ProSelect Insurance Company and ProSelect National Insurance Company, Inc.

We have audited the accompanying statutory statements of admitted assets, liabilities and surplus of Medical Professional Mutual Insurance Company, ProSelect Insurance Company, and ProSelect National Insurance Company, Inc. ("ProMutual Group" or the "Companies") as of December 31, 2007 and 2006, and the related statutory statements of income and changes in surplus, and of cash flows for the years then ended. These financial statements are the responsibility of the Companies' management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the combined financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Note 2 to the combined financial statements, the Companies prepared these combined financial statements using accounting practices prescribed or permitted by the states in which the Companies are domiciled, which practices differ from accounting principles generally accepted in the United States of America. The effects on the combined financial statements of the variances between the statutory basis of accounting and accounting principles generally accepted in the United States of America are material; they are described in Note 2.

In our opinion, because of the effects of the matter discussed in the preceding paragraph, the combined financial statements referred to above do not present fairly, in conformity with accounting principles generally accepted in the United States of America, the financial position of the Companies as of December 31, 2007 and 2006, or the results of its operations or its cash flows for the years then ended.

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the admitted assets, liabilities and surplus of the Companies as of December 31, 2007 and 2006, and the results of its operations and its cash flows for the years then ended, on the basis of accounting described in Note 2.

PricewaterhouseCoopers LLP

April 22, 2008

COMBINED STATEMENTS OF ADMITTED ASSETS, LIABILITIES, AND ACCUMULATED SURPLUS
(STATUTORY BASIS)
DECEMBER 31, 2007 AND 2006
(IN THOUSANDS)

	2007	2006
Admitted Assets		
Cash and investments		
Bonds, at carrying value	$ 1,818,736	$ 1,622,480
Common and preferred stocks, at carrying value	203,072	220,220
Cash and short-term investments	41,144	91,309
Other invested assets	4,132	4,132
Total cash and investments	2,067,084	1,938,141
Premiums receivable	95,577	101,092
Interest and dividends accrued	16,850	12,996
Federal income tax recoverable	-	1,853
Net deferred tax asset	19,075	16,777
Electronic data processing equipment, net	571	609
Reinsurance recoverable on paid losses and loss adjustment expenses	3,902	177
Equity in pool	26,472	28,463
Other assets	5,065	5,132
Total admitted assets	$ 2,234,596	$ 2,105,240
Liabilities and Accumulated Surplus		
Liabilities		
Loss and loss adjustment expense reserves	$ 1,359,314	$ 1,326,139
Unearned premiums	168,241	174,219
Advance premiums	6,502	7,206
Commissions payable and contingent commissions	5,655	6,430
Ceded reinsurance premiums payable, net of ceding commissions	2,271	1,830
Funds held by Company under reinsurance treaties	59,502	64,622
Policyholder dividends declared	1,229	1
Payable for securities purchased	960	7,516
Federal income tax payable	13,320	-
Other liabilities	14,787	12,587
Total liabilities	1,631,781	1,600,550
Accumulated surplus	602,815	504,690
Total liabilities and accumulated surplus	$ 2,234,596	$ 2,105,240

The accompanying notes are an integral part of the combined financial statements.

COMBINED STATEMENTS OF INCOME AND ACCUMULATED SURPLUS
(STATUTORY BASIS)
YEARS ENDED DECEMBER 31, 2007 AND 2006
(IN THOUSANDS)

	2007	2006
Premiums written	$ 316,336	$ 341,472
Decrease (increase) in unearned premiums	6,503	(3,741)
Premiums earned	322,839	337,731
Loss and loss adjustment expenses	217,549	270,187
Commissions	19,889	24,698
Taxes, licenses and fees	8,128	8,289
Other	22,583	20,938
	268,149	324,112
Underwriting gain	54,690	13,619
Net investment income (Note 3)	91,979	81,578
Net realized gains (Note 3)	12,259	6,021
Finance and service charge income	2,102	2,182
Other expense	(6,842)	(6,128)
Dividends to policyholders (Note 11)	(2,831)	(1,900)
Income before federal income taxes	151,357	95,372
Federal income tax expense (Note 4)	40,972	22,222
Net income	$ 110,385	$ 73,150
Accumulated surplus at beginning of year	$ 504,690	$ 410,210
Net income	110,385	73,150
Net unrealized capital (losses) gains (Note 3)	(9,053)	15,609
Decrease in net deferred income tax	(1,355)	(8,118)
(Increase) decrease in nonadmitted assets (Note 7)	(1,830)	12,201
(Increase) decrease in provision for reinsurance	(22)	1,638
Accumulated surplus at end of year	$ 602,815	$ 504,690

The accompanying notes are an integral part of the combined financial statements.

