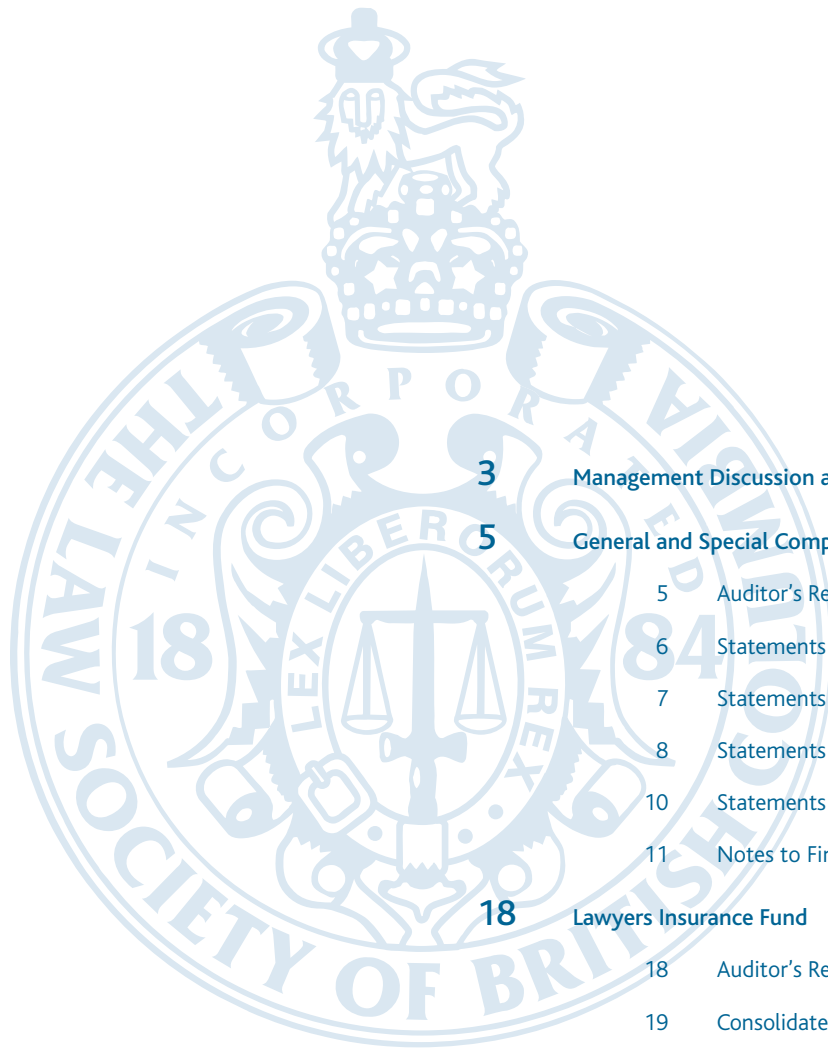




THE LAW SOCIETY OF BRITISH COLUMBIA

Financial Statements

December 31, 2012



**3** Management Discussion and Analysis

**5** General and Special Compensation Funds

5 Auditor's Report

6 Statements of Financial Position

7 Statements of Changes in Net Assets

8 Statements of Revenue and Expenses

10 Statements of Cash Flows

11 Notes to Financial Statements

**18** Lawyers Insurance Fund

18 Auditor's Report

19 Consolidated Statements of Financial Position

20 Consolidated Statements of Changes in Net Assets

21 Consolidated Statements of Revenue and Expenses

22 Consolidated Statements of Cash Flows

23 Notes to Consolidated Financial Statement

The Law Society of British Columbia accounts for its financial activities through three separate funds: the General Fund, the Special Compensation Fund and the Lawyers Insurance Fund (LIF). Society management has the responsibility for assisting the Benchers in fulfilling the Society's mandate, while ensuring that operating expenditures are closely controlled and that appropriate accounting and internal controls are maintained. The 2012 audited financial statements for the three funds are set out in this report. The statements are presented in accordance with the presentation and disclosure standards of the Canadian Institute of Chartered Accountants.

During 2012, in addition to the general oversight by the Benchers, the Finance Committee and the Audit Committee assisted the Benchers in ensuring that management and staff properly managed and reported on the financial affairs of the Society. The oversight by the Benchers, the Finance Committee and the Audit Committee included:

- Reviewing periodic financial statements of the General, Special Compensation and Consolidated Lawyers Insurance Fund
- Reviewing investment performance as managed by the appointed investment managers
- Reviewing with the Law Society's auditors their approach, scope and audit results
- Reviewing the annual Audit Committee Report prepared by the Law Society auditors
- Recommending the 2013 practice fees and assessments, and reviewing corresponding budgets

### General Fund

#### Overview

Overall, the 2012 results for the General Fund were more favourable than expected, operational revenues were higher than expected and the cost of operations was lower than expected, leading to an operating surplus of \$1.4 million.

#### Revenues

General Fund revenue was \$23 million, \$1.5 million higher than 2011 due to growth in the number of lawyers and an increase in the 2012 practice fee. During 2012, net growth in the number of practising lawyers was just below 2% resulting in a total of 10,746 practising lawyers for the year, a similar increase to the last year. The increase in the 2012 practice fee provided for market-based staff salary increases, expenses relating to the implementation of a new regulatory department plan and costs associated with the establishment of the new hearing panel structure. Professional Legal Training Course (PLTC) enrolment revenue was higher than last year, with approximately 410 PLTC students attending during the year. E-filing revenue increased \$129,000 from 2011 due to the implementation of required e-filing in early 2012.

Offsetting these increases was a decline in trust administration fee revenue of \$157,000 compared to 2011, due to the continued downturn in the real estate market.

The Lawyers Insurance Fund contributed \$2.3 million for co-sponsored programs and for general program and administrative expenses attributable to their operations.

The net operating revenue from the Law Society buildings at 845/835 Cambie Street decreased \$508,000, due to lower lease revenues. In 2013, there are two new leases in place, with the Access Pro Bono Society leasing space in 845 Cambie and Bayleaf Software Inc. leasing the second floor of 835 Cambie. The vacant space on the third floor of 835 Cambie continues to be actively marketed.

#### Expenses

The 2012 General Fund expenses were very similar to last year, at \$23.8 million compared to \$23.7 million in 2011.

The regulatory departments had decreased operating expenses from 2011 levels. External professional fees in professional conduct and forensic accounting were lower than last year due to fewer files, and there were staff vacancy cost savings, mainly in the forensic accounting department.

Policy and Legal Services expenses were similar to 2011, with market-based staff salary increases being offset by staff vacancy cost savings within the policy and legal services department and lower hearing panel costs.

Communication and Information Services costs were similar to 2011, with any increases in market-based staff salary costs being offset by printing cost savings due to the electronic distribution of the Benchers' Bulletin and Member's Manual.

Education and Practice expenses increased due to market-based staff salary increases and a staff position vacancy from 2011 being filled in 2012.

General and Administrative costs increased due to market-based staff salary increases.

Benchers Governance expenses were higher as a result of the Benchers undergoing a governance review during the year and a \$75,000 contribution to the CBA Rural Education and Access to Lawyers program. The Federation of Law Societies of Canada contribution increased from \$20 to \$25 per member and CanLII increased \$2.46 to \$34.71 per member.

#### Net Assets

Overall, the General Fund remains financially sound. As of December 31, 2012, net assets in the General fund were \$8.5 million. The General Fund net asset balance (before capital allocation) is \$6.1 million, which equates to three months of operating expenses. In addition, the net assets include \$2.3 million allocated for planned capital expenditures, including the required replacement of two elevators, the fire alarm and the emergency generator at the 845/835 Cambie buildings, as well as workspace improvements within Law Society operational space.

## Special Compensation Fund

### Overview

The Special Compensation Fund was maintained pursuant to Section 31 of the *Legal Profession Act*, was financed by members' annual assessments, and claims were recorded net of recoveries when they had been approved for payment.

During 2012, the *Legal Profession Amendment Act, 2012* repealed section 31 of the *Legal Profession Act*. In addition, Section 23 of the *Legal Profession Act* was amended to remove the requirement that practising lawyers pay the Special Compensation Fund assessment. Section 50 of the *Legal Profession Amendment Act, 2012* provides for the transfer of unused reserves that remain within the Special Compensation Fund to the Lawyers Insurance Fund for the purposes of the insurance program, which is expected to occur in 2013.

