

**Alberta Lawyers Indemnity
Association (formerly The Alberta
Lawyers Insurance Association)**

Financial Statements
December 31, 2019



Independent auditor's report

To the Directors of Alberta Lawyers Indemnity Association (formerly Alberta Lawyers Insurance Association)

Our opinion

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of Alberta Lawyers Indemnity Association (formerly Alberta Lawyers Insurance Association) (the Association) as at December 31, 2019 and the results of its operations and its cash flows for the year then ended in accordance with Canadian accounting standards for not-for-profit organizations.

What we have audited

The Association's financial statements comprise:

- the statement of financial position as at December 31, 2019;
- the statement of revenue, expenses and unrestricted net assets for the year then ended;
- the statement of cash flows for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies.

Basis for opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report.

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

Independence

We are independent of the Association in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada. We have fulfilled our other ethical responsibilities in accordance with these requirements.

Responsibilities of management and those charged with governance for the financial statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with Canadian accounting standards for not-for-profit organizations, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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"PwC" refers to PricewaterhouseCoopers LLP, an Ontario limited liability partnership.



In preparing the financial statements, management is responsible for assessing the Association's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Association or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Association's financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Association's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Association's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Association to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.



We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

PricewaterhouseCoopers LLP

Chartered Professional Accountants

Calgary, Alberta
April 24, 2020

Alberta Lawyers Indemnity Association (formerly The Alberta Lawyers Insurance Association)

Statement of financial position

As at December 31, 2019

	2019 \$	2018 \$
Assets		
Cash and cash equivalents (note 2)	22,838,673	6,221,404
Investments (note 4, 9)	175,897,190	164,607,336
Accounts receivable (note 5)	1,459,971	2,834,085
Prepaid expenses	884,930	811,430
Due from related parties (note 8)	152,250	21,744
Accrued interest receivable	-	132,250
Total Assets	<u>201,233,014</u>	<u>174,628,249</u>
Liabilities and Net Assets		
Accounts payable and accrued liabilities	340,569	602,923
Unearned premiums	13,315,274	14,624,003
Premium deficiency (note 14)	3,201,726	2,316,997
Pension plan payable (note 12)	124,160	118,283
Provision for claims and related costs – Professional liability (note 7)	119,331,000	114,369,000
Provision for claims and related costs – Misappropriation indemnity (note 7)	2,158,000	2,539,000
Total liabilities	<u>138,470,729</u>	<u>134,570,206</u>
Net Assets		
Unrestricted	62,762,265	40,058,023
Share capital	20	20
Total Net Assets	<u>62,762,285</u>	<u>40,058,043</u>
Total Liabilities and Net Assets	<u>201,233,014</u>	<u>174,628,249</u>

Approved by the Board of the Association

Steve Raby, QC Director

Dale Spackman, QC Director

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

Alberta Lawyers Indemnity Association (formerly The Alberta Lawyers Insurance Association)

Statement of Revenue, Expenses and Unrestricted Net Assets
For the year ended December 31, 2019

	2019 \$	2018 \$
Revenue		
Premium - Professional liability	24,979,340	27,153,817
Premium – Misappropriation indemnity	3,105,659	3,284,533
Investment income	18,219,018	7,266,299
Unrealized gain (loss) on the fair market value of investments	1,716,114	(5,639,154)
Voluntary excess insurance administration fee	151,266	139,811
	48,171,397	32,205,306
Expenses		
Provision for claims and related costs – Professional liability (note 7)	20,206,718	18,381,300
Provision for claims and related costs – Misappropriation indemnity (note 7)	(161,515)	(515,577)
Premium deficiency (note 14)	884,729	1,030,792
Premium (received)/paid to the Canadian Lawyers Insurance Association (note 13)	(4,555,838)	635,524
Salaries and employee benefits	3,227,987	3,034,374
Management fee (note 8)	2,661,072	3,696,000
Provision for input tax credits (note 16)	-	(4,367,841)
Insurance expense	1,682,360	1,496,180
Investment counsel fees	380,554	349,542
Premium taxes	-	275,810
Bank and credit card fees	450,581	438,599
Professional fees	350,022	584,134
Administration	220,647	189,051
Board expenses	119,838	107,769
	25,467,155	25,335,657
Excess of revenue over expenses for the year	22,704,242	6,869,649
Unrestricted net assets – beginning of year	40,058,043	33,188,394
Unrestricted net assets – end of year	62,762,285	40,058,043

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

Alberta Lawyers Indemnity Association (formerly The Alberta Lawyers Insurance Association)