COMBINED STATEMENTS OF CASH FLOWS
(STATUTORY BASIS)
YEARS ENDED DECEMBER 31, 2007 AND 2006
(IN THOUSANDS)

	2007	2006
Operating activities		
Premiums collected, net of reinsurance	$ 322,242	$ 333,902
Investment income, net	90,677	86,172
Miscellaneous expenses	(4,169)	(3,893)
Benefits and loss related payments	(131,915)	(118,913)
Commissions and expenses paid	(105,168)	(121,165)
Dividends paid to policyholders	(1,603)	(1,899)
Federal income taxes paid	(34,259)	(24,394)
Net cash provided by operating activities	135,805	149,810
Investing activities		
Proceeds from bonds sold, matured or repaid	577,258	890,542
Proceeds from stocks sold	209,481	112,942
Proceeds from other invested assets	178	162
Total investment proceeds	786,917	1,003,646
Cost of bonds acquired	(779,719)	(1,080,942)
Cost of stocks acquired	(190,008)	(108,733)
Total investments acquired	(969,727)	(1,189,675)
Net cash used in investing activities	(182,810)	(186,029)
Total other cash (applied) provided	(3,160)	2,615
Net decrease in cash and short-term investments	(50,165)	(33,604)
Cash and short-term investments, beginning of year	91,309	124,913
Cash and short-term investments, end of year	$ 41,144	$ 91,309

The accompanying notes are an integral part of the combined financial statements.

NOTES TO COMBINED FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006
(IN THOUSANDS)

1. Business

The combined financial statements include the accounts of Medical Professional Mutual Insurance Company, ProSelect Insurance Company and ProSelect National Insurance Company, Inc. ("ProMutual Group" or the "Companies"). ProMutual Group is the largest writer of medical malpractice insurance in The Commonwealth of Massachusetts.

Medical Professional Mutual Insurance Company ("ProMutual") is licensed to write various lines of insurance in Massachusetts.

ProSelect Insurance Company ("ProSelect") is licensed to write various lines of insurance in the states of Connecticut, Maine, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island and Vermont, and is currently writing in all but New York.

ProSelect National Insurance Company, Inc. ("ProSelect National") is licensed to write various property and casualty lines of insurance in twenty-seven states, but is not currently insuring risks.

2. Basis of Presentation and Significant Accounting Policies

Statutory Basis of Accounting

The combined financial statements of the Companies have been prepared on a statutory basis of accounting in accordance with accounting practices prescribed or permitted by The Division of Insurance of The Commonwealth of Massachusetts (Medical Professional Mutual Insurance Company and ProSelect Insurance Company) and the Arizona Department of Insurance (ProSelect National Insurance Company, Inc.). Intercompany amounts have been eliminated.

Statutory accounting practices include a variety of publications of the National Association of Insurance Commissioners ("NAIC"), as well as state laws, regulations and general administrative rules. Statutory accounting practices differ in some respects from accounting principles generally accepted in the United States of America (GAAP). Significant differences include:

a) Statutory accounting requires that policy acquisition costs (principally commissions and premium taxes) be charged to operations when incurred, and ceding commission received on reinsurance agreements related to the acquisition costs of the business ceded be recorded as income when written. Under GAAP, these items would be deferred and then recognized ratably over the policy period.

b) Under statutory accounting, certain assets designated as "nonadmitted assets" (principally premiums over three months past due, application software, prepaid expenses and office furniture and equipment) are charged directly to accumulated surplus. Under GAAP, the Companies would maintain a reserve for doubtful accounts based upon estimated collectibility, recognize an asset on

NOTES TO COMBINED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

(IN THOUSANDS)

the balance sheet for prepaid expenses and office furniture and equipment and software would be recognized at net depreciated cost.

c) Ceded reinsurance balances relating to unpaid loss and loss adjustment expenses are presented as offsets to reserves; under GAAP, such amounts would be presented as reinsurance recoverable; moreover, under statutory accounting, a provision for reinsurance is established for unsecured recoverable balances from reinsurers which are not authorized which is not recognized under GAAP.