Effective May 1, 2004, Part B of the BC Lawyers' Compulsory Professional Liability Insurance Policy provides defined insurance coverage for dishonest appropriation of money or other property entrusted to and received by insured lawyers.

### Revenues

The Special Compensation Fund was funded through a \$1 assessment from each practising lawyer, resulting in total revenue of \$11,000.

### Expenses

Since 2004, the Lawyers Insurance Fund has been providing coverage for dishonest appropriation of funds by lawyers and claims within the scope of the Special Compensation Fund have been declining every year. During the year, claims and administrative costs of \$260,000 were incurred or accrued, offset by \$515,000 in cost recoveries and \$28,000 in interest income.

### Net Assets

At the end of 2012, the Special Compensation Fund net assets were \$1,226,000.

## Lawyers Insurance Fund

### Overview

The Lawyers Insurance Fund remains in a healthy financial position at the end of 2012. Annual assessments were higher due to additional insured members, and overall investment returns were higher than the benchmark.

### Revenues

The insurance assessment remained at \$1,750 per insured member in 2012, resulting in total revenue of \$13.7 million, compared to \$13.4 million in 2011.

During 2012, the long-term investment portfolio earned a return of 9.5%, compared to a benchmark return of 7.2%.

### Expenses

In 2012, LIF general operating costs, including the \$2.3 million contribution to the General Fund, but excluding claims payments and unallocated loss adjustment expenses (ULAE), were \$6.0 million, compared to \$5.6 million in 2011. This increase reflects market-based salary increases and increased stop-loss reinsurance costs.

The net actuarial provision for settlement of claims in 2012 was \$11.0 million, the same as 2011. The provision for claims on the balance sheet at the end of 2012 was \$52.1 million, compared to \$54.5 million in 2011.

### Net Assets

As of December 31, 2012, the LIF net assets were \$49.8 million, which includes \$17.5 million internally restricted for Part B claims, leaving \$32.3 million in unrestricted net assets.



May 9, 2013

## Independent Auditor's Report

### To the Members of The Law Society of British Columbia

We have audited the accompanying financial statements of The Law Society of British Columbia - General and Special Compensation Funds, which comprise the combined statements of financial position as at December 31, 2012, December 31, 2011 and January 1, 2011 and the combined statements of revenue and expenses, changes in net assets, and cash flows for the years ended December 31, 2012 and December 31, 2011, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

#### Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these 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.

#### Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

#### Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of The Law Society of British Columbia - General and Special Compensation Funds as at December 31, 2012, December 31, 2011 and January 1, 2011 and the results of their operations and their cash flows for the years ended December 31, 2012 and December 31, 2011 in accordance with Canadian accounting standards for not-for-profit organizations.

*PricewaterhouseCoopers LLP*

#### Chartered Accountants

*PricewaterhouseCoopers LLP  
PricewaterhouseCoopers Place, 250 Howe Street, Suite 700, Vancouver, British Columbia, Canada V6C 3S7  
T: +1 604 806 7000, F: +1 604 806 7806*

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

THE LAW SOCIETY OF BRITISH COLUMBIA – GENERAL AND SPECIAL COMPENSATION FUNDS

Statements of Financial Position  
As at December 31, 2012

	December 31, 2012		December 31, 2011	January 1, 2011
	General Fund \$	Special Compensation Fund \$	Total \$	Total \$
<b>Assets</b>				
<b>Current assets</b>				
Cash	671,768	500	672,268	177,871
Unclaimed trust funds (note 3)	1,671,528	-	1,671,528	1,681,796
Accounts receivable and prepaid expenses (note 4)	981,687	-	981,687	1,242,948
B.C. Courthouse Library Fund (note 3)	2,487,341	-	2,487,341	635,094
Due from Lawyers Insurance Fund (notes 7 and 11)	19,401,762	1,396,290	20,798,052	18,472,549
	25,214,086	1,396,790	26,610,876	22,210,258
<b>Non-current assets</b>				
Cambie Street property - net (note 5)	11,382,055	-	11,382,055	12,002,361
Other property and equipment - net (note 5)	952,176	-	952,176	1,035,279
Intangible assets - net (note 5)	640,586	-	640,586	336,950
	38,188,903	1,396,790	39,585,693	35,584,848
<b>Liabilities</b>				
<b>Current liabilities</b>				
Accounts payable and accrued liabilities (note 6)	2,572,528	170,594	2,743,122	3,978,948
Liability for unclaimed trust funds (note 3)	1,671,528	-	1,671,528	1,681,796
Current portion of building loan payable (note 10)	500,000	-	500,000	500,000
Deferred revenue (notes 3 and 7)	18,224,916	-	18,224,916	16,065,782
Deferred capital contributions (notes 3 and 8)	58,373	-	58,373	81,129
B.C. Courthouse Library grant (note 3)	2,487,341	-	2,487,341	635,094
Deposits	30,899	-	30,899	19,700
	25,545,585	170,594	25,716,179	22,962,449
<b>Building loan payable</b> (notes 10 and 11)	4,100,000	-	4,100,000	5,100,000
	29,645,585	170,594	29,816,179	28,062,449
<b>Net assets</b>				
Unrestricted	8,543,318	1,226,196	9,769,514	7,522,399
	38,188,903	1,396,790	39,585,693	35,584,848

Commitments (notes 16)

Approved by



President



Chair of Audit Committee

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

THE LAW SOCIETY OF BRITISH COLUMBIA – GENERAL AND SPECIAL COMPENSATION FUNDS

Statements of Changes in Net Assets

For the years ended December 31, 2012 and 2011

	2012		2011	
	General Fund - Unrestricted \$	Special Compensation Fund - Unrestricted \$	Total \$	Total \$
<b>Net assets - Beginning of year</b>	7,112,236	931,753	8,043,989	7,522,399
Net excess of revenue over expenses for the year	1,431,082	294,443	1,725,525	521,590
<b>Net assets - End of year (note 9)</b>	<u>8,543,318</u>	<u>1,226,196</u>	<u>9,769,514</u>	<u>8,043,989</u>

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

THE LAW SOCIETY OF BRITISH COLUMBIA – GENERAL AND SPECIAL COMPENSATION FUNDS

Statements of Revenue and Expenses

For the years ended December 31, 2012 and 2011

	2012		2011	
	General Fund \$	Special Compensation Fund \$	Total \$	Total \$
<b>Revenue</b>				
Practice fees	17,393,093	-	17,393,093	15,956,108
Annual assessments	-	10,818	10,818	53,377
Trust administration fees	2,158,069	-	2,158,069	2,315,568
Enrolment fees	1,041,900	-	1,041,900	965,542
Interest and other income (note 11)	841,216	-	841,216	779,865
E-filing revenue	854,441	-	854,441	725,546
Fines and penalties	367,344	-	367,344	393,018
Application fees	389,770	-	389,770	400,040
	<u>23,045,833</u>	<u>10,818</u>	<u>23,056,651</u>	<u>21,589,064</u>
<b>Expenses</b>				
Bencher Governance				
Bencher, AGM and other committees	1,312,622	-	1,312,622	1,019,072
Federation of Law Societies' contribution	249,680	-	249,680	215,753
CanLII's contribution	375,736	-	375,736	366,792
Pro bono contribution	161,863	-	161,863	157,900
Communication and Information Services				
Communications and publications	1,049,313	-	1,049,313	1,037,341
Information services	1,360,959	-	1,360,959	1,291,539
Education and Practice				
Credentials	522,884	-	522,884	380,460
Ethics	177,574	-	177,574	107,457
Member services	646,661	-	646,661	682,322
Membership assistance programs	229,080	-	229,080	189,860
Practice advice	553,973	-	553,973	528,878
Practice standards	578,205	-	578,205	541,855
Professional Legal Training Course and Education	1,981,842	-	1,981,842	1,890,182
General and Administrative				
Accounting	738,334	-	738,334	792,519
Amortization of other property and equipment	422,988	-	422,988	426,333
General administration	1,703,402	-	1,703,402	1,587,268
Human resources	830,358	-	830,358	860,759
Records management and library	306,849	-	306,849	285,809
Policy and Legal Services				
Policy and tribunal counsel	1,323,681	-	1,323,681	1,392,808
External litigation and interventions	155,483	-	155,483	164,872
Unauthorized practice	304,230	-	304,230	318,006
Regulation				
Custodianship costs	1,346,852	-	1,346,852	1,371,615
Discipline	1,208,454	-	1,208,454	1,131,044
Professional conduct - intake and investigations	3,921,672	-	3,921,672	4,106,300
Forensic accounting	407,735	-	407,735	948,353
Trust assurance	1,962,182	-	1,962,182	1,930,828
	<u>23,832,612</u>	<u>-</u>	<u>23,832,612</u>	<u>23,725,925</u>
Carried forward	23,832,612	-	23,832,612	23,725,925

