



ALBERTA LAWYERS  
INSURANCE ASSOCIATION

# **Alberta Lawyers Insurance Association**

## **2015 Business Plan and Budget**

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## Introduction

The 2015 Alberta Lawyers Insurance Association (ALIA) business plan and budget for the fiscal year ending December 31, 2015 is presented below. This business plan and budget is presented to the Advisory Board for their consideration to recommend to the ALIA Board of Directors for their approval.

Two major changes took place in the ALIA Indemnity Program during 2014 that have a significant impact on the nature of the ALIA budget and, ultimately, the levy for 2015:

### *Withdrawal from the Canadian Lawyers Insurance Association (CLIA)*

Effective July 1, 2014 ALIA withdrew as a subscriber from the CLIA reciprocal and established its own reciprocal insurance exchange in accordance with the Alberta *Insurance Act*. This reciprocal called the Alberta Lawyers Insurance Exchange (ALIEX) was licensed by the Superintendent of Insurance and began operations on July 1, 2014. An insurance reciprocal is not a legal entity and requires a Principal Attorney to act on its behalf. ALIA acts as the principal attorney for ALIEX and manages ALIEX under a Management Agreement.

As was the case in the CLIA reciprocal, ALIA will continue to handle all claims against Alberta lawyers. The \$500,000 group deductible will be paid by ALIA and amounts in excess of \$500,000 will be paid by ALIEX. Reinsurance and excess insurance have been purchased to provide additional protection.

Claims pre-July 1, 2014 continue to be run off under the CLIA reciprocal. Our goal is a clean break from CLIA and we will monitor this yearly to determine when it is optimal for that to happen. ALIA remains a subscriber to CLIA for the purposes of the Voluntary Excess Program.

The structure of the new professional liability insurance program, including reinsurance coverage not included in the previous CLIA coverage, is depicted in Appendix 1.

### *Trust Safety Insurance*

Prior to July 1, 2014, the liability for claims related to lawyer misappropriation of client trust funds was contained within the Law Society's Assurance Fund. There were no dollar amount or time limitations on defalcation claims under the Assurance Fund model. Consequently, this model represented a significant financial risk to both the Law Society and Alberta lawyers.

To more effectively manage this risk, we've introduced Trust Safety Insurance (TSI) in 2014 as part of the ALIA professional indemnity program. Trust defalcation claims occurring after July 1, 2014 will be covered under the TSI program. Under TSI, theft claims will be managed in the same manner as professional liability claims with appropriate dollar amount and time limitations and exclusions. The structure of the TSI program is depicted in Appendix 2. Defalcation claims occurring prior to July 1, 2014 will be adjudicated and paid out of the legacy Law Society Assurance Fund.

## Levy and budget implications

The withdrawal from CLIA, creation of ALIEX and the introduction of TSI has a number of implications to the structure of ALIA's 2015 budget. The discussion below is based on the proposed budget included on page 8. This budget contains very preliminary amounts for the 2015/16 Part A and Part B levy revenue and claims expense estimates. We'll have a much better sense of these amounts once we've received the formal actuarial report in the spring of 2015 in conjunction with the setting of the actual 2015/16 levies.

### Revenue

#### *Annual levy – Part A and B*

The ALIA levy for the insurance policy year commencing July 1, 2015 will consist of two parts – a Part A levy representing the traditional professional liability coverage and a Part B levy representing the new TSI coverage. We refer to Part A and Part B as these are the distinct sections of the new indemnity program insurance policy that addresses professional liability and trust theft coverage respectively.

The Part A and Part B levy for the 2015/16 policy year will be established by the Advisory Board in the spring of 2015. Insured Alberta lawyers (estimated at 6,300) will be required to pay the combined levy before the commencement of the new policy year – July 1, 2015. The insurance policy year (July) and ALIA's fiscal year (December) do not coincide, so this makes our 2015 revenue budget a bit complicated. In addition, there was no TSI levy for the 2014/15 policy year so the 2015 budget only reflects TSI (or Part B) levy revenue for the last six months of fiscal 2015. For clarity, Appendix 3 illustrates the structure of the proposed revenue budget for 2015.

The claims environment under which the new combined levy will be established is as follows:

#### Part A;

Normal claims year prior to 2008 were around \$12 million. Since the global economic crash at that time, we've had claims years in the mid \$20 million up to \$30 million. By far, the greatest impact on the program during this time period was mortgage fraud which accounted for 25% of our claims loss. We see the trend going back down in 2011 and 2012 to \$18 million and \$20 million. We appear to be "normalizing" and remain cautiously optimistic.