Statement of Cash Flows

For the year ended December 31, 2019

	2019 \$	2018 \$
Cash provided by (used in)		
Operating activities		
Excess of revenue over expenses for the year	22,704,242	6,869,649
Items not affecting cash		
Gain on sale of investments	(10,732,677)	(1,818,544)
Unrealized (gain) loss on fair market value of investments	(1,716,114)	5,639,154
Provision for claims and related costs – Professional liability (note 7)	20,206,718	18,381,300
Provision for claims and related costs – Misappropriation indemnity (note 7)	(161,515)	(515,577)
	<u>30,300,654</u>	<u>28,555,982</u>
Increase (decrease) in pension plan payable (note 12)	5,877	(28,439)
Changes in non-cash working capital items	483,753	2,258,767
Claims and related costs paid Professional liability – net of recoveries (note 7)	(14,820,339)	(15,023,299)
Claims and related costs paid Misappropriation indemnity– net of recoveries (note 7)	(219,485)	(116,423)
	<u>15,750,460</u>	<u>15,646,588</u>
Investing activities		
Sale of investments	147,610,597	117,955,708
Purchase of investments	(146,743,788)	(137,768,517)
	<u>866,809</u>	<u>(19,812,809)</u>
Increase (decrease) in cash and cash equivalents	16,617,269	(4,166,221)
Cash and cash equivalents – beginning of year	<u>6,221,404</u>	<u>10,387,625</u>
Cash and cash equivalents – end of year	<u>22,838,673</u>	<u>6,221,404</u>
Cash and cash equivalents include:		
Cash	3,792,644	3,373,228
Treasury bills	19,046,029	2,848,176
	<u>22,838,673</u>	<u>6,221,404</u>
Interest received	4,360,558	2,614,954

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

Alberta Lawyers Indemnity Association (formerly The Alberta Lawyers Insurance Association)

Notes to the Financial Statements

For the year ended December 31, 2019

1 Nature of operations

Alberta Lawyers Indemnity Association, formerly the Alberta Lawyers Insurance Association (the Association) is a wholly owned subsidiary of the Law Society of Alberta (the Law Society). Pursuant to section 99(1) of the *Legal Profession Act of Alberta*, the Association administers a program under which active members of the Law Society in private practice (indemnified lawyers) are required to purchase coverage under the Alberta Lawyers' Professional Liability and Misappropriation Indemnity Group Policy (the Policy).

The Association is incorporated in Alberta and is an entity domiciled in Canada and the address of its registered office is Suite 700, 333 11th Avenue, SW, Calgary, Alberta, T2R 1L9.

The financial statements were authorized for issue by the Board of the Association on April 22, 2020.

Professional Liability Indemnity

Under the Professional Liability section (or Part A) of the Policy, indemnified lawyers have coverage for claims and potential claims arising from negligent acts, errors or omissions for \$1,000,000 per occurrence, with an annual aggregate limit of \$2,000,000 per indemnified lawyer.

Prior to July 1, 2014 the Association contracted with the Canadian Lawyers Insurance Association (CLIA) for group Professional Liability coverage subject to a group deductible of \$500,000 for each claim. The Association was subject to premiums and other assessments that arose from the agreement with CLIA. The Association withdrew from CLIA effective June 30, 2014. In its place, the Alberta Lawyers Insurance Exchange (the Exchange) was created effective July 1, 2014. The Exchange was a reciprocal insurance exchange through which the Law Society, the Association, and the members of the Law Society, entered into agreements of mutual indemnification. The Exchange provided the Association with group coverage subject to a deductible of \$500,000 for each claim until June 30, 2019. As at July 1, 2019, the Association assumed coverage for claims under this policy up to the \$1,000,000 per occurrence limit.

For the 2020 and 2019 policy years (for the period July 1 to June 30 annually), the Association (and the Exchange for the 2019 policy year) obtained stop-loss insurance in the amount of \$10,000,000 to cover annual aggregate payments over \$26,000,000 to a maximum of \$36,000,000.

Misappropriation Indemnity

Effective July 1, 2014, the Misappropriation Indemnity section (or Part B) of the Policy provides defined coverage for misappropriation of money or other property entrusted to and received by indemnified lawyers in their capacity as barristers and solicitors and in relation to the provision of professional services. For the 2020 and 2019 policy years, there is a \$5,000,000 per misappropriation limit and a \$25,000,000 profession-wide annual aggregate limit. This coverage is subject to a \$3,000,000 group deductible. Until July 1, 2019 the Association paid the first \$500,000 of a misappropriation claim and the Exchange paid the next \$2,500,000.

For the 2020 and 2019 policy years, the Association (and the Exchange for the 2019 policy year) purchased excess insurance in the amount of \$22,000,000 to cover aggregate payments over \$3,000,000, up to the profession-wide annual aggregate limit of \$25,000,000.

Claims for trust misappropriation arising before July 1, 2014 were covered under the provisions of the Law Society's Assurance Fund.

Alberta Lawyers Indemnity Association (formerly The Alberta Lawyers Insurance Association)

Notes to the Financial Statements

For the year ended December 31, 2019

2 Reconciliation of Association and Exchange

Effective July 1, 2019, and as approved by the Association's Board and the Law Society of Alberta, the assets, liabilities, revenue and expenses of the Exchange were assumed and combined with the operations of the Association. Therefore, the financial statements represent the combined financial position of the Association and of the Exchange for 2019 and 2018.