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



	2012		2011	
	General Fund \$	Special Compensation Fund \$	Total \$	Total \$
Brought forward	23,832,612	-	23,832,612	23,725,925
<b>Special Compensation Fund</b>				
Recoveries	-	(515,460)	(515,460)	-
Claims and costs (note 12)	-	162,399	162,399	(93,100)
General and administrative costs	-	97,196	97,196	71,397
Loan interest income from Lawyers Insurance Fund (note 11)	-	(27,760)	(27,760)	(26,318)
	23,832,612	(283,625)	23,548,987	23,677,904
<b>Costs recovered from Special Compensation and Lawyers Insurance Funds</b>				
Co-sponsored program costs	(783,053)	-	(783,053)	(717,773)
Program and administrative costs	(1,556,930)	-	(1,556,930)	(1,506,600)
	21,492,629	(283,625)	21,209,004	21,453,531
<b>Excess of revenue over expenses before the following:</b>	1,553,204	294,443	1,847,647	135,533
<b>845 Cambie net results</b>				
Rental revenue	115,698	-	115,698	418,113
Allocated rental revenue (note 3)	1,772,320	-	1,772,320	1,732,329
	1,888,018	-	1,888,018	2,150,442
<b>Expenses</b>				
Amortization	547,813	-	547,813	546,908
Insurance	72,323	-	72,323	66,027
Loan interest expense (note 10)	110,293	-	110,293	143,709
Property management	189,858	-	189,858	198,479
Property taxes	481,360	-	481,360	430,332
Repair and maintenance	677,473	-	677,473	553,124
Utilities	113,827	-	113,827	142,865
Recovery from tenants	(182,807)	-	(182,807)	(317,059)
	2,010,140	-	2,010,140	1,764,385
<b>Net 845 Cambie operating revenue</b>	(122,122)	-	(122,122)	386,057
<b>Net excess of revenue over expenses for the year</b>	1,431,082	294,443	1,725,525	521,590

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

## Statements of Cash Flows

For the years ended December 31, 2012 and 2011

	2012		2011	
	General Fund \$	Special Compensation Fund \$	Total \$	Total \$
<b>Cash flows from operating activities</b>				
Net excess of revenue over expenses for the year	1,431,082	294,443	1,725,525	521,590
Items not affecting cash				
Amortization of Cambie Street building and tenant improvements	592,951	-	592,951	546,908
Amortization of other property and equipment	278,926	-	278,926	332,144
Amortization of intangible assets	98,924	-	98,924	94,189
Amortization of deferred capital contributions	(11,378)	-	(11,378)	(11,378)
Loss on disposal of capital assets	13,873	-	13,873	8,529
	2,404,378	294,443	2,698,821	1,491,982
Decrease (increase) in current assets				
Unclaimed trust funds	176,323	-	176,323	(166,055)
Accounts receivable and prepaid expenses	147,376	-	147,376	113,886
B.C. Courthouse Library Fund	(1,809,623)	-	(1,809,623)	(42,624)
Increase (decrease) in current liabilities				
Accounts payable and accrued liabilities	(1,465,992)	162,399	(1,303,593)	69,966
Liability for unclaimed trust funds	(176,323)	-	(176,323)	166,055
Deferred revenue	733,819	(10,450)	723,369	1,435,765
B.C. Courthouse Library grant	1,809,623	-	1,809,623	42,624
Deposits	1,500	-	1,500	7,500
	1,821,081	446,392	2,267,473	3,119,099
<b>Cash flows from financing activities</b>				
Decrease in long-term debt	(500,000)	-	(500,000)	(500,000)
<b>Cash flows from investing activities</b>				
Property and equipment	(459,109)	-	(459,109)	(708,879)
Intangible assets	(398,684)	-	(398,684)	-
	(857,793)	-	(857,793)	(708,879)
<b>Interfund transfers</b>	(70,675)	(446,392)	(517,067)	(1,808,436)
<b>Increase in cash</b>	392,613	-	392,613	101,784
<b>Cash - Beginning of year</b>	279,155	500	279,655	177,871
<b>Cash - End of year</b>	671,768	500	672,268	279,655
<b>Supplementary cash flow information</b>				
Interest paid	110,293	-	110,293	143,709
Interest income received	245,839	27,760	273,599	362,445

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

**1. Nature of operations**

The General Fund comprises the assets, liabilities, net assets, revenue and expenses of the operations of The Law Society of British Columbia (the Society) other than those designated to the statutory Special Compensation Fund and the Lawyers Insurance Fund (including its wholly owned subsidiary, LSBC Captive Insurance Company Ltd.).

The Special Compensation Fund is maintained by the Society pursuant to Section 31 of the Legal Profession Act. The Special Compensation Fund is financed by members' annual assessments, and claims are recorded net of recoveries from the Special Compensation Fund's insurers when they have been approved for payment by the Special Compensation Fund Committee as delegated by the Benchers and the settlement has been accepted by the claimant. The Legal Profession Act provides that the assets of the Special Compensation Fund are not subject to process of seizure or attachment by creditors of the Society.

Effective May 1, 2004, Part B to the B.C. Lawyers' Compulsory Professional Liability Insurance Policy provides defined insurance coverage for dishonest appropriation of money or other property entrusted to and received by insured lawyers in their capacity as barrister and solicitor and in relation to the provision of professional services. Part B (Trust Protection Coverage) is recorded in the Lawyers Insurance Fund.

The Society is a not-for-profit organization and the Funds are considered to be non-assessable under current income tax legislation.

Separate financial statements have been prepared for the Lawyers Insurance Fund, including LSBC Captive Insurance Company Ltd.

**2. First time adoption of accounting standards for not-for-profit organizations**

Effective January 1, 2012, the Society elected to adopt Canadian accounting standards for not-for-profit organizations (Part III of the Canadian Institute of Chartered Accountants Handbook) (ASNPO) as issued by the Canadian Accounting Standards Board. The accounting policies selected under this framework have been applied consistently and retrospectively as if these policies had always been in effect. The organization has not utilized any transitional exemptions on the adoption of ASNPO. There were no adjustments to the statement of financial position or the statements of revenue and expenses, changes in net assets and cash flows.

\$

**Statement of changes in net assets**

Net assets at December 31, 2010, as previously reported (transitional adjustments not required)	7,522,399
	<u>-</u>
Opening net assets as at January 1, 2011 under ASNPO	<u>7,522,399</u>

**Statement of revenue and expenses**

Excess of revenue over expenses for the year ended December 31, 2011, as previously reported (transitional adjustments not required)	521,590
	<u>-</u>
Excess of revenue over expenses for the year ended December 31, 2011 under ASNPO	<u>521,590</u>

**3. Significant accounting policies**

These financial statements are prepared in accordance with ASNPO.

**Allocated administrative expenses**

Administrative expenses are recovered by the General Fund from both the Lawyers Insurance and Special Compensation Funds. Recoveries are based on amounts derived either on percentage of use, the proportion of the Lawyers Insurance Fund's staff compared to the Society's total staff costs, or a set amount.

**Allocated rental revenue**

The Cambie Street property is treated as a separate cost centre. Allocated rental revenue represents estimated market rent, allocated to each of the Funds. The corresponding rental expense is included within the relevant functions and therefore has not been eliminated in the preparation of these financial statements.