#### Part B;

Prior to the establishment of Part B (or TSI) coverage, theft claims covered by the Law Society's Assurance Fund have been a stand out in terms of large losses hitting that fund. Since 2004, we have averaged \$10 million in claims against the Assurance Fund per year.

The estimated Part A and Part B levies for the 2015/16 policy year reflected in this budget are designed to provide adequate funding to support ALIA's budgeted expenses and to maintain an adequate accumulated surplus. The Part B (or TSI) levy is a new element to what insured lawyers have paid in previous years. Prior to July 1 2014, all Alberta lawyers (about 9,000) funded theft claims through the Law Society's Assurance Fund levy. The Assurance Fund levy covered more

than the cost of theft claims including custodianships, the Trust Safety audit program, and investigations staff. Spread over 9,000 lawyers, the portion of the theft claims cost funded by the Assurance Levy was about \$170. The new TSI program is now funded by 6,300 insured lawyers, so the equivalent of the per lawyer theft claim cost coverage in the previous Assurance Fund model is about \$250. The Assurance Fund levy has been kept artificially low in the past few years resulting in deficit funding over that time period. The accumulated surplus in that fund has declined from just under \$8 million in 2009 to just under \$5 million in 2013, a decline of \$3 million.

The preliminary TSI levy reflected in this budget is designed to fund the estimate cost of claims and the cost of reinsurance for ALIA and ALIEX. That all adds up to \$2,875,000 or about \$460 spread over 6,300 insured lawyers. The estimated levy of \$470 covers these budgeted costs and provides additional funding to build some surplus for the new Part B program.

In summary, the 2015 budget reflects an estimated 2015/16 levy of \$3,930 Part A and \$470 for Part B (the new Trust Safety Insurance). The actual levy for the policy year commencing July 1, 2015 will be established by the Advisory Board in the spring of 2015. The ALIA levy history is outlined in Appendix 4. Again, these estimated levies are very preliminary and will be subject to change upon receipt of our actuary's formal report in the spring of 2015 prior to the establishment of the actual levies for the 2015/16 indemnity program policy year.

#### *Investment income*

ALIA has about \$120 million of invested funds under professional management governed by a Statement of Investment Policies and Goals. Investment income is derived from interest, dividends and gains or losses on the disposition of securities. The investment revenue budget is derived from historical experience

#### *Management fee – ALIEX*

ALIA will charge a management fee to ALIEX to recover a portion of overhead costs attributable to the operations of ALIEX.

#### *Voluntary excess administration fee*

ALIA remains a subscriber to CLIA for the purposes of the Voluntary Excess Program and will collect an administration fee for handling these claims on CLIA's behalf.

### **Expenses**

ALIA's budgeted expenses have increased by \$6,064,710 from 2014 to 2015. The factors driving this increase are:

#### *Trust Safety Insurance (Part B)*

The TSI program introduces three new elements to ALIA's cost structure – a provision for Part B claims, a premium paid to ALIEX for excess Part B coverage and reinsurance premium costs. This accounts for \$2,925,000 of ALIA's budgeted cost increase.

## *Conversion from CLIA to ALIEX – Part A coverage*

The budgeted cost of Part A coverage in excess of \$500,000 has increased by \$639,200 from budget 2014 due primarily to a retroactive assessment that ALIA is required to pay CLIA of \$635,500 in 2015. Combined with additional reinsurance coverage that did not exist under the CLIA program for \$960,000 and an increase in the budgeted Part A claims provision of \$275,000, budgeted expenses for the Part A program have increased by \$1,874,200 from 2014.

### *Other increases:*

Budgeted staffing costs have increased by \$409,100. This increase includes the addition of a senior staff member and increased contract costs. The management fee charged by the Law Society to ALIA will increase by \$348,000 to recover ALIA's allocated share of increased support costs.

## **Business Plan**

This year's budget preparation began with the development of a business plan. This business plan forms the foundation of the budget presented later in this document.

ALIA's overall goal is to be a model for excellence in delivery of Alberta's lawyers' professional liability and trust safety insurance.

### **Goals:**

- Organizational Capacity
  - Continued implementation of reorg to ensure regulatory compliance and governance support, enhanced oversight of claims, including reserving, claims handling, litigation management and coverage; as well as operations resources to support regulatory and reinsurance requirements
- Regulatory compliance
  - ensure that ALIEX is in compliance with the Alberta Insurance Act and Regulations at all times; develop regulatory compliance plan and plan for implementation
  - ensure the program is effectively governed and managed.
- Risk Management
  - Work with Law Society to develop risk and loss prevention management program
- Communications
  - Enhanced Communications Plan to ensure a regular communication tool to inform and educate lawyers.