Statement of Financial Position

Association and Exchange Combined with Eliminations - December 31, 2018

Assets	Association	Exchange	Eliminations	Combined
Cash	3,344,409	28,819	-	3,373,228
Investments	134,332,732	33,122,780	-	167,455,512
Accounts receivable	2,834,085	-	-	2,834,085
Prepaid expenses	2,735,544	167,886	(2,092,000)	811,430
Due (to)/from related parties	26,271	(4,527)	-	21,744
Accrued interest receivable	31,040	101,210	-	132,250
Total Assets	143,304,081	33,416,168		174,628,249
Liabilities and Net Assets				
Accounts payable and accrued liabilities	366,524	236,399	-	602,923
Unearned premiums	14,624,003	2,092,000	(2,092,000)	14,624,003
Premium deficiency	1,965,997	351,000	-	2,316,997
Pension plan payable	118,283	-	-	118,283
Provision for claims and related costs - Professional liability	95,938,000	18,431,000	-	114,369,000
Provision for claims and related costs - Misappropriation indemnity	1,825,000	714,000	-	2,539,000
Total Liabilities	114,837,807	21,824,399		134,570,206
Net Assets				
Contributed capital	-	14,500,000	(14,500,000)	-
Unrestricted	28,466,254	(2,908,231)	14,500,000	40,058,023
Share capital	20	-	-	20
Total Net Assets	28,466,274	11,591,769		40,058,043
Total Liabilities and Net Assets	143,304,081	33,416,168	-	174,628,249

Alberta Lawyers Indemnity Association (formerly The Alberta Lawyers Insurance Association)

Notes to the Financial Statements

For the year ended December 31, 2019

Statement of Revenue, Expenses and Unrestricted Net Assets

Association and Exchange Combined with Eliminations - December 31, 2018

Revenue	Association	Exchange	Eliminations	Combined
Premium - Professional liability	27,153,817	4,271,000	(4,271,000)	27,153,817
Premium - Misappropriation indemnity	3,284,533	531,000	(531,000)	3,284,533
Investment income	6,613,710	652,589	-	7,266,299
Unrealized gain (loss) on fair market value of investments	(5,339,748)	(299,406)	-	(5,639,154)
Management fees	472,600	-	(472,600)	-
Voluntary excess insurance administration fee	139,811	-	-	139,811
	<u>32,324,723</u>	<u>5,155,183</u>	<u>(5,274,600)</u>	<u>32,205,306</u>
Expenses				
Provision for claims and related costs - Professional liability	12,141,920	6,239,380	-	18,381,300
Provision for claims and related costs - Misappropriation indemnity	(512,577)	(3,000)	-	(515,577)
Premium deficiency	679,792	351,000	-	1,030,792
Exchange Premium - Part A	4,271,000	-	(4,271,000)	-
Exchange Premium - Part B	531,000	-	(531,000)	-
Premium paid to CLIA	635,524	-	-	635,524
Salaries and employee benefits and contractors	3,034,374	-	-	3,034,374
Management fee	3,696,000	472,600	(472,600)	3,696,000
Provision for input tax credits	(4,367,841)	-	-	(4,367,841)
Insurance expense	1,196,944	299,236	-	1,496,180
Investment counsel fees	290,265	59,277	-	349,542
Premium taxes	-	275,810	-	275,810
Bank and credit card fees	418,467	20,132	-	438,599
Professional fees	457,817	126,317	-	584,134
Administration	189,051	-	-	189,051
Board expenses	-	107,769	-	107,769
	<u>22,661,736</u>	<u>7,948,521</u>	<u>(5,274,600)</u>	<u>25,335,657</u>
Excess of revenue over expenses for the year	9,662,987	(2,793,338)	-	6,869,649
Unrestricted net assets - beginning of the year	24,303,287	8,885,107	-	33,188,394
Less: Contribution from Association (to Exchange)	(5,500,000)	5,500,000	-	-
Unrestricted net assets - end of the year	<u>28,466,274</u>	<u>11,591,769</u>	<u>-</u>	<u>40,058,043</u>

Alberta Lawyers Indemnity Association (formerly The Alberta Lawyers Insurance Association)

Notes to the Financial Statements

For the year ended December 31, 2019

3 Summary of significant accounting policies

The principal accounting policies applied in the presentation of these financial statements are set out below. These policies have been consistently applied to the periods presented.

a) Basis of preparation

These financial statements are prepared in accordance with Canadian Accounting Standards for not for profit organizations (ASNPO) as issued by the Canadian Accounting Standards Board.

The statement of financial position is presented on a non-classified basis. Assets expected to be realized and liabilities expected to be settled within the Association's normal operating cycle of one year would typically be considered as current, including the following balances: cash and cash equivalents, treasury bills included in investments, prepaid expenses, accrued interest receivable, accounts receivable, due to related parties, accounts payable and accrued liabilities, and unearned premiums.

The following balances are generally comprised of current and non-current amounts: bonds and equity investments included in investments, and the provision for claims and related costs. The current and non-current portions of such balances are disclosed, where applicable, throughout the notes to the financial statements. Some comparative figures from the prior year have changed.

b) Use of estimates and judgment

The preparation of the financial statements in conformity with ASNPO requires management to make estimates and assumptions that affect the reported amount of assets and liabilities as at the date of the financial statements and the reported amounts of revenue and expenses during the reporting periods. Actual results could differ from these estimates.

Information about judgments, estimates and assumptions that have the most significant effect on the amounts reflected in the financial statements is included in note 6 – Provision for claims and related costs.

c) Functional and presentation currency

The financial statements are presented in Canadian dollars, which is also the Association's functional currency.

d) Financial instruments

The Association initially measures financial assets and financial liabilities at cost. It subsequently measures its investments at fair value. The financial assets subsequently measured at amortized cost include cash and cash equivalents, accounts receivable and accrued interest receivable. The financial liabilities subsequently recorded at amortized cost include accounts payable and accrued liabilities.