**B.C. Courthouse Library Fund**

The Society administers funds held on behalf of the B.C. Courthouse Library. Such funds are held in trust and the use of the funds is not recorded in the statement of revenue and expenses of the General Fund. The Society grants money to the B.C. Courthouse Library through its fees per lawyer assessments.

**Cash and cash equivalents**

Cash and cash equivalents comprise cash on hand, demand deposits, and short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value.

**Claims liabilities**

In accordance with the absolute discretionary nature of the Special Compensation Fund arrangements, the claims become a liability only when approved by the Special Compensation Fund Committee and accepted by the claimant.

**Deferred capital contributions**

Contributions restricted for the purchase of capital assets are deferred and recognized as revenue on the same basis as the capital assets are amortized.

**Fair value of financial instruments**

The fair values of cash, accounts receivable, and accounts payable and accrued liabilities correspond to their carrying values due to their short-term nature.

The carrying values of the interfund balances including the building loan payable and other interfund transactions are recorded at their carrying amounts which approximate their exchange amounts.

**Intangible assets**

Intangible assets comprise computer software. Software is recorded at cost and amortized on a straight-line basis at 10% - 20% per annum.

**Property and equipment**

Property and equipment, including leasehold improvements, are recorded at cost less accumulated amortization.

The Society provides for amortization on a straight-line basis as follows:

Buildings	2-1/2% per annum
Computer hardware	10% - 20% per annum
Furniture and fixtures	10% per annum
Leasehold improvements	10% per annum

Tenant improvements are amortized over the term of the lease to which they relate. The Society recognizes a full year's amortization expense in the year of acquisition.

**Revenue recognition**

The Society follows the deferral method of accounting for annual fees and assessments. Fees and assessments are billed and received in advance on a calendar-year basis. Accordingly, fees and assessments for the next fiscal year received prior to December 31 have been recorded as deferred revenue for financial reporting purposes and will be recognized as revenue in the next calendar year.

All other revenues are recognized when earned if the amount to be received can be reasonably estimated and collection is reasonably assured.

**Unclaimed trust funds**

The General Fund recognizes unclaimed trust funds as an asset as well as a corresponding liability on the statement of financial position. If these funds are claimed, the owner of the trust fund balance is entitled to the principal balance plus interest at prime rate minus 2%. Due to the historically low collection rates on these balances, the General Fund does not accrue for any interest owing on the trust fund amounts held and recognizes income earned from the unclaimed trust fund investments in the statement of revenue and expenses. Unclaimed funds outstanding for more than five years are transferred to the Law Foundation of British Columbia.

**Use of estimates**

The preparation of financial statements in accordance with ASNPO requires management to make estimates and assumptions that affect the reported amounts of certain assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of certain revenues and expenses during the year. Actual results could differ from these estimates.

**4. Accounts receivable**

Accounts receivable are presented net of the allowance for doubtful accounts of \$651,531 (2011 - \$629,727).

5. Property, equipment and intangible assets

a) 845 Cambie Street property

December 31, 2012			
	Cost \$	Accumulated amortization \$	Net \$
Land	4,189,450	-	4,189,450
Buildings	12,011,261	6,034,257	5,977,004
Leasehold improvements	5,943,787	4,729,190	1,214,597
Tenant improvements	989,595	988,591	1,004
	23,134,093	11,752,038	11,382,055

December 31, 2011			
	Cost \$	Accumulated amortization \$	Net \$
Land	4,189,450	-	4,189,450
Buildings	12,011,261	5,705,653	6,305,608
Leasehold improvements	5,708,012	4,465,705	1,242,307
Tenant improvements	989,565	987,699	1,866
	22,898,288	11,159,057	11,739,231

January 1, 2011			
	Cost \$	Accumulated amortization \$	Net \$
Land	4,189,450	-	4,189,450
Buildings	12,065,416	5,377,024	6,688,392
Leasehold improvements	5,326,646	4,205,555	1,121,091
Tenant improvements	1,103,252	1,099,824	3,428
	22,684,764	10,682,403	12,002,361

b) Other property and equipment

December 31, 2012			
	Cost \$	Accumulated amortization \$	Net \$
Furniture and fixtures	2,258,669	1,653,756	604,913
Computer hardware	964,698	617,443	347,255
Artwork and collectibles	45,412	45,405	7
Law libraries - at nominal value	1	-	1
	3,268,780	2,316,604	952,176

**December 31, 2011**

	<b>Cost</b>	<b>Accumulated</b>	<b>Net</b>
	<b>\$</b>	<b>amortization</b>	<b>\$</b>
		<b>\$</b>	<b>\$</b>
Furniture and fixtures	2,441,025	1,731,594	709,431
Computer hardware	1,214,322	902,112	312,210
Artwork and collectibles	45,405	45,405	-
Law libraries - at nominal value	1	-	1
	<u>3,700,753</u>	<u>2,679,111</u>	<u>1,021,642</u>

**January 1, 2011**

	<b>Cost</b>	<b>Accumulated</b>	<b>Net</b>
	<b>\$</b>	<b>amortization</b>	<b>\$</b>
		<b>\$</b>	<b>\$</b>
Furniture and fixtures	2,533,698	1,844,474	689,224
Computer hardware	1,109,836	763,782	346,054
Artwork and collectibles	45,405	45,405	-
Law libraries - at nominal value	1	-	1
	<u>3,688,940</u>	<u>2,653,661</u>	<u>1,035,279</u>

c) Intangible assets

**December 31, 2012**

	<b>Cost</b>	<b>Accumulated</b>	<b>Net</b>
	<b>\$</b>	<b>amortization</b>	<b>\$</b>
		<b>\$</b>	<b>\$</b>
Computer software	1,204,475	563,889	640,586

**December 31, 2011**

	<b>Cost</b>	<b>Accumulated</b>	<b>Net</b>
	<b>\$</b>	<b>amortization</b>	<b>\$</b>
		<b>\$</b>	<b>\$</b>
Computer software	805,792	464,966	340,826

**January 1, 2011**

	<b>Cost</b>	<b>Accumulated</b>	<b>Net</b>
	<b>\$</b>	<b>amortization</b>	<b>\$</b>
		<b>\$</b>	<b>\$</b>
Computer software	707,726	370,776	336,950

In 2012, intangible assets, consisting entirely of computer software, with an aggregate amount of \$398,683 (2011 - \$98,066) were purchased.

**6. Government remittances**

The following government remittances are included in accounts payable:

	December 31, 2012 \$	December 31, 2011 \$	January 1, 2011 \$
Receiver General - payroll withholding tax	-	28,202	-
Medical Services Plan of BC	(156)	(1,202)	(1,221)
Receiver General - HST	41,673	41,522	-
<b>Total government remittances payable</b>	<b>41,517</b>	<b>68,522</b>	<b>(1,221)</b>

**7. Deferred revenue**

As at December 31, 2012, fees and assessments of \$18.2 million (2011 - \$17.5 million) related to the subsequent year were received and recorded as deferred revenue. Revenue will be recognized on a monthly basis as earned. Surplus funds are invested in the Lawyers Insurance Fund's investment portfolio.

**8. Deferred capital contributions**

Deferred capital contributions represent externally restricted grants for the purchase of Professional Legal Training Course related capital assets. Unamortized amounts which will be recognized as revenue in future periods are as follows:

	2012 \$	2011 \$
Balance - Beginning of year	69,751	81,129
Less: Amortization for the year	(11,378)	(11,378)
<b>Balance - End of year</b>	<b>58,373</b>	<b>69,751</b>

**9. Unrestricted net assets**

The General Fund unrestricted net assets include \$71,517 (2011 - \$238,835) which has been appropriated for contribution to future trust administration fee related expenses. During the year, \$2.2 million (2011 - \$2.3 million) in trust administration fee revenue was collected, and \$2.3 million (2011 - \$2.3 million) in trust administration fee expenses were incurred.

The General Fund unrestricted net assets also include \$2,301,567 (2011 - \$1,870,561) which has been allocated to capital expenditures in accordance with the capital plan.