### **2015 Initiatives:**

- Enhance the oversight of claims, including reserving, claims handling, litigation management and increased in-house coverage analysis; to ensure effective management of increasingly complex claims and Trust Safety claims.
- Effectively manage claims in a fair, reasonable and timely manner so that claimants who have suffered a loss due to the negligence or theft of a lawyer are fairly compensated. Ensure defence files are properly managed.
  - Measure against reorg plan, performance management, LEADS and Litigation Management Program review.

- Provide a high level of customer service.
  - Measure success through the Closed Claim Survey program
- Ensure the program is compliant with regulatory, compliance and governance requirements.
  - Measure against plan.
- Enhance communication to ensure program lawyers are informed.
  - Measure success through the Communications Plan
- Work with Law Society to develop project for Risk Management and Loss Prevention Program
- Ensure the program is managed in an effective, efficient and financially accountable manner

## Budget

The following budget is based on a fiscal period ending December 31, 2015. We refer to:

- **Budget 2015**, which means the fiscal period beginning January 1, 2015 and ending December 31, 2015;
- **Budget 2014**, which means the fiscal period beginning January 1, 2014 and ending December 31, 2014; and
- **Forecast 2014**, which is our forecast (a combination of actual financial results and our best estimate of revenue and expenses to the end of the current fiscal period) for the year that began January 1, 2014 and ending December 31, 2014.

## Budget Assumptions

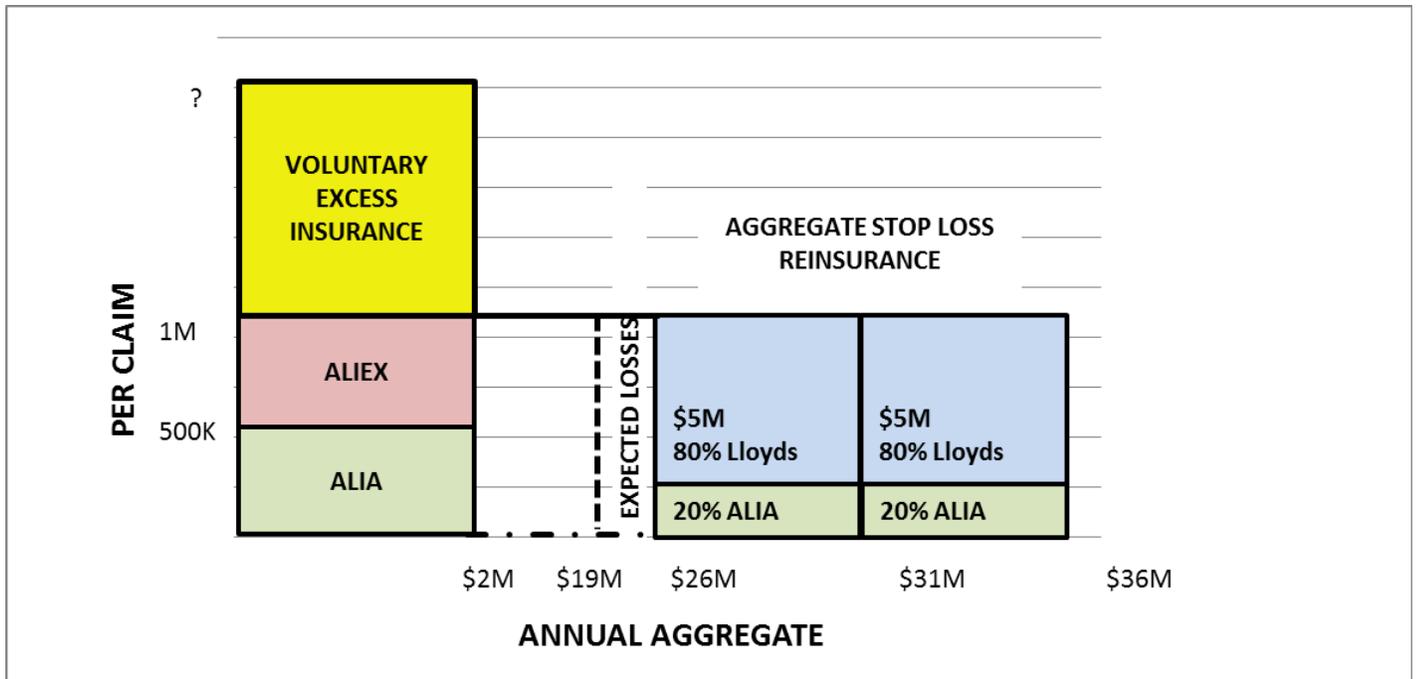
- For purposes of estimating revenue from the insurance levy, we have assumed a 2% growth in insured lawyers based on historical trends.
- The budget for investment income is based on the average income (interest, dividends and realized gains/losses on liquidations of securities) on ALIA's portfolio of cash, bonds and equities over the past three years.
- Unrealized gains or losses on changes in the market value of investments have not been budgeted as these amounts are virtually impossible to predict and are, by their nature, non-cash items.
- The budget for the provision for claims and related costs is based on preliminary estimates provided by our actuary.

