



ALBERTA LAWYERS INDEMNITY ASSOCIATION

BUDGET 2020

Approved by the ALIA Board, November 26, 2019

Contents

- ALBERTA LAWYERS INDEMNITY ASSOCIATION 1**
- BUDGET 2020..... 1**
- INTRODUCTION 2
- BUDGET STRUCTURE..... 3
- ALIA 2020 BUDGET 4
- REVENUE 5
- EXPENSES..... 7
- APPENDIX 1 - ALIA 2020 PREMIUM REVENUE ANALYSIS..... 10

INTRODUCTION

The budget contained in this document represents management's funding proposal to carry out the activities and initiatives of the Alberta Lawyers Indemnity Association ("ALIA") in 2020.

While the budget and forecast are necessarily speculative, there are particular challenges in preparing a budget where the major contributing revenues and expenses will, of necessity, remain undetermined for many months. ALIA's major sources of revenue is its investment income and, more significantly, the levies received for both Part A and Part B which will not be determined until the spring of 2020, when the Board sets the levies based on the actuary's levy report.

Accordingly, the figures used in the budget for the significant line items are based on the best information available at this time, as set out in the detailed commentary below.

In addition, while the Business Plan identifies the initiative of undertaking an analysis of the opportunity to align ALIA's policy year end and fiscal year end, the budget assumes a fiscal year of January 1 to December 31 and a policy year of July 1 to June 30. Management anticipates that the fiscal year, or policy year, or both may change in 2020, and the results of the analysis and a recommendation will be presented to the Board as management undertakes this work.

The following pages highlights the 2020 budget for ALIA accompanied by explanations. The 2019 budget used for comparison purposes is the combined budget of the Alberta Lawyers Insurance Exchange ("ALIEX") and ALIA.

BUDGET STRUCTURE

In discussing the budget, we refer to:

- **Budget 2020** - which means the fiscal year beginning January 1, 2020 and ending December 31, 2020;
- **Budget 2019** - which means the fiscal year beginning January 1, 2019 and ending December 31, 2019; and
- **Forecast 2019** - which is our forecast of revenue and expenses for the fiscal year beginning January 1, 2019 and ending December 31, 2019 based on management's current estimate of anticipated results to December 31, 2019.

ALIA 2020 BUDGET

	2020 Budget	2019 Forecast	2019 Budget	Variance 2020 Budget to 2019 Budget	Variance 2019 Forecast to 2019 Budget
Revenue					
Premium - Professional liability	\$22,383,500	\$24,919,500	\$27,375,500	\$ (4,992,000)	\$ (2,456,000)
Premium - Misappropriation indemnity	2,900,000	3,100,000	3,115,000	(215,000)	(15,000)
Insurance - Professional liability	(1,367,000)	(1,232,250)	(1,162,500)	(204,500)	(69,750)
Insurance - Misappropriation indemnity	(468,700)	(447,000)	(448,000)	(20,700)	1,000
Net premium	23,447,800	26,340,250	28,880,000	(5,432,200)	(2,539,750)
Investment income	7,450,000	15,360,000	7,309,000	141,000	8,051,000
Unrealized gain (loss) on Investments	-	6,000,000	-	-	6,000,000
Voluntary excess insurance administration fee	145,000	148,932	145,000	-	3,932
	<u>31,042,800</u>	<u>47,849,182</u>	<u>36,334,000</u>	<u>(5,291,200)</u>	<u>11,515,182</u>
Expenses					
Provision for claims and related costs - Professional liability	17,500,000	17,000,000	26,000,000	(8,500,000)	(9,000,000)
Provision for claims and related costs - Misappropriation indemnity	50,000	(310,500)	400,000	(350,000)	(710,500)
Premium deficiency	3,000,000	2,300,000	-	3,000,000	2,300,000
Premium paid to CLIA	-	(4,555,838)	-	-	(4,555,838)
Salaries and benefits	3,458,400	2,808,000	3,337,400	121,000	(529,400)
Management fee - Law Society	3,151,200	3,012,000	3,012,000	139,200	-
Contractors	235,000	395,000	562,000	(327,000)	(167,000)
Premium taxes	-	-	200,400	(200,400)	(200,400)
Investment fees	420,000	380,000	380,000	40,000	-
Bank and credit card charges	126,000	465,000	459,500	(333,500)	5,500
Professional fees	378,500	343,000	633,500	(255,000)	(290,500)
Board expenses	100,000	100,000	147,200	(47,200)	(47,200)
CLIA Wind up	-	-	55,000	(55,000)	(55,000)
Risk management	-	-	17,500	(17,500)	(17,500)
Administration	259,500	147,000	242,200	17,300	(95,200)
	<u>28,678,600</u>	<u>22,083,662</u>	<u>35,446,700</u>	<u>(6,768,100)</u>	<u>(13,363,038)</u>
Net income	<u>\$ 2,364,200</u>	<u>\$25,765,520</u>	<u>\$ 887,300</u>	<u>\$ 1,476,900</u>	<u>\$ 24,878,220</u>