The Association's investments consist of equity securities, corporate bonds, municipal government bonds, provincial government bonds and federal government bonds. The investment in equity securities which are traded on active markets are recorded at fair value. The Association has elected to record the investments in corporate bonds, municipal government bonds, provincial government bonds and federal government bonds at fair value. Changes in fair value of the investments are recorded on the statement of revenue, expenses and unrestricted net assets.

Alberta Lawyers Indemnity Association (formerly The Alberta Lawyers Insurance Association)

Notes to the Financial Statements

For the year ended December 31, 2019

Financial assets are tested for impairment at the end of each reporting period and when there are indications that the assets may be impaired.

e) Revenue recognition

The Association follows the deferral method for revenue recognition. Amounts received or receivable from indemnified lawyers that pertain to the period subsequent to fiscal year end are recorded as unearned premiums and recorded as revenue in the next fiscal year.

f) Premium income

Premiums are determined annually prior to July 1st, the commencement of the policy year, and amounts are due from indemnified lawyers prior to that date. Premium revenue is recorded evenly throughout the policy year as the services are rendered.

g) Investment income

Investment income comprises interest, dividends, fund distributions, and gains and losses realized on the disposal of investments. Interest and dividends earned on investments are included as revenue on an accrual basis. The change in fair value of investments is recorded in the statement of revenue, expenses and unrestricted net assets as an unrealized gain (loss) on the fair market value of investments.

h) Provision for claims and related costs

The provision for claims and related costs is based upon the change from year to year in the reserve for claims and related costs. The reserve amount is the actuarially determined discounted cost of possible claims and related costs as at the end of the fiscal year.

The Association has engaged a third-party actuary to provide an annual valuation of the reserve for claims and related costs in accordance with the standards of practice adopted by the Canadian Institute of Actuaries. For the purpose of the actuarial valuation, the actuary uses information contained in the Association's financial records.

i) Insurance

The Association enters into insurance contracts with coverage in excess of certain maximum amounts. Estimates of any amounts recoverable from insurers on unpaid claims will be recorded separately from other estimated amounts payable. Amounts recoverable from insurers are estimated in a manner consistent with the liabilities associated with the insurance policy.

Insurance arrangements do not relieve the Association from its obligations to policyholders.

Insurance assets and liabilities are derecognized when the contractual rights are extinguished or expire, or when the contract is transferred to another party.

As of December 31, 2019, no insurance assets have been recorded.

j) Recoveries

Recoveries for claims and related costs from insurers and other third parties are recorded when they can be reasonably estimated, and collectability is reasonably assured. Otherwise, the recovery is recorded when received.

Alberta Lawyers Indemnity Association (formerly The Alberta Lawyers Insurance Association)

Notes to the Financial Statements

For the year ended December 31, 2019

k) Cash and cash equivalents

Cash includes cash on deposit with banks and other highly liquid short-term investments comprised of treasury bills and corporate bonds with an original term to maturity of three months or less.

l) Donated services

A portion of the Association's work is dependent on the services of volunteers, in particular the significant contribution of the Benchers of the Law Society, the Advisory Board and committees of the Advisory Board. These services are not normally purchased by the Association and, due to the difficulty in determining their fair value, donated services are not recognized in these financial statements.

m) Unearned premiums

Indemnity premiums for each fiscal year are billed in advance and recognized as revenue on a monthly basis during the fiscal year. Unearned premiums represent the portion of premiums remaining to be earned at the reporting date.

n) Income taxes

The Association meets the qualifications of a non-profit organization as defined in the *Income Tax Act* and, as such, is exempt from income taxes.

4 Investments

The Association's investments are governed by a Statement of Investment Policies and Goals as approved by the Board of the Association and managed under contract with an investment manager. The Association's investments are carried at fair market value and the statement of revenue, expenses and unrestricted net assets reports both realized and unrealized gains and losses on investments. The Association's investments, which are denominated in Canadian dollars, consist of T-bills, pooled bond funds, and pooled equity investments.

Investments are as follows:

	2019	2018
	\$	\$
T-Bills	-	16,232,883
Bonds	101,892,294	94,568,659
Equities	74,004,896	53,805,794
	<u>175,897,190</u>	<u>164,607,336</u>

5 Accounts Receivable

Accounts receivable consists of the following amounts:

	2019	2018
	\$	\$
Premiums due from indemnified lawyers	366,766	1,815,354
Insurance recoverables due from CLIA	1,093,205	1,018,731
	<u>1,459,971</u>	<u>2,834,085</u>

Alberta Lawyers Indemnity Association (formerly The Alberta Lawyers Insurance Association)

Notes to the Financial Statements

For the year ended December 31, 2019

6 Share capital

On January 30, 2006, the Association was converted from a company limited by guarantee to a company limited by shares. As a result of this conversion, share capital of \$20 was issued representing four common shares; three shares issued to the Law Society and one common share issued to the person from time to time holding the office of Executive Director of the Law Society, as bare trustee for the Law Society.