d) Statutory accounting requires that certain debt securities be stated at amortized cost. Bonds with ratings of 3 or lower are stated at the lower of amortized cost or NAIC market value. Under GAAP, debt securities are classified as trading or available for sale, which are valued at fair value, or as held to maturity and valued at amortized cost.

e) Under statutory accounting, classification of certain items on the statement of cash flows differs from GAAP. A reconciliation of indirect cash flows is not presented in the statutory basis cash flow statement, but would be required under GAAP.

f) Under statutory accounting, majority owned insurance and noninsurance subsidiaries are not consolidated. Under GAAP, such subsidiaries would be consolidated.

g) The Companies account for income taxes under the asset and liability method. Deferred federal income taxes are generally recognized when assets and liabilities have different values for financial statement carrying amounts and their respective tax bases. However, the realization on any resulting deferred tax asset is subject to certain criteria in accordance with SSAP 10, *Income Taxes.*

The following is a reconciliation of policyholders' surplus on a statutory basis to policyholders' surplus presented on a GAAP basis for the Companies:

	2007	2006
Policyholders' surplus, statutory basis	$ 602,815	$ 504,690
Valuation adjustments on investments	12,990	(7,526)
Deferred policy acquisition costs	18,678	19,949
Deferred federal income taxes	29,644	33,189
Other, net	2,450	2,316
Nonadmitted assets	4,551	5,196
Provision for reinsurance	22	-
Policyholders' surplus, GAAP	$ 671,150	$ 557,814

The net income for the Companies determined in accordance with GAAP for the years ended December 31, 2007 and 2006 was $108,913 and $63,934, respectively.

NOTES TO COMBINED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

(IN THOUSANDS)

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with statutory accounting practices requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Short-Term Investments

For financial statement purposes, the Companies consider all cash and investments with maturities of less than one year at the time of their acquisition to be cash and short-term investments. Short-term investments, consisting primarily of money market funds, are stated at cost, which approximates fair value.

The Companies invest their excess short-term funds in repurchase agreements with reputable third party financial institutions. Funds are debited from the Companies' accounts on a nightly basis, earn a predetermined rate of interest, and are redeposited in full the following business day. The funds are fully collateralized, as required by the Companies' policy, by bank-owned government agency securities.

Investments

The Companies employ New England Asset Management, Inc., Wellington Management Co., L.L.P., Advent Capital Management, L.L.C. and NISA Investment Advisors L.L.C. ("NISA") to furnish investment management services. These investment fund managers, subject to the supervision of the Board of Directors, direct the investments of the Companies in accordance with established investment objectives, policies and limitations. For their services under their respective contracts, NISA receives a contractual flat annual fee and all other fund managers receive a monthly management fee calculated based on market values. During 2007 and 2006, the Companies incurred aggregate management fees of approximately $2,205 and $2,055, respectively.

Valuation of investments is determined in accordance with the requirements, methods and values adopted by the NAIC, which provide that bonds, so qualified, be carried at amortized cost, preferred stock, so qualified, be carried at cost and other preferred and common stocks and other bonds at fair values established by the NAIC. The Companies have elected to use the retrospective method on loan-backed securities. The Companies use the scientific method for amortizing their debt securities.

The Companies value their investment in subsidiary pursuant to the equity method using audited GAAP equity adjusted for statutory requirements, as is required under the rules promulgated by the NAIC.

NOTES TO COMBINED FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006
(IN THOUSANDS)

Realized capital gains and losses on the sale of investments are included in net income and are determined on a specific identification basis. Where declines in securities' values are deemed other than temporary, the securities are reported at market value and the loss is reported as a component of net realized gains (losses). Unrealized capital gains and losses from the valuation of nonqualified bonds and equity investments at market are credited or charged directly to accumulated surplus.

The Companies participate in a securities lending program to maximize investment income. Certain investment securities are exchanged for collateral, consisting of cash or U.S. Government securities, equal to at least 102% of the fair value of the investment securities on loan. The fair value of the loaned investment securities is monitored on a daily basis, with additional collateral obtained or refunded as the fair value of the loaned investment securities fluctuates. The collateral is retained and invested by a custodian to generate additional investment income.

