

# Financial results explained

## INCOME STATEMENTS

Statement of Profit or Loss		Lawyers' Professional Indemnity Company 2014 Annual Report	
Stated in thousands of Canadian dollars			
For the year ended December 31	2014	2013	
<b>Revenue</b>			
Gross written premiums	\$ 122,149	113,561	
Premiums ceded to reinsurers (note 11)	(7,229)	(7,051)	
Net written premiums	114,920	106,510	
(Increase) decrease in unearned premiums (note 10)	(20)	(26)	
<b>A » Net premiums earned</b>	<b>114,900</b>	<b>106,484</b>	
<b>D » Net investment income (note 5)</b>	<b>26,472</b>	<b>16,255</b>	
Ceded commissions	1,679	1,535	
	<b>\$ 143,051</b>	<b>124,274</b>	
<b>Expenses</b>			
Gross claims and adjustment expenses (note 9)	\$ 104,847	99,178	
Reinsurers' share of claims and adjustment expenses	(5,262)	(2,475)	
<b>B » Net claims and adjustment expenses</b>	<b>99,585</b>	<b>96,703</b>	
<b>C » Operating expenses (note 15)</b>	<b>16,830</b>	<b>16,330</b>	
Premium taxes	3,665	3,408	
	<b>120,080</b>	<b>116,441</b>	
<b>Profit (loss) before income taxes</b>	<b>\$ 22,971</b>	<b>7,833</b>	
Income tax expense (recovery) (note 14)			
Current	\$ 6,220	2,126	
Deferred	(309)	(226)	
	<b>5,911</b>	<b>1,900</b>	
<b>E » Profit (loss)</b>	<b>\$ 17,060</b>	<b>5,933</b>	

*Accompanying notes are an integral part of the financial statements.*

investments). The decrease in the discount rate creates a higher additional claims liability; in this case, an unfavourable development of \$7.7 million. In other words, because we must assume we will make less interest on our reserves while we wait to pay individual claims, we must set more money aside.

### **C** General expenses: \$16.8 million

LAWPRO's general expenses in 2014 were \$0.5 million higher than in 2013, but still \$450,000 lower than budgeted, as a result of disciplined cost containment efforts.

### **D** Investment income: \$26.5 million

Investment income increased by \$10.2 million to \$26.5 million in 2014. This was primarily due to a \$2.3 million increase in unrealized gains and losses on the cash flow matched investment portfolio (compared to prior year's same period decrease of \$6.0 million), combined with realized gains of \$7.6 million (compared to prior year's same period realized gains of \$5.6 million).

### **A** Net premiums: \$114.9 million

Net LAWPRO revenues in 2014 were \$114.9 million, almost exactly as budgeted. Premiums from the mandatory insurance program were \$8.4 million higher than in 2013.

### **B** Net claims: \$99.6 million

Incurred claims and adjustment expenses for 2014 increased by \$2.9 million compared to 2013. However, they were lower than the \$105.3 million budgeted.

The discount rate used to value claims liabilities decreased from 2.68 per cent at December 31, 2013 to 1.95 per cent at December 31, 2014. Tracking the discount rate causes an adjustment to the amount reserved to pay future claims costs (it reflects current and projected interest rates on

### **E** Net income: \$17 million

LAWPRO experienced total net income for 2014 of \$17 million (compared to net income of \$5.9 million for 2013). After including \$1.7 in other comprehensive income (see F, opposite, for details), this resulted in shareholder's equity of \$208.6 million at the end of 2014, up from \$189.9 million at the end of 2013 – for a year-over-year increase of \$18.7 million.

## Statement of Comprehensive Income

Lawyers' Professional Indemnity Company  
2014 Annual Report

Stated in thousands of Canadian dollars

For the year ended December 31	2014	2013
<b>Profit (loss)</b>	<b>\$ 17,060</b>	<b>5,933</b>
Other comprehensive income (loss), net of income tax:		
<u>Items that will not be reclassified subsequently to profit or loss:</u>		
Remeasurements of defined benefit obligation, net of income tax expense (recovery) of (\$206) [2013: (\$174)]	(570)	480
<u>Items that may be reclassified subsequently to profit or loss:</u>		
<i>Available-for-sale assets</i>		
Net changes unrealized gains (losses), net of income tax expense (recovery) of \$2,517 (2013: \$5,780)	6,979	16,034
Reclassification adjustment for (gains) losses recognized in profit or loss, net of income tax (expense) recovery of (\$1,929) [2013: (\$1,618)]	(5,349)	(4,486)
Reclassification adjustment for impairments, recognized in profit or loss, net of income tax expense of \$227 (2013: \$226) (note 5)	630	625
<b>F » Other comprehensive income (loss)</b>	<b>1,690</b>	<b>12,653</b>
<b>Comprehensive income</b>	<b>\$ 18,750</b>	<b>18,586</b>

Accompanying notes are an integral part of the financial statements.

### F Other comprehensive income: \$1.7 million (after tax amounts quoted)

In the category of other comprehensive income, LAWPRO earned \$1.7 million in 2014. This compares to 2013 other comprehensive income of \$12.7 million, which was primarily driven by a late rally in the markets in that year.

“LAWPRO experienced total comprehensive income for 2014 of \$18.7 million, which resulted in shareholder’s equity of \$208.6 million at the end of 2014.”

### Minimum Capital Test: a key solvency benchmark

The Minimum Capital Test (MCT) is designed to ensure that a financial institution’s assets are sufficient to meet its present and future obligations.

Calculating the MCT at December 31, 2014, LAWPRO’s score is **251 per cent** – up from 233 per cent on December 31, 2013, and above the 220-230 score for which the company aims.

However, regulatory changes have begun to place significant pressure on the company’s MCT result. Less favourable changes to the MCT calculation began to be phased in effective January 1, 2015. The full scope of the changes will come to bear over a 3-year period. A current calculation based on the *eventual* formula (ignoring the phase-in) results in a MCT score of 214 per cent, below the company’s preferred target range. As a result, despite the encouraging financial results in 2014, LAWPRO continues to face pressure to maintain an acceptable MCT result in the coming years. ■