**The Alberta Lawyers Insurance Association  
Budget  
For the Year Ending December 31, 2015**

	<u>2015 Budget</u>	<u>2014 Forecast</u>	<u>2014 Budget</u>	<u>Variance 2015 budget from 2014</u>
<b>Revenue</b>				
Annual levy (Part A)	\$ 24,714,500	\$ 23,047,900	\$ 22,634,000	\$ 2,080,500
Annual levy (Part B)	1,480,500	-	-	1,480,500
Investment income	6,770,000	7,796,000	4,300,000	2,470,000
Management Fee - ALIEX	200,000	100,000	-	200,000
Voluntary Excess Admin Fee	145,000	142,000	-	145,000
	<u>33,310,000</u>	<u>31,085,900</u>	<u>26,934,000</u>	<u>6,376,000</u>
<b>Expenses</b>				
Provision for claims and related costs - Part A	19,100,000	18,825,000	18,825,000	275,000
Provision for claims and related costs - Part B	2,250,000	1,125,000	-	2,250,000
ALIEX Premium - Part A	3,627,500	1,985,000	1,750,000	1,877,500
ALIEX Premium - Part B	495,000	-	-	495,000
Premium paid to CLIA	635,500	4,416,000	1,873,800	(1,238,300)
Salaries and benefits	2,493,600	2,379,000	2,084,500	409,100
Management fee	2,208,000	1,860,000	1,860,000	348,000
Administration	367,300	263,600	194,550	172,750
Professional fees	208,000	118,000	93,000	115,000
Reinsurance - Part A	960,000	120,000	-	960,000
Reinsurance - Part B	180,000	-	-	180,000
Investment fees	280,000	280,000	264,000	16,000
Risk Management	104,000	14,000	27,500	76,500
Regulatory	115,500	-	-	115,500
CLIA Wind Up	19,500	-	-	19,500
Amortization	3,000	10,000	9,840	(6,840)
	<u>33,046,900</u>	<u>31,395,600</u>	<u>26,982,190</u>	<u>6,064,710</u>
<b>Net Income (Loss)</b>	263,100	(309,700)	(48,190)	311,290
Unrealized gain (losses) on Investments	-	4,000,000	-	-
<b>Net Income (Loss)</b>	<u>\$ 263,100</u>	<u>\$ 3,690,300</u>	<u>\$ (48,190)</u>	<u>\$ 311,290</u>

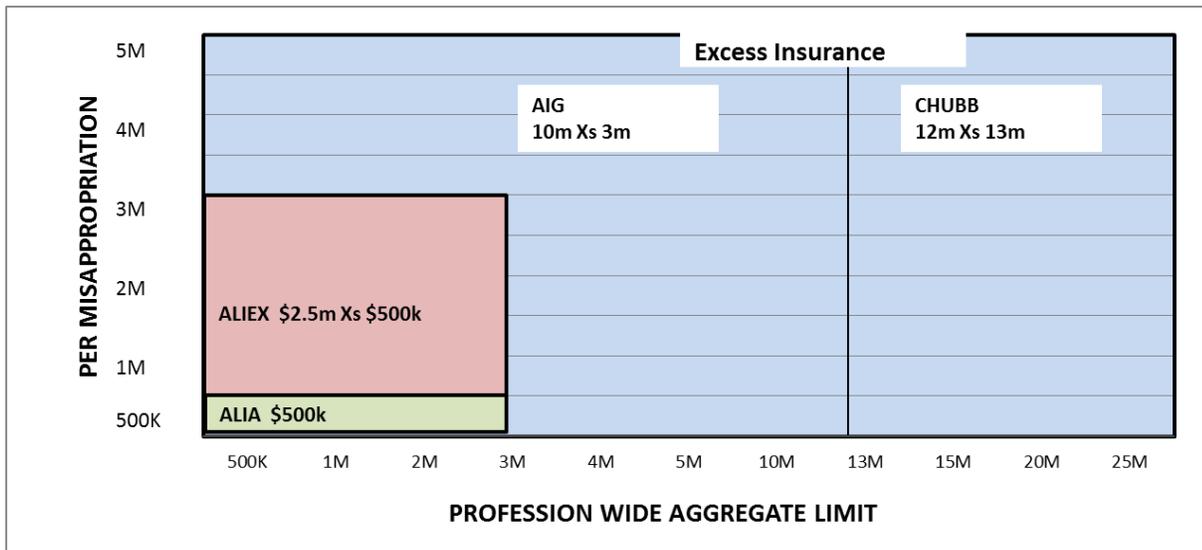
# Appendix 1 – Professional liability insurance program structure