Reinsurance
In the normal course of business, the Companies seek to reduce the losses that cause unfavorable underwriting results by reinsuring certain levels of risk in various areas of exposure with other insurance enterprises or reinsurers. Amounts recoverable from reinsurers are estimated in a manner consistent with the associated claim liabilities.

Premiums Earned and Unearned
Premiums are recorded as earned on a daily pro rata basis over the terms of the policies. Unearned premiums represent the portion of premiums written applicable to the unexpired terms of the policies in force. A statutory premium deficiency reserve relating to insurance contracts is recognized if the sum of the expected loss and loss adjustment expenses, dividends to policyholders, and maintenance costs exceed the related unearned premiums. The Companies anticipate investment income in determining the need for a premium deficiency reserve.

Loss and Loss Adjustment Expense Reserves
Liabilities for losses and loss adjustment expenses represent the estimated ultimate net cost of all unpaid reported and unreported claims. These estimates are continuously reviewed and modified to reflect current conditions and any adjustments are reflected in current operating results. The Companies anticipate salvage and subrogation in recording their loss and loss adjustment expense reserves. The Companies do not discount their loss and loss adjustment expense reserves (Note 5).

Depreciation
The provision for depreciation on electronic data processing equipment is computed on the straight-line method over the assets' estimated useful lives of three years.

NOTES TO COMBINED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

(IN THOUSANDS)

3. Investments

At December 31, 2007 and 2006, the amortized cost, NAIC market values and gross unrealized gains and losses of investments in securities are as follows:

	2007			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	NAIC Market Value
U.S. Treasury and obligations of U.S. Government and agencies	$ 240,815	$ 10,630	$ (409)	$ 251,036
Obligations of states and political subdivisions	556,814	3,951	(5,617)	555,148
Industrial and miscellaneous	319,247	6,819	(7,390)	318,676
Asset-backed securities	701,852	3,923	(4,324)	701,451
Total bonds	$ 1,818,728	$ 25,323	$ (17,740)	$ 1,826,311

	2007			
	Cost	Gross Unrealized Gains	Gross Unrealized Losses	NAIC Market Value
Preferred stock	$ 29,191	$ 1,925	$ (1,203)	$ 29,913
Common stock	131,397	44,923	(2,845)	173,475
Investment in subsidiary	4,090	-	(2,699)	1,391
Total stocks	$ 164,678	$ 46,848	$ (6,747)	$ 204,779

	2006			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	NAIC Market Value
U.S. Treasury and obligations of U.S. Government and agencies	$ 193,782	$ 451	$ (2,107)	$ 192,126
Obligations of states and political subdivisions	331,522	1,202	(697)	332,027
Industrial and miscellaneous	315,014	6,648	(5,574)	316,088
Asset-backed securities	782,691	1,973	(11,096)	773,568
Total bonds	$ 1,623,009	$ 10,274	$ (19,474)	$1,613,809

	2006			
	Cost	Gross Unrealized Gains	Gross Unrealized Losses	NAIC Market Value
Preferred stock	$ 13,037	$ 1,237	$ (442)	$ 13,832
Common stock	148,979	57,785	(772)	205,992
Investment in subsidiary	4,090	-	(2,439)	1,651
Total stocks	$ 166,106	$ 59,022	$ (3,653)	$ 221,475

NOTES TO COMBINED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

(IN THOUSANDS)

Other investments represent amounts invested in a LLC, accounted for under the cost method.

The amortized cost and NAIC market value of debt securities at December 31, 2007, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	2007	
	Amortized Cost	NAIC Market Value
Due in one year or less	$ 42,504	$ 42,501
Due after one year through five years	273,110	276,673
Due after five years through ten years	333,838	337,622
Due after ten years	467,424	468,064
Asset-backed securities	701,852	701,451
	$ 1,818,728	$ 1,826,311

At December 31, 2007 and 2006, the Companies held investments in certain bonds with an NAIC rating of 3 or lower. This resulted in a $2,582 and $708 reduction to the investment balance at December 31, 2007 and 2006, respectively, which was reflected as an unrealized loss for statutory reporting purposes. Additionally, $2,590 and $178 was recorded as unrealized gains on treasury inflation-protected securities in 2007 and 2006, respectively.