**10. Building loan payable**

In 1992, the Benchers authorized the borrowing of monies from the Lawyers Insurance Fund to fund the capital development of the Society's buildings at 845 Cambie Street, Vancouver, BC. The loan is secured by the building, has no fixed repayment terms and bears interest calculated monthly at a rate equal to the stated monthly bond yield to maturity earned on the Lawyers Insurance Fund investment portfolio. Interest paid on the building loan is disclosed in note 11. The outstanding building loan balance at the end of the 2012 year is \$4.6 million. It is the intention of the Benchers to require the General Fund to repay a minimum of \$500,000 of the principal each year. During 2012, principal of \$500,000 (2011 - \$500,000) was repaid.

	2012 %	2011 %
Weighted average rate of interest	2.39	2.81

**11. Interfund transactions**

The operations of the General, Lawyers Insurance and Special Compensation Funds are controlled by the management of the Society. Balances between the funds generally arise from transactions of an operating nature and are recorded at the exchange amount at the dates of the transactions. Surplus funds are invested in the Lawyers Insurance Fund's investment portfolio.

Amounts due to and from the Lawyers Insurance Fund are due on demand and have no fixed terms of repayment. The Lawyers Insurance Fund has authorized a loan facility of up to \$1 million, of which \$nil has been drawn down at December 31, 2012 (2011 - \$nil), to the General Fund to fund capital expenditures in accordance with the capital plan. The Lawyers Insurance Fund has also authorized a loan facility of up to \$8 million, of which \$nil has been drawn down at December 31, 2012 (2011 - \$nil), to the Special Compensation Fund.

Monthly interest on the Lawyers Insurance Fund's net loan position with the General and Special Compensation Funds is earned at the rate equal to the stated monthly bond yield to maturity earned on the Lawyers Insurance Fund investment portfolio. The average bond yield for 2012 was 2.39% (2011 - average rate - 2.81%). The General Fund's net loan position includes the General Fund's building loan and other operating balances with the Lawyers Insurance Fund. The net loan position fluctuates during the year as amounts are transferred between the General Fund, the Special Compensation Fund and the Lawyers Insurance Fund to finance ongoing operations.

During 2012, interest of \$110,293 was paid on the building loan and interest revenue of \$245,839 was received from General Fund cash balances held by the Lawyers Insurance Fund and \$27,760 was received from Special Compensation Fund cash balances held by the Lawyers Insurance Fund for a net interest income of \$163,306.

During 2011, interest of \$143,709 was paid on the building loan and interest revenue of \$263,604 was received from General Fund cash balances held by the Lawyers Insurance Fund and \$26,318 was received from Special Compensation Fund cash balances held by the Lawyers Insurance Fund for a net interest income of \$146,213.

Other interfund transactions are disclosed elsewhere in these financial statements.

## 12. Special Compensation Fund claims and program changes

### a) Outstanding claims

Pursuant to section 31(6) of the Legal Profession Act, the payment of Special Compensation Fund claims is at the discretion of the Special Compensation Fund Committee as delegated by the Benchers. As at December 31, 2012, there were no remaining claims for which statutory declarations had been received. All claims for which statutory declarations were received have been reviewed by the Special Compensation Fund Committee.

For claims reported prior to May 1, 2004, the insurance bond provided that total claims attributable to the period in excess of \$2,500,000 were 100% reimbursed by a commercial insurer up to a maximum of \$15,000,000 for claims against one lawyer and in total, other than as noted in note 12(b). As set out in note 1, claims reported after May 1, 2004, are subject to Part B coverage by the Lawyers Insurance Fund.

### b) Wirick case

In May 2002, the Discipline Committee ordered an audit investigation, pursuant to Rule 4-43, of Martin Keith Wirick's practice.

At December 31, 2012, there were no remaining claims still under consideration.

Until May 1, 2004, the Special Compensation Fund carried insurance of \$15,000,000 for each bond period (\$17,500,000 total coverage with a deductible of \$2,500,000). The bond period is defined as the year in which the Society becomes aware of evidence indicating a member may have been guilty of an act or acts of misappropriation or wrongful conversion. All claims concerning Mr. Wirick fell into the 2002 bond period and, as such, the Special Compensation Fund had claims greater than its level of insurance. In early 2005, the final proof of loss that reached this limit was filed. In 2002, the Benchers agreed to allow the Special Compensation Fund Committee to exceed the \$17,500,000 cap they had imposed in the Society rules.

In 2006, the Benchers approved a payment of \$7,543,528 to be paid to claimants over four years commencing in fiscal 2007 at \$1,885,882 per year. The final payment was made in 2010.

In December 2012, the Benchers approved a further payment of \$162,399 to be paid to claimants in 2013. This amount has been accrued in the financial statements of the Special Compensation Fund.

In 2012, the Special Compensation Fund recovered \$515,459 (2011 - \$94,100) related to the Wirick case.

### c) Changes to Special Compensation Fund

Effective January 1, 2013, the Legal Profession Amendment Act, 2012 repealed Section 31 of the Legal Profession Act (LPA). The legislation was changed pursuant to Section 50 of the Legal Profession Amendment Act, 2012 (SBC 2012, C16), to initiate the transfer of unused reserves that remain within the Special Compensation Fund, after all recoveries are received and expenses and claims are paid, to be used in the Lawyers Insurance Fund. Additionally, Section 23 of LPA was amended to remove the requirement that practising lawyers pay the Special Compensation Fund assessment. Accordingly, for 2013, the per member Special Compensation Fund assessment has been reduced to \$nil (2012 - \$1).

## 13. Related parties

The elected Benchers include members drawn from law firms across the province. These law firms may at times be engaged by the Society in the normal course of business. During the year ended December 31, 2012, expenses of \$140,517 (2011 - \$188,949) recorded at carrying amount were incurred by the General Fund during the normal course of business with these law firms.



**14. Capital management**

The Society defines its capital as the amounts included in its unrestricted net assets. Its objective when managing capital is to safeguard its ability to continue as a going concern so that it can continue to fulfil its objectives and meet its requirements.

**15. Financial instruments**

The General and Special Compensation Funds' financial instruments consist of cash, accounts receivable, and accounts payable and accrued liabilities.

The significant financial risks to which the Society is exposed are credit risk and liquidity risk.

a) Credit risk

Cash and accounts receivable expose the Funds to credit risk.

The maximum exposure to credit risk arising from the above-noted items is \$1,017,347 (2011 - \$739,199). Credit risk arises from the possibility that a counterparty to an instrument fails to meet its obligations.

b) Liquidity risk

Liquidity risk is the risk that the Funds will not be able to meet all cash outflow requirements. Financial instruments held by the Society are limited to cash, accounts receivable and accounts payable and accrued liabilities and, therefore, bear no significant liquidity risk.

**16. Obligations and commitments under operating leases**

The Society has committed to payments under certain operating leases relating to vehicle costs. Future minimum lease payments required in each of the next five fiscal years and thereafter are:

	2012 \$	2011 \$
For the year ended December 31		
2012	25,112	25,112
2013	39,149	7,402
2014	24,144	6,987
2015	20,069	2,911
2016	17,158	-
2017	1,911	-
Thereafter	-	-
Total future minimum lease payments	<u>127,543</u>	<u>42,412</u>

For the year ended December 31, 2012, an amount of \$25,112 representing payments under operating leases was expensed (2011 - \$29,919).



May 9, 2013

## Independent Auditor's Report

### To the Members of The Law Society of British Columbia

We have audited the accompanying consolidated financial statements of The Law Society of British Columbia – Lawyers Insurance Fund, and its subsidiary, which comprise the consolidated statements of financial position as at December 31, 2012, December 31, 2011 and January 1, 2011 and the consolidated statements of revenue and expenses, changes in net assets, and cash flows for the years ended December 31, 2012 and December 31, 2011, and the related notes, which comprise a summary of significant accounting policies and other explanatory information

#### Management's responsibility for the consolidated financial statements

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated financial statements that are free from material misstatement, whether due to fraud or error.

#### Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

#### Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of The Law Society of British Columbia – Lawyers Insurance Fund and its subsidiary, as at December 31, 2012, December 31, 2011 and January 1, 2011 and the results of their operations and their cash flows for the years ended December 31, 2012 and December 31, 2011 in accordance with Canadian accounting standards for not-for-profit organizations.