REVENUE

Premiums – Professional liability and Misappropriation Indemnity

The budget includes the current levy of \$3,344 for the first six months of 2020 (second half of the 2019/2020 policy year) and a projected levy for July 1, 2020 to December 31, 2020 (first half of the 2020/2021 policy year). The budget assumes a \$3,000 Professional Liability levy for the 2020/2021 policy year, which is a decrease of \$344 decrease compared to the current 2019/2020 levy of \$3,344. The budget also assumes a \$400 Misappropriation Indemnity levy, which is a decrease of \$48 compared to the current 2019/2020 levy. The assumption is that based on the 2019 forecast which assumes a projected net income of \$25.7 million and considering that the indemnity program surplus is estimated at approximately 99.65 percentile by the end of 2019 that the levy will decrease. An analysis of Part A and Part B levy revenue is provided in Appendix 1. Actual levies for the 2020/2021 policy will be approved by the Board in the spring of 2020 upon receipt of the actuary's levy setting report.

The number of lawyers who participate in Alberta's Mandatory Indemnity program ("Subscribers") estimated within the budget is based on an estimated growth of 1% from 2019 levels. This growth rate was derived from actual increase over the last three years and an assessment of future trends.

Insurance – Professional Liability and Misappropriation Indemnity

Insurance for Professional Liability and Misappropriation indemnity represents the premium paid to third parties for insurance (formerly called "reinsurance").

Currently the Professional Liability coverage is \$10 million in excess of \$26 million annual aggregate. It is purchased from Liberty Mutual (25%), Continental Casualty (25%) and Alliance Global Risks (50%). The budget for the Professional Liability insurance assumes a 10% increase of the premium paid for the 2019/2020 policy year which was \$1,302,000.

The Misappropriation indemnity excess insurance has two layers of coverage providing an aggregate of up to \$25 million – layer 1 is with AIG and provides coverage in excess of \$3 million up to \$13 million. Layer 2 is with Chubb and provides coverage in excess of \$13 million up to \$25 million. The budget for Misappropriation indemnity excess insurance assumes a 10% increase of the premium paid for the 2019/2020 policy year which was \$453,500.

Investment Income

The budget for investment income is conservative and consists of interest, dividends and realized gains or losses on sales of investments. The actual amount of investment income can vary considerably from budget depending on investment market conditions and the extent to which we are required to liquidate investments to pay claims. As at the end of Q3 2019 ALIA's portfolio has experienced a 10.6% return in 2019 compared to a three-year average of 5.6%. In addition, investment income for 2019 includes re-balancing of ALIA's portfolio within the current asset mix following transfer of assets from ALIEX to ALIA, which resulted in a higher than anticipated realized investment income. Given the special circumstance in 2019 of transferring assets from ALIEX into ALIA and based on consultation with Mawer, realized investment income is anticipated to experience similar results as 2018 which is reflected in the 2020 budget.

Unrealized Gain (Loss) on Investments

Accounting convention requires that we record to income the changes in the market value of our investments from one reporting period to another. As it is inherently difficult to predict investment markets, and as recommended by our investment manager, we do not budget for unrealized gains or losses on the investment portfolio. In 2019 the portfolio recovered dramatically from an unrealized loss in December 2018 however the trend is not anticipated to continue.

Voluntary Excess Insurance Administration Fee

ALIA administers the voluntary excess insurance program provided by the Canadian Lawyers Insurance Association (CLIA) to Subscribers. ALIA charges a fee to CLIA of 10% of the excess insurance premium purchased by Subscribers.

EXPENSES

Provision for claims and related costs – Professional Liability and Misappropriation Indemnity

The professional liability claims provision budget is based on ALIA's actuary, Willis Towers Watson (WTW), review of the 2019 data up to September 30 which is updated within the 2019 forecast and the anticipated trend for 2020. WTW anticipates a 2% increase in claims liability compared to 2019 data which is reflected in both the Professional Liability and the Misappropriation Indemnity 2020 budget.

Salaries and Benefits

This budget line item includes the cost of ALIA's full time staff consisting of 25 full time equivalents (FTE's) in 2020.

Management Fee

The Law Society provides several services and facilities to ALIA, including office space, Accounting, Information Technology, Customer Service, Information Management, Human Resources and Governance support. The cost of these facilities and services are recovered through the management fee. The fee also includes a provision for loss prevention services provided to ALIA through the Law Society's proactive Early Intervention and Practice Management programs. The ALIA management fee has increased from 2019 by \$139,200 (5%). The Law Society and ALIA are mutually working towards implementing a management agreement regarding the terms and provision of services. This management agreement will formalize our processes and allow both organizations clearer oversight of our respective resources.