Management believes that the gross unrealized losses reflected on ProMutual Group's fixed income portfolio as of December 31, 2007 were primarily the result of increases in market interest rates from the time of acquisition to the current period. These decreases in value are viewed as being temporary as ProMutual Group has the intent and ability to retain such investments for a period of time sufficient to allow for any anticipated recovery in market value. The majority of the debt securities that are in an unrealized loss position are highly rated by the Securities Valuation Office (SVO) of the NAIC and are therefore not required to be written down under NAIC guidelines. An unrealized loss on equity securities of $2,699 relates to a wholly owned subsidiary, for which management has the ability and intent to hold for sufficient recovery. Management also believes that the remaining gross unrealized losses recorded on ProMutual Group's domestic equity portfolio as of December 31, 2007 were primarily the result of routine fluctuations in market prices as opposed to the issuer's financial condition. Therefore, these decreases in value are also viewed as being temporary. In compliance with statutory regulations, the Companies obtain market prices and NAIC designations from the SVO of the NAIC. All statutory unrealized losses have a direct impact on the Companies' policyholders' surplus.

NOTES TO COMBINED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

(IN THOUSANDS)

December 31, 2007	Under 12 Months	Over 12 Months	Totals
Debt securities			
Number of positions	170	277	447
NAIC market value	$ 356,347	$ 496,109	$ 852,456
Amortized cost	365,908	504,288	870,196
Unrealized loss	$ (9,561)	$ (8,179)	$ (17,740)
Equity securities			
Number of positions	64	1	65
NAIC market value	$ 46,893	$ 1,391	$ 48,284
Cost	50,941	4,090	55,031
Unrealized loss	$ (4,048)	$ (2,699)	$ (6,747)
Total			
Number of positions	234	278	512
Carrying value	$ 403,240	$ 497,500	$ 900,740
Cost	416,849	508,378	925,227
Unrealized loss	$ (13,609)	$ (10,878)	$ (24,487)

Proceeds from the sale of investments during 2007 and 2006 were $653,785 and $848,375, respectively. Gross gains of $11,516 and $14,200 and gross losses of $7,390 and $16,643 were realized on sales of debt securities during 2007 and 2006, respectively. Gross gains of $29,872 and $13,509 and gross losses of $12,419 and $3,809 were realized on sales of equity securities during 2007 and 2006, respectively. The calculation of the gain or loss on the sale of marketable securities is based on specific identification at the time of sale. In addition, the Companies realized $1,038 and $0 losses in 2007 and 2006, respectively, due to other than temporary declines in securities' market value.

Net investment income for 2007 and 2006 consisted of the following:

	2007	2006
Interest and dividend income	$ 94,350	$ 83,788
Investment expenses	(2,371)	(2,210)
Net investment income	91,979	81,578
Net realized gains (less capital gains tax of $8,460 in 2007 and $1,789 in 2006)	12,259	6,021
Net investment gain	$ 104,238	$ 87,599

NOTES TO COMBINED FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006
(IN THOUSANDS)

The Companies participate in a securities lending program where they loan certain investment securities in exchange for collateral, consisting of cash or U.S. government securities, equal to at least 102% of the fair value of the investment securities on loan. As of December 31, 2007 and 2006, investment securities with a fair value of $316,392 and $260,469, respectively, were on loan. Investment income earned on securities lending transactions for 2007 and 2006 was $433 and $289, respectively.

4. Federal Income Taxes

The main components of the Companies' deferred tax asset and deferred tax liability as of December 31, 2007 and 2006 are as follows:

	2007	2006
Total of gross deferred tax assets	$ 77,957	$ 78,382
Total of deferred tax liabilities	14,915	20,113
Net deferred tax asset	63,042	58,269
Deferred tax asset nonadmitted	(43,967)	(41,492)
Net admitted deferred tax asset	19,075	16,777
Increase (decrease) in nonadmitted asset	$ 2,475	$ (12,873)

The Companies have no unrecognized deferred tax liabilities.