7 Provision for claims and related costs

The change in the Professional liability provision for claims and related costs is summarized as follows:

	2019 \$	2018 \$
Provision for claims and related costs, Professional liability – beginning of year	114,369,000	111,011,000
Claims paid and accrued	(13,079,148)	(13,146,193)
Related costs paid and accrued	(6,147,577)	(6,694,370)
Recoveries	4,406,386	4,817,264
	<u>(14,820,339)</u>	<u>(15,023,299)</u>
Increase due to claims experience	19,782,339	18,381,299
Provision for claims and related costs, Professional liability – end of year	<u>119,331,000</u>	<u>114,369,000</u>
Case reserves	77,723,000	73,875,000
Provision for adverse deviation	15,808,000	16,903,000
Provision for incurred but unreported claims	25,800,000	23,591,000
Provision for claims and related costs, Professional liability	<u>119,331,000</u>	<u>114,369,000</u>

The change in the Trust safety provision for claims and related costs is summarized as follows:

	2019 \$	2018 \$
Provision for claims and related costs, Misappropriation Indemnity – beginning of year	2,539,000	3,171,000
Claims paid and accrued	(193,709)	(93,080)
Related costs paid and accrued	(25,776)	(23,343)
	<u>(219,485)</u>	<u>(116,423)</u>
(Decrease) due to claims experience	(161,515)	(515,577)
Provision for claims and related costs, Misappropriation Indemnity – end of year	<u>2,158,000</u>	<u>2,539,000</u>
Case reserves	217,000	283,000
Provision for adverse deviation	237,000	332,000
Provision for incurred but unreported claims	1,704,000	1,924,000
Provision for claims and related costs, Trust safety	<u>2,158,000</u>	<u>2,539,000</u>

Alberta Lawyers Indemnity Association (formerly The Alberta Lawyers Insurance Association)

Notes to the Financial Statements

For the year ended December 31, 2019

Included in the Provision for claims and related costs on the statement of revenue, expenses and unrestricted net assets is the increase due to claims experience of \$19,782,339 for Professional liability (2018 - \$18,381,300) and (\$161,515) for Misappropriation indemnity (2018 - \$515,577).

The discount rate applied by the actuary at December 31, 2019 is 2.00% (2018 – 3.10%) which is based on the expected market yield of the Association’s investment portfolio. The Professional liability undiscounted provision balance at December 31, 2019 is \$109,706,000 (2018 – \$106,515,000) and the Misappropriation indemnity undiscounted provision balance at December 31, 2019 is \$2,030,000 (2018 - \$2,415,000).

Actuarial analysis

The process of determining actuarial liabilities necessarily involves the risk that actual results may vary from assumed results. The risk varies in proportion to the length of period covered by each assumption and the potential volatility of the actual results.

The provision for incurred but not reported claims has been estimated for the period using actuarial methods and is based on expected claims development patterns and expected losses.

Sensitivity analysis

The sensitivity analysis below is based on a change in assumption while holding all other conditions constant. In practice, this is unlikely to occur, and changes in some of the assumptions may not be correlated. The table below provides the impact on net income of the most significant assumption changes.

Assumption	Income and equity impact December 31, 2019	Income and equity impact December 31, 2018
	\$	\$
10% increase in incurred but not reported claims	(4,309,000)	(3,208,000)
10% decrease in incurred but not reported claims	4,309,000	3,208,000
1% increase in discount rate impact on claims provision	3,361,000	2,680,000
1% decrease in discount rate impact on claims provision	(3,560,000)	(2,837,000)
1% increase in interest rate impact on bond values	(8,208,000)	(5,105,000)
1% decrease in interest rate impact on bond values	8,208,000	5,105,000

Claims development tables

A review of the historical development of the Association’s insurance estimates provides a measure of the Association’s ability to estimate the ultimate value of claims. The top half of the following tables illustrates how the Association’s estimate of total undiscounted claim costs for each year has changed at successive year-ends. The bottom half of the tables reconcile the cumulative claims to the amount appearing in the statement of financial position.

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Historical Estimate of Ultimates – Part A Net of Reinsurance ('000\$)

Fund Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Total
After 6 months	8,110	8,044	7,807	6,153	7,596	7,460	7,747	9,553	9,238	8,915	11,093	
One year later	19,083	14,325	15,582	12,855	17,392	16,102	18,984	23,124	18,335	20,207		
Two years later	19,427	15,047	16,715	12,754	18,002	17,169	21,626	22,878	22,447			
Three years later	20,764	15,733	19,731	12,930	20,833	15,481	21,173	26,270				
Four years later	20,814	15,784	20,300	15,917	19,996	13,556	23,449					
Five years later	20,768	16,327	19,538	16,178	19,286	16,867						
Six years later	20,779	16,143	19,717	15,460	19,705							
Seven years later	20,846	16,110	20,352	15,509								
Eight years later	20,577	14,799	20,150									
Nine years later	20,569	14,935										
Ten years later	20,569											
Current Estimate of Cumulative Claims	20,569	14,935	20,150	15,509	19,705	16,867	23,449	26,270	22,447	20,207	11,093	211,203
Cumulative payments to date	(20,727)	(13,878)	(16,618)	(13,497)	(13,387)	(7,893)	(8,352)	(8,614)	(5,074)	(2,001)	(42)	(110,082)
Net Liability	(158)	1,057	3,532	2,013	6,318	8,974	15,097	17,657	17,374	18,206	11,051	101,121
Net Liability in Respect of Prior Years												1,050
Net Liability - Internal Claims Admin. Expenses												7,535
Net Liability - Effect of Discounting and PfAD												9,627
Liability recoverable from reinsurers												0
Total Net Liability												119,331