<u>Part A</u>	Professional Liability Insurance
<u>Limits</u>	\$1m per Occurrence / \$2m Annual Aggregate
<u>Reinsurance</u>	80% of \$10m excess of \$26m
<u>Reinsurers</u>	Lloyds
<u>Group Deductible</u>	\$500k per Occurrence
<u>ALIEX Limits</u>	\$500k excess of \$500k



## Appendix 2 – Trust Safety Insurance program structure

<u>Part B</u>	Trust Safety Insurance
<u>Limits</u>	\$5m per Misappropriation \$25m Profession Wide Annual Aggregate
<u>Excess Insurance</u>	\$22m Annual Aggregate Excess of \$3m Annual Aggregate
<u>Insurers</u>	Primary \$10m AIG Excess \$12m Chubb
<u>Group Deductible</u>	\$500k per Claim Subject to \$3m Aggregate
<u>ALIEX Limits</u>	\$2.5m Excess of \$500k Group Deductible Subject to \$3m Aggregate



## Appendix 3 – Levy revenue analysis

### 2015 Part A Revenue Budget

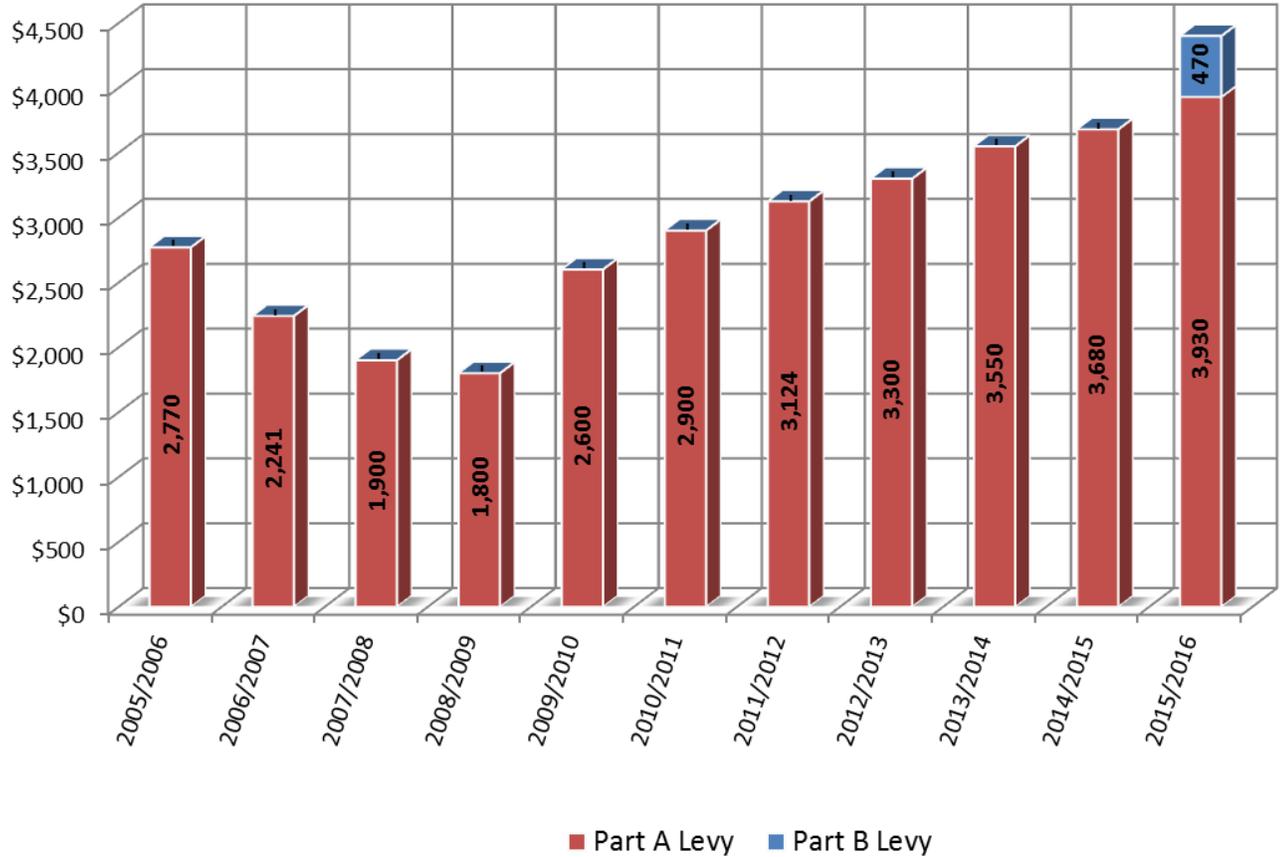
Insurance policy year - July 1 to June 30 (12 months)	Fiscal 2015 - January 1, 2015 to December 31, 2015		
	January 1, 2015 to June 30, 2015 (6 months)	July 1, 2015 to December 31, 2015 (6 months)	January 1, 2015 to December 31, 2015 (12 months)
Budgeted revenue based on actual 2014/15 Part A levy @ \$3,680	\$ 11,592,000	-	\$ 11,592,000
Budgeted revenue based on estimated 2015/16 Part A levy @ \$3,930	-	12,379,500	12,379,500
Surcharge revenue	300,000	335,000	635,000
	<u>\$ 11,892,000</u>	<u>\$ 12,714,500</u>	<u>24,606,500</u>
Administration fees			<u>108,000</u>
Total 2015 budgeted Part A revenue			<u>\$ 24,714,500</u>