Current income taxes incurred consist of the following major components:

	2007	2006
Current income tax expense on operations	$ 40,923	$ 21,943
Realized capital gains tax	8,460	1,789
Prior year underaccrual	49	279
Total income tax expense	$ 49,432	$ 24,011

NOTES TO COMBINED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

(IN THOUSANDS)

Changes in the main components of the Companies' deferred tax asset ("DTA") and deferred tax liability ("DTL") are as follows:

	2007	2006	Change
Deferred tax assets			
Loss and LAE reserves	$ 58,093	$ 58,883	$ (790)
Unrealized capital losses	1,248	347	901
Impairments on investment securities	1,085	722	363
Unearned premium	11,777	12,195	(418)
Deferred compensation plans	1,503	1,339	164
Nonadmitted assets	1,639	1,809	(170)
Other	943	929	14
Alternative minimum tax credit	12	12	-
Loss carryforward	1,657	2,146	(489)
Total DTA	77,957	78,382	(425)
Nonadmitted DTA	(43,967)	(41,492)	2,475
Admitted DTA	33,990	36,890	(2,900)
Deferred tax liabilities			
Unrealized capital gains	14,727	19,954	(5,227)
Other	188	159	29
Total DTL	14,915	20,113	(5,198)
Net admitted DTA	$ 19,075	$ 16,777	$ 2,298

The change in net deferred income taxes is comprised of the following:

	2007	2006	Change
Total deferred tax assets	$ 77,957	$ 78,382	$ (425)
Total deferred tax liabilities	14,915	20,113	(5,198)
Net deferred tax asset	$ 63,042	$ 58,269	4,773
Tax effect on unrealized gains (losses)			(6,128)
Change in net deferred income tax			$ (1,355)

In accordance with SAAP 10, the Companies have nonadmitted that portion of the deferred tax asset that is not expected to be realized in the next year.

The provision for federal and foreign income taxes incurred is different from that which would be obtained by applying the statutory federal income tax rate to income before taxes. The significant items causing this difference are as follows:

NOTES TO COMBINED FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006
(IN THOUSANDS)

	2007	Effective Tax Rate
Provision computed at statutory rate	$ 55,936	35.0%
Tax-exempt income deduction	(5,127)	(3.2%)
Dividends received deduction	(1,870)	(1.2%)
Other	1,849	1.2%
	$ 50,788	31.8%
Federal and foreign income taxes incurred	$ 49,433	30.9%
Change in net deferred income taxes	1,355	0.9%
Total statutory income taxes	$ 50,788	31.8%

At December 31, 2007, the Companies had an operating loss carryforward originating in 2005 in the amount of $3,953, which will expire, if unused, in 2025. In addition, the Companies had capital loss carryforwards originating in 2005 and 2007 in the amounts of $708 and $76, respectively, which will expire, if unused, in 2010 and 2012, respectively. The Companies also have AMT credits of $12 that do not expire.

The Companies have $49,383 and $21,855 income taxes incurred in the current or prior years, respectively, that are available for recoupment in the event of future net losses.

The Companies file a consolidated federal income tax return with their affiliates, which include ProMutual Group, Inc. and ProMutual Insurance Agency, Inc.

The method of allocation between the Companies is subject to written agreement, approved by the Board of Directors. The consolidated tax liability is allocated to the Member Companies in accordance with Reg. Section 1.1502-33 (d)(2)(ii) in conjunction with the method provided by Reg. Section 1.1552-1(a)(2) of the Internal Revenue Code whereby the tax is computed on an "as if separate return" basis. Intercompany tax balances are settled annually.

5. Loss and Loss Adjustment Expense Reserves

The loss and loss adjustment expense reserves at December 31, 2007 and 2006 consisted of the following:

	2007	2006
Reported claims		
Losses	$ 542,050	$ 542,259
Loss adjustment expenses	305	514
	542,355	542,773
Claims incurred but not yet reported		
Losses	473,859	459,335
Loss adjustment expenses	343,100	324,031
	816,959	783,366
Loss and loss adjustment expense reserves	$ 1,359,314	$ 1,326,139

NOTES TO COMBINED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

(IN THOUSANDS)

The activity in the liability for unpaid loss and loss adjustment expenses is summarized as follows:

	2007	2006
Balance at January 1	$ 1,326,139	$ 1,234,774
Payments made on claims existing at January 1	(180,279)	(173,472)
Decrease in liability on claims existing at January 1	(91,216)	(49,236)
Balance at December 31 on prior year claims	1,054,644	1,012,066
Estimated losses on new claims	308,764	319,423
Payments made on new claims	(4,094)	(5,350)
Balance at December 31 on current year claims	304,670	314,073
Total loss and loss adjustment expense reserves at December 31	$ 1,359,314	$ 1,326,139