Historical Estimate of Ultimates – Part B Net of Reinsurance ('000\$)

Reported/Calendar Year	2015	2016	2017	2018	2019	Total
End of year	1,591	373	489	349	500	
One year later	1,423	319	299	331		
Two years later	979	241	335			
Three years later	442	264				
Four years later	221					
Current Estimate of Cumulative Claims	221	264	335	331	500	1,651
Cumulative payments to date	(168)	(104)	(107)	(15)	(81)	(474)
Net Liability	53	160	228	316	419	1,177
Net Liability in Respect of Prior Years						0
Net Liability - Internal Claims Admin. Expenses						837
Net Liability - Effect of Discounting and PfAD						127
Liability recoverable from reinsurers						0
Total Net Liability						2,141

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8 Related party transactions

As described in note 4 the Association is a wholly owned subsidiary of the Law Society. During the year, the Association paid the Law Society \$2,661,072 (December 2018 – \$3,696,000) for management fees. The balance receivable from the Law Society at December 31, 2019 of \$152,250 is non-interest bearing and due on demand (2018 – \$21,744).

The elected Benchers of the Law Society and members of the Board include lawyers drawn from law firms across the province. These law firms may at times be engaged by the Association in the normal course of business. During the year ended December 31, 2019, expenses of \$341,839 (2018 - \$3,077,721) were incurred with these law firms. The Benchers and Board members are not involved in retaining these firms.

9 Financial instruments

The Association recognizes financial instruments at fair value upon initial recognition, plus transaction costs in the case of financial instruments measured at amortized cost. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Association has transferred substantially all risks and rewards of ownership. Financial liabilities are derecognized when the obligation is discharged, cancelled, or has expired.

The Association's investments are classified as held for trading or designated at Fair Value Through Profit or Loss (FVTPL) at inception. A financial asset or financial liability is classified as held for trading if it is acquired or incurred principally for the purpose of selling or repurchasing in the short term; or if, on initial recognition, it is part of a portfolio of identifiable financial investments that are managed together and for which there is evidence of a recent actual pattern of short-term profit taking.

Gains and losses arising from changes in the fair value of FVTPL financial instruments are presented in the statement of revenue, expenses and unrestricted net assets as net changes in unrealized gain (loss) on fair market value of investments in the period in which they arise.

All other financial assets and liabilities are measured at amortized cost. Under this method, financial assets and liabilities reflect the amount required to be received or paid, discounted, when appropriate, at the contract's effective interest rate.

Fair value hierarchy

A fair value hierarchy presented below distinguishes the significance and objectivity of the inputs used in determining the fair value measurements of financial instruments. The hierarchy contains the following levels based on the nature of the pricing inputs:

Level 1 – Inputs that reflect unadjusted quoted prices in active markets for identical assets or liabilities that are publicly available at the measurement date.

Level 2 – Inputs other than quoted prices that are observable for the assets or liabilities either directly or indirectly, including inputs in markets that are not considered to be active.

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Notes to the Financial Statements

For the year ended December 31, 2019

Level 3 – Inputs that are largely unobservable. Fair value requires significant management estimate and judgment.

The following table illustrates the fair value classification of the Association’s financial instruments within the fair value hierarchy as at December 31, 2019:

	Estimated fair value (2019)			Estimated fair value (2018)		
	Level 1	Level 2	2019 Total	Level 1	Level 2	2018 Total
	\$	\$	\$	\$	\$	\$
T-Bills	-	-	-	16,232,883	-	16,232,883
Bonds	-	101,892,294	101,892,294	22,662,486	71,906,173	94,568,659
Equities	-	74,004,896	74,004,896	11,110,020	42,695,774	53,805,794
Total Investments	-	175,897,190	175,897,190	50,005,389	114,601,947	164,607,336

Investments classified as Level 2 are held in pooled funds, the underlying assets of which are traded in active markets. The pooled funds are valued based on the net asset value per share of the pooled fund. The Association re-balanced all equities invested in pooled funds at December 31, 2019. There were no transfers between levels in the year ended December 31, 2018. There were no level 3 investments in 2018 or 2019.

10 Insurance

The Association entered into stop loss and excess insurance contracts as described in Note 1.

As of December 31, 2019, there were no claims above the Professional Liability and Misappropriation Indemnity coverage of \$26,000,000 and \$3,000,000 respectively and no claims above these levels considered to be incurred but not reported as determined by the appointed actuary (2018 - NIL). As such, no assets for the insurance or excess insurance contracts have been recognized in the statement of financial position.

11 Insurance and financial risk management

In the normal course of business, the Association enters into contracts that transfer insurance risk or financial risk or both. The Association monitors and manages these risks relating to the operations of the Association through internal risk reports which analyze exposures by degree and magnitude of risk.

Insurance risk

The insurance risk under any one insurance contract is the possibility that the insured event occurs and the uncertainty of the amount of the resulting claim. By the very nature of an insurance contract, this risk is random and therefore unpredictable. The key risk related to insurance is that the actual claims payment amounts or timing are different from expectations.

The Association manages insurance risk rating within an overall risk management framework that includes a focus on rating, use of insurance and surplus management. Insurance is purchased to mitigate the effect of potential loss to the Association from individual large events. Insurance policies are written with insurers who meet the Association’s standards for financial strength. Insurers and insurer security are monitored on a continuous basis.