### 2015 Part B Revenue Budget

Insurance policy year - July 1 to June 30 (12 months)	Fiscal 2015 - January 1, 2015 to December 31, 2015		
	January 1, 2015 to June 30, 2015 (6 months)	July 1, 2015 to December 31, 2015 (6 months)	January 1, 2015 to December 31, 2015 (12 months)
Budgeted revenue based on estimated 2015/16 Part B levy @ \$470	-	\$ 1,480,500	\$ 1,480,500

## Appendix 4 – Historical levy comparison

### LEVY HISTORY



***Please note the 2015/16 levy is an estimate, a portion of which is the new Part B Trust Safety Insurance premium of \$470. The actual levy for Part A and Part B coverage will be determined in the spring of 2015 for the policy year commencing July 1, 2015.***

## Appendix 5 – Fund balance analysis

<b>Actual balance at December 31, 2013</b>	\$ 38,998
Forecast net income to December 31, 2014	3,690
Investment in ALIEX	<u>(5,000)</u>
<b>Forecast balance at December 31, 2014</b>	37,688
Budgeted net income to December 31, 2015	<u>263</u>
<b>Budgeted balance at December 31, 2015</b>	<u><u>\$ 37,951</u></u>

*Note:*

*Accumulated Surplus, also known as Net Assets or Retained Earnings, is the difference between Assets and Liabilities and represents the residual equity in ALIA available to pay future claims.*

*Based on the advice and analysis of ALIA's actuary, the recommended minimum accumulated surplus is \$28.5 million. Management anticipates this minimum balance will increase and is awaiting a recommendation in this regard from the actuary.*

## Appendix 6 - Claims reserve summary

	Rounded to the nearest \$1,000				
	Dec 31 2013	Dec 31 2012	Jun 30 2012	Jun 30 2011	Jun 30 2010
Net Reserve - Beginning of Year	\$ 64,338	\$ 62,620	\$ 55,354	\$ 55,034	\$ 46,027
Less: Claims Paid and accrued	(21,941)	(4,094)	(10,374)	(15,588)	(6,947)
Less: Related costs paid and accrued	(5,764)	(2,834)	(5,285)	(5,391)	(5,231)
Add: Recoveries	10,741	528	2,943	5,131	1,011
Add: Provision	18,698	8,118	19,982	16,168	20,174
Net Reserve - End of Year	<u>\$ 66,072</u>	<u>\$ 64,338</u>	<u>\$ 62,620</u>	<u>\$ 55,354</u>	<u>\$ 55,034</u>