These liabilities include estimates of expected trends in claim severity, frequency and other factors which could vary as the claims are ultimately settled. In establishing the reserve for losses and loss adjustment expenses, the Companies have relied upon their independent actuaries to review the reasonableness of management's best estimates. These recommendations are based principally upon the historical experience of the Companies in writing medical malpractice. As a result of changes in estimates of insured events in prior years, the liability on claims existing at January 1, 2007 and 2006, respectively, decreased $91,216 and $49,236 for the years ended December 31, 2007 and 2006, respectively, primarily related to coverage years 2002 through 2006 predominantly in the physicians and surgeons line of business.

Claims in the medical malpractice line of insurance have traditionally been characterized by delayed discovery and reporting and, in many cases, the final payment of claims is dependent upon the outcome of litigation. As a result, the total of claims paid from the premiums earned in any policy year will not be known for many years.

6. Leases

The Companies occupy office facilities under an operating lease agreement which expires on February 29, 2016. Total rent expense was $1,564 and $1,557 for 2007 and 2006, respectively.

Minimum annual rental commitments as of December 31, 2007 under the operating lease are as follows:

Fiscal Year	
2008	$ 1,556
2009	1,604
2010	1,651
2011	1,698
2012	1,746
Thereafter	5,838

NOTES TO COMBINED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

(IN THOUSANDS)

7. Nonadmitted Assets

Certain assets, designated as nonadmitted by The Division of Insurance of The Commonwealth of Massachusetts and the Arizona Department of Insurance, were directly charged to accumulated surplus as follows:

	2007	2006
Premiums receivable over three months due	$ 870	$ 1,517
Funds held by reinsured companies	34	34
Nonadmitted deferred income tax	43,967	41,492
Equipment, furniture and application software	2,261	2,334
Accounts receivable	59	57
Prepaid expenses and deposits	1,327	1,254
	$ 48,518	$ 46,688

8. Statutory Requirements

Regulatory limits restrict the amount of dividends that can be remitted to a company from its insurance subsidiaries without approval of state insurance regulators. The maximum amount of dividends which can be paid to shareholders by ProSelect without prior approval of the insurance commissioner is the greater of 10% of policyholder surplus as of the prior year-end or the net income for the twelve months ending the prior December 31. The maximum amount of dividends which can be paid to shareholders by ProSelect National without prior approval of the insurance commissioner is the lesser of 10% of policyholder surplus as of the prior year-end or the net investment income for the twelve months ending the prior December 31. No stockholder dividends were declared or paid in 2007.

9. EDP Equipment

EDP equipment at December 31, 2007 and 2006 consisted of the following:

	2007	2006
EDP equipment	$ 2,167	$ 1,873
Less: Accumulated depreciation	(1,596)	(1,264)
	$ 571	$ 609

Depreciation expense was $332 and $342 during 2007 and 2006, respectively.

10. Employee Benefit Plans

The Companies' employees are covered by a qualified defined contribution pension plan sponsored by ProMutual. A contribution was made in 2007 in the amount of $671 for 2006 that was based on each employee's age and average salary over the most recent five years to meet a target benefit. A contribution of approximately $700 will be made for 2007 in 2008.

The Company sponsors a 401(k) Employee Savings Plan. Substantially all employees of the Companies are eligible to participate in the Companies' Employee Savings Plan under which a portion of employee contributions are matched by the Companies. The match by the Companies was $722 and $520 in 2007 and 2006, respectively.

The Companies' executives and members of their Board of Directors are also eligible to participate in a deferred compensation plan.

11. Dividends to Policyholders

On June 7, 2006, the Board of Directors of ProMutual voted to pay a dividend of $1,900 related to the experience of the dental line of business for calendar years 1986 through 1999 allocated to dentists based on their respective premiums earned by the Company during the period. The dividends were paid in November and December 2006.

On June 6, 2007, the Board of Directors of ProMutual voted to pay a divided of $1,600 related to the experience of the dental line of business for calendar years 1986 through 1999 allocated to dentists based on their respective premiums earned by the Company during the period. The dividends were paid in September 2007.

On December 12, 2007, the Board of Directors of ProMutual voted to pay a dividend to physician and surgeon professional liability policyholders in The Commonwealth of Massachusetts on policies expiring between July 1, 2008, and June 30, 2009, in the amount of 5% of the premium paid by such policyholders. The amount accrued at December 31, 2007 was $1,229.