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Financial risk

The Association is exposed to a range of financial risks. The key financial risk is that in the long term its investment proceeds are not sufficient to fund the obligations arising from its insurance contracts. The most important components of this financial risk are market risk, credit risk and liquidity risk.

Market risk

Market risk is the risk that the fair value of financial instruments will fluctuate due to changes in market prices. The Association separates market risk into three categories: foreign exchange risk, price risk, and interest rate risk.

Foreign exchange risk

Foreign exchange risk arises from the possibility that changes in the price of foreign currencies will result in losses. The Association holds assets and liabilities, including cash and investments, in Canadian dollars. The Association is exposed to foreign exchange risk through its investments in pooled funds.

Price risk

General economic conditions affect the market value of equity investments and currency exchange rates impact the market value of the investments denominated in currencies other than the Canadian dollar. The risk is managed by engaging an investment manager for the long-term portfolio investments and by investing other funds in short term fixed rate products with high credit ratings. The Association's investment policy specifies limits to the exposure to equity markets.

A 10% increase in the market value of equities would result in an increase in the excess of revenue over expenses for the year ended December 31, 2019 of \$7,400,489 (2018 - \$5,380,579). A 10% decrease in the market value of equities would result in a decrease in the excess of revenue over expenses for the year ended December 31, 2019 of \$7,400,489 (2018 - \$5,380,579).

Interest rate risk

Interest rate risk is the risk of financial loss arising from changes in interest rates. Fluctuations in interest rates will impact the market value of the fixed income portion of the investment portfolio. The Association is exposed to interest rate risk if the cash flows from investments are not matched to the liabilities they support. The Association manages the interest rate risk on fixed income bonds by engaging an investment manager who operates subject to investment parameters designed to mitigate this risk.

An interest rate sensitivity analysis is provided in Note 6.

Credit risk

Credit risk is the risk that a counterparty will be unable to pay amounts in full when due. The Association's financial assets exposed to credit risk consist of investments in bonds, accrued interest receivable and accounts receivable. The maximum exposure of the Association to credit risk is the carrying amount of these financial instruments as disclosed in the financial statements at December 31, 2019.

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The Association manages credit risk by maintaining bank accounts with reputable financial institutions, only investing in securities that are highly rated and traded in active markets. Accounts Receivable are from indemnified lawyers for their annual assessments.

The credit quality of the Association's investment in bonds, which is held in a pooled fund, is described in the following table:

Securities:	2019	2018
	\$	\$
Bonds – AAA rating	38,181,656	37,285,511
Bonds – AA rating	27,314,792	28,048,700
Bonds – A rating	20,976,353	18,310,230
Bonds – BBB rating	15,419,493	10,766,024
T-Bills	-	158,194
	101,892,294	94,568,659

Liquidity risk

Liquidity risk is risk that the Association will be unable to meet its obligations when they fall due, or that it may be required to settle its obligations on terms that are disadvantageous. The Association engages an investment manager to administer the investments it plans to hold for a long period of time. These investments are subject to liquidity risk if the Association is required to sell at a time the market for these investments is unfavourable or the investments are illiquid.

The maturity dates and interest rate ranges of the underlying bond holdings are as follows:

	2019		2018	
	Interest rate range	Market value \$	Interest rate range	Market value \$
Maturity dates (from balance sheet date)				
Within five years	1.25-7.56%	39,287,079	1.25-7.56%	35,656,656
Greater than five years but less than ten years	1.90-5.75%	31,115,367	1.00-4.29%	33,643,368
Greater than ten years	2.00-6.35%	31,489,848	2.50-6.50%	25,268,635
		101,892,294		94,568,659

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Notes to the Financial Statements

For the year ended December 31, 2019

The following tables present a comparison of the estimated maturities of the assets and liabilities of the Association as at December 31, 2019:

<i>Terms to maturity of assets</i>	Less than 1 year	From 1 to 5 years	Over 5 years	No specific maturity	Total
Cash and cash equivalents	3,792,644				3,792,644
Investments	19,046,028	39,287,080	62,605,214	74,004,897	194,943,219
Accounts receivable	1,612,221				1,612,221
Prepaid expenses	884,930				884,930
Total	25,335,823	39,287,080	62,605,214	74,004,897	201,233,014

<i>Terms to maturity of liabilities and equity</i>	Less than 1 year	From 1 to 5 years	Over 5 years	No specific maturity	Total
Accounts payable and accrued liabilities	340,569				340,569
Unearned premiums	13,315,274				13,315,274
Premium deficiency	3,201,726				3,201,726
Pension plan payable				124,160	124,160
Claims liabilities - Professional liability	31,037,000	67,532,000	20,762,000		119,331,000
Claims liabilities - Trust safety	594,000	1,208,000	356,000		2,158,000
Equity				62,762,285	62,762,285
Total	48,488,569	68,740,000	21,118,000	62,886,445	201,233,014

12 Pension Plan

a. Pension plan payable

	2019	2018
	\$	\$
Pension accrued liability	<u>124,160</u>	<u>118,283</u>

Prior to June 1, 2006, the Association provided a non-contributory defined benefit pension plan (the Plan) to eligible management employees based on earnings and years of service. The Plan is closed to new members and there were no active members of the Plan at December 31, 2019. Effective January 1, 2014 the Association adopted CICA 3463 and decided to use accounting valuation results.