Contractors

The 2020 budget includes estimated contractor funding for initiatives described in the Business Plan document as well as a placeholder for initiatives discussed during the 2019 Strategic Retreat including:

- Contractor resources for Lean, Root Cause, Litigation Assessment, Survey of the Profession, Loss Prevention, and Coding projects;
- Contractor resources to develop an ALIA website;
- Regular external review of claim files; and
- Other projects that management expects will proceed in 2020.

Board Expenses

Board expenses includes funding for honoraria, the annual premium for Directors and Officers insurance, Board training and Board travel expenses. These expenses were previously budgeted in ALIEX, but now reside with ALIA. The 2020 budget has decreased by \$47,200 and aligns with the 2019 forecast. In addition, a board retreat is proposed to be held every two years with the next retreat anticipated in 2021.

Investment Fees

Our investment manager (Mawer) charges investment management fees quarterly calculated on a tiered percentage schedule based on the market value of ALIA's investment portfolio. The 2020 budget is based on estimates of the market value of the ALIA portfolio. In addition, a third-party investment review is scheduled in 2020.

Bank Charges

Along with bank service charges, this category historically included fees charged by our credit card service provider (Moneris) for levies collected from our Subscribers via credit cards. While payment of the levy by credit card provides an additional payment option to lawyers, the costs to the Law Society and ALIA over the past five years has amounted to \$3 million and is expected to increase by 10% annually.

Following an in-depth analysis by the Law Society of both the costs and the impact internally and to the profession, the Law Society is proceeding with eliminating the credit card payment option from its infrastructure in early 2020. As all billing of ALIA's levies is done through the Law Society, this change by the Law Society means that ALIA can no longer accept credit card payments but benefits from the substantial cost savings. Other methods of on-line payment such as Electronic Funds Transfer (EFT) and on-line bill payments will be accepted, which are cost effective payment options. In addition, the Law Society is developing communications around this issue, including a useful resource guide to assist lawyers who do not have experience with EFT and on-line bill payment in their professional and/or personal lives.

Professional Fees

Professional fees include audit, actuarial, insurance consultant and legal fees. The 2020 budget has decreased by \$255,000 from 2019 and is a direct savings from the successful EEE project. With the windup of ALIEX, expenses decrease as a result of requiring only one year-end audit and one actuarial valuation, as well as the elimination of the requirement to adopt the IFRS17 accounting standard.

Risk Management

The proposed budget does not include budget for risk management, except as specified in the Business Plan and The Management Fee. The budget for 2019 consisted of costs related to ALIA Alerts to Subscribers and changes to ALIA's information systems stemming from a revised levy surcharge structure which occurred in the prior year. As indicated within the Business Plan, management is proposing to setup a Loss Prevention Committee that includes Law Society representation to identify and implement, as appropriate, potential risk management and loss prevention opportunities. Currently most loss prevention services are provided through the Law Society (and paid for through the Management Fee) or by ALIA staff at no additional cost.

Administration

This budget item includes estimated costs for staff recruiting, travel, training, communication, and professional dues.

APPENDIX 1 - ALIA 2020 PREMIUM REVENUE ANALYSIS

2020 ALIA Premium Revenue Actual to Budget (Forecast based on actual premiums set for 2019/2020 policy year)

Insurance policy year - July 1 to June 30 (12 months)	Budget Fiscal 2020 - Jan 1, 2020 to Dec 31, 2020			Budget Fiscal 2019 - Jan 1, 2019 to Dec 31, 2019			Difference 2020 to 2019 (12 months)
	Jan 1, 2020 to Jun 30, 2020 (6 months)	Jul 1, 2020 to Dec 31, 2020 (6 months)	Jan 1, 2020 to Dec 31, 2020 (12 months)	Jan 1, 2019 to Jun 30, 2019 (6 months)	Jul 1, 2019 to Dec 31, 2019 (6 months)	Jan 1, 2019 to Dec 31, 2019 (12 months)	
PART A:							
Part A Premium	\$ 3,344	\$ 3,000		\$ 3,772	\$ 4,072		
Number of insured lawyers	6,820	6,850		6,750	6,850		
Sub-total Part A premium revenue	\$ 11,403,100	\$ 10,275,400	\$ 21,678,500	\$ 12,730,500	\$ 13,947,000	\$ 26,677,500	\$ (4,999,000)
Surcharge revenue	235,000	325,000	560,000	265,000	285,000	550,000	10,000
Administration fees			145,000			148,000	(3,000)
Total premium revenue (Part A)	\$ 11,638,100	\$ 10,600,400	\$ 22,383,500	\$ 12,995,500	\$ 14,232,000	\$ 27,375,500	\$ (4,992,000)
PART B:							
Part B Premium	\$ 448	\$ 400		\$ 458	\$ 458		
Number of insured lawyers	6,820	6,850		6,750	6,850		
Total premium revenue (Part B)	\$ 1,528,000	\$ 1,370,000	\$ 2,898,000	\$ 1,546,000	\$ 1,569,000	\$ 3,115,000	\$ (217,000)