*PricewaterhouseCoopers LLP*

#### Chartered Accountants

*PricewaterhouseCoopers LLP*  
*PricewaterhouseCoopers Place, 250 Howe Street, Suite 700, Vancouver, British Columbia, Canada V6C 3S7*  
*T: +1 604 806 7000, F: +1 604 806 7806*

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

THE LAW SOCIETY OF BRITISH COLUMBIA – LAWYERS INSURANCE FUND  
Consolidated Statements of Financial Position

	December 31, 2012 \$	December 31, 2011 \$	January 1, 2011 \$
<b>Assets</b>			
Cash	3,869,634	5,133,153	2,806,770
Accounts receivable - net of allowance (note 4)	491,321	794,665	685,508
Prepaid expenses	498,226	25,272	115,962
Short-term investments (note 5)	19,355,051	18,585,598	18,727,783
Reinsurers' share of provision for claims (note 1)	-	423,000	825,000
Members' share of provision for claims	1,093,888	1,231,902	1,105,231
General Fund building loan (note 7)	4,600,000	5,100,000	5,600,000
Investments (note 6)	108,573,086	102,895,235	108,286,716
	<u>138,481,206</u>	<u>134,188,825</u>	<u>138,152,970</u>
<b>Liabilities</b>			
Accounts payable and accrued liabilities (note 4)	1,707,090	1,232,478	2,339,524
Deferred revenue	6,947,265	6,812,979	6,706,891
Due to General Fund (note 9)	19,401,762	19,331,087	17,577,601
Due to Special Compensation Fund (note 9)	1,396,290	949,898	894,948
Provision for claims (note 8)	52,052,328	54,530,489	57,582,333
Provision for ULAE (note 8)	7,155,000	7,065,000	7,618,000
	<u>88,659,735</u>	<u>89,921,931</u>	<u>92,719,297</u>
<b>Net assets</b>			
Unrestricted net assets	32,321,471	26,766,894	27,933,673
Internally restricted net assets (note 10)	17,500,000	17,500,000	17,500,000
	<u>49,821,471</u>	<u>44,266,894</u>	<u>45,433,673</u>
	<u>138,481,206</u>	<u>134,188,825</u>	<u>138,152,970</u>

Commitments (note 9)

Contingencies (note 13)

Approved by

  
President

  
Chair of Audit Committee

The accompanying notes are an integral part of these consolidated financial statements.

THE LAW SOCIETY OF BRITISH COLUMBIA – LAWYERS INSURANCE FUND

Consolidated Statements of Changes in Net Assets  
For the years ended December 31, 2012 and 2011

	2012		2011
	Unrestricted \$	Internally restricted \$	Total \$
<b>Net assets - Beginning of year</b>	26,766,894	17,500,000	44,266,894
Excess (deficiency) of revenue over expenses for the year	5,554,577	-	5,554,577
<b>Net assets - End of year</b>	32,321,471	17,500,000	49,821,471

The accompanying notes are an integral part of these consolidated financial statements.

THE LAW SOCIETY OF BRITISH COLUMBIA – LAWYERS INSURANCE FUND

Consolidated Statements of Revenue and Expenses  
For the years ended December 31, 2012 and 2011

	2012 \$	2011 \$
<b>Revenue</b>		
Annual assessments	13,665,545	13,436,523
Investment income (notes 2 and 6)	2,729,208	3,082,450
Other income	90,096	30,827
	<u>16,484,849</u>	<u>16,549,800</u>
<b>Insurance expenses</b>		
Actuary, consultant and investment manager fees	390,137	433,126
Allocated office rent from General Fund	148,280	148,280
Contribution to program and administrative costs of General Fund	1,566,272	1,515,668
Office	803,530	532,897
Premium taxes	13,184	13,448
Provision for settlement of claims (note 8)	11,010,313	10,960,438
Provision for (recovery of) ULAE (note 8)	90,000	(553,000)
Salaries, wages and benefits	2,336,090	2,234,875
	<u>16,357,806</u>	<u>15,285,732</u>
<b>Loss prevention expenses</b>		
Contribution to co-sponsored program costs of General Fund	783,053	713,023
	<u>17,140,859</u>	<u>15,998,755</u>
<b>(Deficiency) excess of revenue over expenses before the following</b>	(656,010)	551,045
<b>Fair value changes in investments</b> (notes 2 and 6)	6,216,336	(1,712,830)
	5,560,326	(1,161,785)
<b>Provision for income taxes</b>	5,749	4,994
<b>Excess (deficiency) of revenue over expenses for the year</b>	<u>5,554,577</u>	<u>(1,166,779)</u>

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Statements of Cash Flows  
For the years ended December 31, 2012 and 2011

	2012 \$	2011 \$
<b>Cash flows from operating activities</b>		
Excess (deficiency) of revenue over expenses for the year	5,554,577	(1,166,779)
Items not affecting cash		
Unrealized (gain) loss on investments	(5,878,139)	11,471,797
Realized gain on disposal of investments	(338,197)	(9,666,685)
Amortization of 750 Cambie Street building	442,431	439,188
Amortization of deferred tenant inducement	35,244	38,486
	(184,084)	1,116,007
Decrease (increase) in assets		
Accounts receivable	303,344	(109,157)
Prepaid expenses	(472,954)	90,690
Short-term investments	(769,453)	142,185
Reinsurers' share of provision for claims	423,000	402,000
Members' share of provision for claims	138,014	(126,671)
Increase (decrease) in liabilities		
Accounts payable and accrued liabilities	474,612	(1,107,046)
Deferred revenue	134,286	106,088
Provision for claims	(2,478,161)	(3,051,844)
Provision for ULAE	90,000	(553,000)
Purchase of investments	(4,689,190)	(44,702,858)
Proceeds from disposal of investments	4,750,000	47,811,553
	(2,280,586)	17,947
<b>Cash flows from investing activities</b>		
Decrease in General Fund building loan	500,000	500,000
<b>Cash flows from financing activities</b>		
Interfund transfers (note 9)	517,067	1,808,436
<b>(Decrease) increase in cash</b>	(1,263,519)	2,326,383
<b>Cash - Beginning of year</b>	5,133,153	2,806,770
<b>Cash - End of year</b>	3,869,634	5,133,153
<b>Supplementary cash flow information</b>		
Interest paid	273,599	289,925
Interest income received	110,293	143,907

The accompanying notes are an integral part of these consolidated financial statements.

**1. Nature of operations**

The Lawyers Insurance Fund (the Fund) is maintained by The Law Society of British Columbia (the Society) pursuant to Section 30 of the Legal Profession Act. The Society is a not-for-profit organization, and only the subsidiary, LSBC Captive Insurance Company Ltd. (the Captive), is considered assessable for income tax under current legislation. Effective January 1, 1990, the Fund began underwriting the program by which errors and omissions insurance is provided to members of the Society.

**Part A**

The Society's members have limits of coverage for claims and potential claims arising from negligent acts, errors or omissions under Part A of the B.C. Lawyers' Compulsory Professional Liability Insurance Policy (the Policy) as follows:

	\$		\$
The Fund	995,000	or	990,000
Deductible - applicable to indemnity payments only	5,000	or	10,000
Limit per error or related errors			1,000,000
Annual aggregate limit for all errors per member			2,000,000

The amount of the member deductible is \$5,000 for each initial claim resulting in the payment of damages and \$10,000 for each additional claim within a three-year period resulting in the payment of damages.

For claims reported between 1990 and 1996, the Captive entered into reinsurance contracts under which all claim payments above a per claim limit and in excess of inner aggregate retentions were ceded to reinsurers. Reinsurance does not relieve the Captive of primary liability as the originating insurer. For the 2012 policy year, the Society and the Captive have obtained stop-loss reinsurance in the amount of \$12,000,000 to cover aggregate payments over \$25,000,000 for Parts A and C of the Policy. This limit is co-insured 80/20 with the reinsurer paying 80% of losses over \$25,000,000 to a maximum of \$12,000,000 and the Fund paying 20%. All losses on claims since 1997 are fully reimbursed by the Fund on behalf of the Society under agreement.

**Part B**

Effective May 1, 2004, Part B of the Policy provides defined insurance coverage for dishonest appropriation of money or other property entrusted to and received by insured lawyers in their capacity as barristers and solicitors and in relation to the provision of professional services.