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Notes to the Financial Statements

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As of December 31, 2019, and on advice of the actuary, the details of the Plan are as follows:

	2019 \$	2018 \$
Reconciliation of fair value of plan assets		
Fair value of plan assets – beginning of year	1,312,864	1,166,142
Actual return on plan assets	170,516	(9,068)
Less benefits paid during year to retirees	(24,463)	(24,142)
	<u>1,278,985</u>	<u>1,132,932</u>
Fair value of plan assets – end of year		
Reconciliation of the accrued benefit obligation		
Accrued benefit obligation – beginning of year	1,251,215	1,312,864
Interest on accrued benefit obligation	47,081	43,577
Actuarial loss (gain) during year	129,312	(81,084)
Less benefits paid during year to retirees	(24,463)	(24,142)
	<u>1,403,145</u>	<u>1,251,215</u>
Accrued benefit obligations – end of year		
	(124,160)	(118,283)
Plan deficit		
Pension cost		
Interest cost on accrued benefit obligation	47,081	43,577
Actual return on plan assets	(170,516)	9,068
Net actuarial (gains) losses	129,312	(81,084)
	<u>5,877</u>	<u>(28,439)</u>
Pension cost recognized during year		
Accrued benefit asset		
Beginning balance – Accrued benefit liability	(118,283)	(146,722)
Less pension cost during year	(5,877)	28,439
	<u>(124,160)</u>	<u>(118,283)</u>
Ending balance – Accrued benefit liability		
Reconciliation of accrued benefit liability		
Funded status (plan deficit)	(124,160)	(118,283)
	<u>(124,160)</u>	<u>(118,283)</u>
Accrued benefit liability		

Plan assets

The plan assets are invested in a balanced fund that consists of the following asset mix:

	2019	2018
Fixed income	32.1%	32.7%
Foreign equities	45.0%	44.7%
Canadian equity	16.9%	17.3%
Cash and cash equivalents	6.0%	5.3%
Other	0.0%	0.0%
	<u>100%</u>	<u>100%</u>

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Assumptions

The actuary used the following rates in their calculations:

	2019	2018
Discount rate – beginning of period	3.80%	3.35%
Discount rate – end of period	3.05%	3.80%
Expected long-term rate of return on plan assets	3.05%	3.80%
Rate of compensation increase	3.50%	3.50%

13 Equity in Canadian Lawyers Insurance Association

Effective June 30, 2014, the Association withdrew as a subscriber to the Canadian Lawyers Insurance Association (CLIA), a reciprocal insurance exchange through which the law societies of ten provinces and territories (or their associated liability insurance entities) entered into agreements of mutual indemnification. Separate reserves are maintained by CLIA with respect to risks assumed by each member of the exchange. The Association will maintain an interest in surpluses in these reserves until such time that the Association and CLIA reach mutually agreeable terms of winding up claims that existed prior to July 1, 2014. In 2019, the Association received a surplus distribution from CLIA in the amount of \$4.55M.

CLIA prepares annual Subscriber Accounts, as at the end of CLIA's fiscal year (December 31), which are approved by the CLIA Advisory Board. These accounts include a reserve for claims liabilities on a discounted basis. On that basis, the Subscriber Accounts of CLIA as at December 31, 2019 show the Association's equity to be \$6.5 million (December 31, 2018 – \$7.9 million). The Association's equity in CLIA is not reflected in these financial statements.

14 Premium deficiency

The premium deficiency as at December 31, 2019 of \$3,201,726 (December 31, 2018 - \$2,316,997) represents the difference between the projected costs of the indemnity program from January 1, 2020 to June 30, 2020 and unearned premiums recorded at December 31, 2019 as determined by the actuary. The premium deficiency does not include offsetting investment income that will accrue to the Association from January 1, 2020 to June 30, 2020.

15 Equity management

As at December 31, 2019 the Association's equity was \$62,762,285 (December 31, 2018 - \$40,058,043). The Association's objectives for managing the equity are for the prudent operation of the Association and to provide relatively stable premiums for indemnified lawyers over time.

16 Input tax credit

The Canada Revenue Agency (CRA) had ruled the Association was not entitled to collect Goods and Services Tax (GST) or claim input tax credits (ITCs) for GST paid on expenses. The Association appealed this ruling to the Tax Court of Canada. Pending resolution of this issue with CRA, the Association had recorded ITCs including interest and penalties, in the amount of \$4,359,730 as an expense from February 1, 2009 to December 31, 2017. Subsequent to the 2017 year-end, CRA notified the Association that it did not intend to contest the Association's appeal in Tax Court and the Association received a refund during 2018 for the full amount.

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17 Subsequent Event

The COVID-19 pandemic and its impact on business operations, supply chains, travel, commodity prices, consumer confidence and business forecasts, and the associated impact on domestic and international equity markets and fixed income yields, is expected to have a material impact on all equity and fixed income portfolios during the first half of 2020, and potentially beyond. Management will continue to monitor the operational and financial impact of the COVID-19 pandemic on the Association. While it is too early to predict the impact of COVID-19 related factors, during a time of increased uncertainty and volatility, we expect that the performance of the Association's portfolio, will be negatively affected, at the least in the near term.