12. Reinsurance

Reinsurance is obtained to reduce exposure to large claims. Such ceded reinsurance includes quota share, excess of loss, and facultative contracts, on all lines of insurance. These reinsurance contracts do not relieve the Companies from their obligations to policyholders. Failure of reinsurers to honor their obligations could result in losses to the Companies.

The Companies purchased an excess of loss agreement in 2006 and 2007, providing coverage of 95% of $8 million in excess of $2 million. The principal reinsurers for this contract are Axa Re, Platinum Underwriters Reinsurance, Inc., Max Re Ltd. and Transatlantic Reinsurance Company.

NOTES TO COMBINED FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006
(IN THOUSANDS)

The Companies participate in the Massachusetts Medical Malpractice Reinsurance Plan (MMMRP), a residual market pool. The Companies, as well as other insurance companies, cede policies into the pool on a facultative basis. The MMMRP assesses each participant an amount based on the profitability of the pool and their respective market share by policy year.

As of December 31, 2007 and 2006, a provision for reinsurance has been established in the amounts of $22 and $0, respectively, for unsecured recoverables from unauthorized reinsurers.

Irrespective of the protection afforded against claim exposure by the above reinsurance agreements, the Companies remain liable as the direct insurer to the insured.

The amounts by which unearned premiums, loss reserves, loss adjustment expense reserves, premiums earned and loss and loss adjustment expenses incurred have been decreased for amounts ceded are as follows:

	2007	2006
Unearned premiums	$ 2,867	$ 6,224
Loss reserves	100,137	124,428
Loss adjustment expense reserves	27,562	32,540
Premiums earned	8,987	11,529
Loss and loss adjustment expenses incurred	(9,238)	24,870
Commission equity	683	1,190

The effect of assumed reinsurance from unaffiliated insurers is as follows:

	2007	2006
Unearned premiums	$ -	$ -
Loss reserves	61,327	68,454
Loss adjustment expense reserves	16,812	19,436
Premiums earned	2,764	11,926
Loss and loss adjustment expenses incurred	(5,500)	28,245
Commission equity	-	-

13. Commitments and Contingencies

Various legal claims arise from time to time in the ordinary course of business. In the opinion of management, these claims should not result in judgments or settlements which, in the aggregate, would have a material effect on the Companies' results of operations or financial condition.

On January 3, 2008, ProMutual, as plaintiff, was successful in an arbitration ruling in a reinsurance dispute which required final resolution within 60 days. On February 4, 2008, ProMutual received $4,659 for amounts previously paid. The Companies will record a surplus benefit of $6,460 for the rescission of the reinsurance contract in its first quarter, 2008 financial statements.

NOTES TO COMBINED FINANCIAL STATEMENTS
DECEMBER 31, 2007 AND 2006
(IN THOUSANDS)

14. Reconciliation to Statutory Annual Statement

Certain items in this report differ from corresponding items reflected in the statutory annual statement, and are presented in the table below. The differences are due to the fact that the Companies' accounting treatment for the Massachusetts Medical Malpractice Reinsurance Plan (MMMRP) reflected management's best estimate of anticipated assessments in accordance with SSAP No. 35, *Guaranty Fund and Other Assessments.* Additionally, the related reinsurance transactions were recorded on a gross basis in accordance with SSAP No. 63, *Underwriting Pools and Associations including Intercompany Pools.* Upon further review of the MMMRP rules of operation, it was deemed to be more appropriate to use SSAP No. 63 alone. The increase to net income of $7,753 at December 31, 2006 represents the reversal of the after-tax impact of the net cumulative effect of the adjustments since inception of the MMMRP which was reported in the December 31, 2005 audited financial statements.

	2006
Accumulated surplus as reported in the statutory annual statement	$ 504,690
Increase to underwriting expenses	-
Decrease to federal income tax expense	-
Increase to net deferred income tax asset	-
Increase to nonadmitted assets	-
Accumulated surplus as reported in the audited financial statements	$ 504,690
Net income as reported in the statutory annual statement	$ 65,397
Decrease to underwriting expenses	9,691
Increase to federal income tax expense	(1,938)
Net income as reported in the audited financial statements	$ 73,150

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