For the 2012 policy period, there is a \$300,000 per claim limit and a \$17,500,000 profession-wide annual aggregate limit. The Fund has obtained reinsurance in the amount of \$5,000,000 to cover a portion of the annual aggregate limit. There is no deductible. This reinsurance attaches above a \$3,000,000 deductible and is co-insured 80/20 with the reinsurer paying 80% of losses over \$3,000,000 to a maximum of \$5,000,000 and the Society paying 20%.

**Part C**

Effective January 1, 2012, Part C of the Policy provides defined insurance coverage for trust shortages suffered by insured lawyers as a result of relying on fraudulent certified cheques.

For the 2012 policy period, there is a limit of \$500,000 per claim, and per lawyer and firm annually, a profession-wide annual aggregate of \$2 million, and a deductible of 35% of the client trust fund shortage (reduced by the amount of any overdraft paid). Coverage is contingent upon compliance with the Society's client identification and verification rules.

**2. First time adoption of accounting standards for not-for-profit organizations**

Effective January 1, 2012, the Society elected to adopt Canadian accounting standards for not-for-profit organizations (Part III of the Canadian Institute of Chartered Accountants Handbook) (ASNPO) as issued by the Canadian Accounting Standards Board. The accounting policies selected under this framework have been applied consistently and retrospectively as if these policies had always been in effect. The Society has not utilized any transitional exemptions on the adoption of ASNPO and the following adjustments were made on transition:

The excess of revenue over expenses for the year ended December 31, 2011 increased by \$7,266,867 to reflect the change in fair value of the investments in equity securities quoted in an active market. Prior to the transition, changes in the fair value of these investments were recorded in the statement of changes in net assets.

The transition from Canadian generally accepted accounting principles (GAAP) to ASNPO had no significant impact on cash flows generated by the Society.

**Consolidated statement of changes in net assets**

Transitional adjustments were not required in the three years presented other than to excess of revenue over expenses as detailed below and the inclusion of amounts relating to unrealized gain on investments as required under ASNPO.

	\$
Net assets at December 31, 2010, as previously reported	45,433,673
Transitional adjustments:	
• Other comprehensive income previously recorded in consolidated statement of changes in net assets	(18,738,664)
• Fair value changes in investments as part of consolidated statement of revenue and expenses	18,738,664
	45,433,673
Opening net assets as at January 1, 2011 under ASNPO	45,433,673
Net assets at December 31, 2011, as previously reported	44,266,894
Transitional adjustments:	
• Fair value changes in investments recognized in consolidated statement of revenue and expenses on transition	(11,471,797)
• Other comprehensive income representing unrealized gains on available-for-sale financial assets previously recorded in consolidated statement of changes in net assets	11,471,797
	44,266,894
Net assets as at December 31, 2011 under ASNPO	44,266,894

**Consolidated statement of revenue and expenses**

	\$
Excess of revenue over expenses as previously reported for the year ended December 31, 2011	10,305,018
Unrealized loss on investments previously recorded as an adjustment to net assets	(11,471,797)
	(1,166,779)
Deficiency of revenue over expenses for the year ended December 31, 2011 under ASNPO	(1,166,779)

**3. Significant accounting policies**

These financial statements are prepared in accordance with ASNPO.

**Basis of consolidation**

These consolidated financial statements include the accounts of the Fund and the Captive, a wholly owned subsidiary.

Separate financial statements have been prepared for the Law Society's General Fund and Special Compensation Fund.

**Allocated administrative expenses**

Administrative expenses are recovered by the General Fund of the Society from the Fund. Recoveries are based on amounts derived either on percentage of use or the proportion of the Fund's staff compared to the Society's total staff cost, or a set amount.

**Amortization**

Amortization is provided on a straight-line basis as follows:

Building - 750 Cambie Street	2-1/2% per annum
Base building improvements	2-1/2% per annum
Tenant improvements	over lease period
Deferred tenant inducements	over lease period

**Cash**

Cash comprises cash on hand.

**Deferred tenant inducements**



In 2006, the Fund provided two of its tenants in the 750 Cambie Street building with free gross rent of \$408,706 at the start of the lease. This free gross rent is amortized over the term of the lease.

#### **Fair value of financial instruments**

The fair values of cash, accounts receivable, short-term investments, accounts payable and accrued liabilities and claims payable correspond to their carrying values due to their short-term nature.

The interfund balances including the building loan receivable and other interfund transactions are recorded at their carrying amounts which approximate their exchange amounts.

#### **Short-term investments**

Short-term investments consist of pooled fund money market investments with maturities of less than one year.

#### **Investments**

The Fund's investments consist of units in pooled equity and bond funds and are initially and subsequently measured at fair value. Changes in fair value are recognized in the statement of revenue and expenses in the period incurred. Transaction costs that are directly attributable to the acquisition of these investments are recognized in the statement of revenue and expenses in the period incurred.

#### **Investment income**

Investment income and pooled fund distributions are recorded on an accrual basis. Dividends are recorded on the date of record. Gains and losses realized on the disposal of investments are taken into income on the date of disposal.

#### **Provision for claims**

The provision for claims and unallocated loss adjustment expenses (ULAE) represents an estimate for all external costs of investigating and settling claims and potential claims reported prior to the date of the statement of financial position. The provision is adjusted as additional information on the estimated amounts becomes known during the course of claims settlement. All changes in estimates are expensed in the current period. The Fund presents its claims on a discounted basis.

#### **Reinsurance**

The Fund reflects reinsurance balances on the statement of financial position on a gross basis to indicate the extent of credit risk related to reinsurance and its obligations to policy holders, and on a net basis on the statement of revenue and expenses to indicate the results of its retention of assessments retained.

#### **Revenue recognition**

The Fund follows the deferral method of accounting for annual assessments. Assessments are billed and received in advance on a calendar-year basis. Accordingly, assessments for the next fiscal year received prior to December 31 have been recorded as deferred revenue for financial reporting purposes and will be recognized as revenue in the next calendar year.

All other revenues are recognized when receivable if the amount to be received can be reasonably estimated and collection is reasonably assured.

#### **Use of estimates**

The preparation of financial statements in conformity with ASNPO requires management to make estimates and assumptions which affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses for the period reported. The determination of the provision for claims and ULAE and the reinsurers' share of the provision for claims, and the fair value of the investment property, involves significant estimation. Actual results could differ from those estimates and the differences could be material.

#### **Financial instruments**

The Fund's financial instruments consist of cash, accounts receivable, short-term investments, investments, and accounts payable and accrued liabilities.

The significant financial risks to which the Fund is exposed are credit risk, market risk, price risk, and liquidity risk.

#### **Credit risk**

Cash, accounts receivable, reinsurers' share of provision for claims, members' share of provision for claims and bond pooled funds indirectly expose the Fund to credit risk.

The maximum exposure to credit risk arising from the above-noted items is \$64,466,939 (2011 - \$66,326,275).

Credit risk arises from the possibility that a counterparty to an instrument fails to meet its obligations.

The investment guidelines mitigate credit risk by ensuring the investments in the bond pooled funds have an adequate minimum credit rating and well-diversified portfolios.

**Market risk**

Market risk is the potential for loss to the Fund from changes in the value of its financial instruments due to changes in interest rates, foreign exchange rates or equity prices.

The Fund manages market risk by diversifying investments within the various asset classes and investing in pooled funds as set out in the guidelines of the Society's statement of investment policies and procedures.

**Price risk**

Price risk is the risk that the fair value of the Society's investments will fluctuate due to changes in the market prices whether these changes are caused by factors specific to the individual financial instrument, its issuer, or factors affecting all similar financial instruments traded in the market. It arises primarily on pooled equity and bond fund investments.

To manage price risk, the Society has guidelines on the diversification and weighting of investments within pooled funds which are set and monitored against the Society's statement of investment policies and procedures.

As at December 31, 2012, if pooled fund prices increased or decreased by 10% with all other factors remaining constant, net assets would have increased or decreased by approximately \$9.7 million (2011 - \$9.1 million).

**Liquidity risk**

Liquidity risk is the risk that the Fund will not be able to meet all cash outflow requirements. At December 31, 2012, the sum of the Fund's cash, short-term investments and pooled fund investments, at fair value, which are available to settle the liabilities of the Society as they come due, exceeded the sum of the liabilities by \$31.6 million, or 36% (2011 - \$24.3 million, or 27%).

**4. Government remittances**

The following government remittances are included in accounts receivable and accounts payable:

	December 31, 2012 \$	December 31, 2011 \$	January 1, 2011 \$
Receiver General - HST	(243,096)	381,942	368,646
Receiver General - corporate income tax	1,665	551	5,453
Ministry of Finance - premium tax	13,184	13,448	13,441
Ministry of Finance and Corporate Relations	-	47	-
	<u>(228,247)</u>	<u>395,988</u>	<u>387,540</u>
(Receivable) payable			

**5. Short-term investments**

Short-term investments comprise pooled money market funds with the following balances:

	December 31, 2012 \$	December 31, 2011 \$	January 1, 2011 \$
Money market funds	<u>19,355,051</u>	<u>18,585,598</u>	<u>18,727,783</u>

**6. Investments**

	December 31, 2012 \$	December 31, 2011 \$	January 1, 2011 \$
Investments - at fair value	96,986,896	90,831,371	95,745,177

750 Cambie Street Building	11,586,190	12,063,864	12,541,539
	<u>108,573,086</u>	<u>102,895,235</u>	<u>108,286,716</u>

**December 31, 2012**

	Carrying cost \$	Gross unrealized gains \$	Gross unrealized losses \$	Estimated fair value \$
Bonds				
Pooled Funds	39,286,570	370,475	-	39,657,045
Equities				
Canadian Pooled Funds	16,873,326	6,340,285	-	23,213,611
International Pooled Funds	27,681,994	6,434,246	-	34,116,240
	<u>44,555,320</u>	<u>12,774,531</u>	<u>-</u>	<u>57,329,851</u>
	<u>83,841,890</u>	<u>13,145,006</u>	<u>-</u>	<u>96,986,896</u>

The effective yield on the investment portfolio was 2.50% (2011 - 2.68%).

**December 31, 2011**

	Carrying cost \$	Gross unrealized gains \$	Gross unrealized losses \$	Estimated fair value \$
Bonds				
Pooled Funds	39,919,715	238,242	-	40,157,957
Equities				
Canadian Pooled Funds	16,308,369	4,850,942	-	21,159,311
International Pooled Funds	27,336,421	2,177,682	-	29,514,103
	<u>43,644,790</u>	<u>7,028,624</u>	<u>-</u>	<u>50,673,414</u>
	<u>83,564,505</u>	<u>7,266,866</u>	<u>-</u>	<u>90,831,371</u>

January 1, 2011

	Carrying cost \$	Gross unrealized gains \$	Gross unrealized losses \$	Estimated fair value \$
Bonds				
Pooled Funds	37,676,943	3,437,687	-	41,114,630
Equities				
Canadian Pooled Funds	15,575,500	8,685,762	-	24,261,262
International Pooled Funds	23,754,070	6,615,215	-	30,369,285
	39,329,570	15,300,977	-	54,630,547
	77,006,513	18,738,664	-	95,745,177

#### Investment risk management

The Society has adopted policies which establish the guidelines for all investment activities. These guidelines apply to the investment funds owned and controlled by the Fund.

The Society's overall investment philosophy is to maximize the long-term real rate of return subject to an acceptable degree of risk.

The Society's long-term funding requirements and relatively low level of liquidity dictate a moderate portfolio with a mix of fixed income and equity securities. The Society invests in bonds and equities through pooled funds.

#### Investment income

	2012 \$	2011 \$
Interest on cash	4,850	198
Pooled distributions	2,608,794	2,883,750
Net interfund loan interest expense (note 7)	(163,307)	(146,213)
Building income - 750 Cambie Street (revenue of \$1,648,537; net of expenses of \$1,369,666)	278,871	344,715
Investment income	2,729,208	3,082,450

#### Fair value changes in investments

	2012 \$	2011 \$
Realized gain on disposal of investments	338,197	9,666,685
Realized gain on disposal of short-term investments	-	92,282
Unrealized gain (loss) on investments measured at fair value	5,878,139	(11,471,797)
Fair value changes in investments	6,216,336	(1,712,830)

**750 Cambie Street Building**

In 2004, a building at 750 Cambie Street was purchased as an investment for the Fund.

	December 31, 2012			December 31, 2011	
	Cost \$	Accumulated amortization \$	Net \$	Net \$	Net \$
Land	4,299,850	-	4,299,850	4,299,850	4,299,850
Building	4,971,376	1,066,542	3,904,834	4,030,797	4,156,759
Base building improvements	3,219,651	654,642	2,565,009	2,647,739	2,730,468
Tenant improvements	2,314,520	1,613,484	701,036	931,532	1,162,028
Deferred tenant inducements	408,705	293,244	115,461	153,947	192,434
	<u>15,214,102</u>	<u>3,627,912</u>	<u>11,586,190</u>	<u>12,063,865</u>	<u>12,541,539</u>

**7. General Fund building loan**

In 1992, the Benchers authorized the lending of monies from the Fund to support the capital development of the Society's buildings at 845 Cambie Street, Vancouver, B.C. The loan is secured by the building, has no fixed repayment terms and bears interest calculated monthly at a rate equal to the stated monthly bond yield to maturity earned on the Fund's investment portfolio. It is the intention of the Benchers to require the General Fund to repay a minimum of \$500,000 of the principal each year. During 2012, principal of \$500,000 (2011 - \$500,000) was repaid.

	2012 %	2011 %
Weighted average rate of return	<u>2.39</u>	<u>2.81</u>

**8. Provision for claims and unallocated loss adjustment expenses (ULAE)**

The changes in unpaid claims recorded in the consolidated statement of financial position are as follows:

	2012 \$	2011 \$
<b>Part A and Part C Insurance Coverage</b>		
Provision for claims - Beginning of year	54,043,143	57,145,957
Provision for losses and expenses for claims occurring in the current year	14,073,000	14,993,997
Decrease in estimated losses and expenses for losses occurring in prior years	<u>(3,223,607)</u>	<u>(3,628,000)</u>
Provision for claims liability	<u>64,892,536</u>	<u>68,511,954</u>
Less:		
Payments on claims incurred in the current year	(435,172)	(2,299,008)
Payments on claims incurred in prior years	(13,004,583)	(12,040,278)
Recoveries on claims	864,702	145,803
Change in reinsurers' share of recovery of claims	(423,000)	(402,000)
Change in due from members	<u>(138,014)</u>	<u>126,672</u>
Claim payments - net of recoveries	<u>(13,136,067)</u>	<u>(14,468,811)</u>
Provision for claims - End of year	<u>51,756,469</u>	<u>54,043,143</u>
<b>Part B Insurance Coverage</b>	<u>295,859</u>	<u>487,346</u>
<b>Total provision for Parts A, B and C Insurance Coverage</b>	<u>52,052,328</u>	<u>54,530,489</u>

The determination of the provision for unpaid claims and adjustment expenses and the related reinsurers' share requires the estimation of three major variables or quanta, being development of claims, reinsurance recoveries and the effects of discounting, to establish a best estimate of the value of the respective liability or asset.

The provision for unpaid claims and adjustment expenses and related reinsurers' share is an estimate subject to variability, and the variability, as with any insurance company, could be material in the near term. The variability arises because all events affecting the ultimate settlement of claims have not taken place and may not take place for some time. Variability can be caused by receipt of additional claim information, changes in judicial interpretation of contracts, significant changes in severity of claims from historical trends, the timing of claims payments, the recoverability of reinsurance, and future rates of investment return. The estimates are principally based on the Fund's historical experience. Methods of estimation have been used that the Society believes produce reasonable results given current information.

The provision for ULAE is an actuarially determined estimate of the Fund's future costs relating to the administration of claims and potential claims reported up to the statement of financial position date.

The Fund discounts its best estimate of claims provisions at a rate of interest of 4.23% (2011 - 4.22%). The Fund determines the discount rate based upon the expected return on its investment portfolio of assets with appropriate assumptions for interest rates relating to reinvestment of maturing investments.

A 1% increase in the discount rate will have a favourable impact on the claims liability of \$1.805 million (December 31, 2011 - \$2.045 million; January 1, 2011 - \$2.254 million) and a 1% decrease in the discount rate will have an unfavourable impact on the claims liability of \$1.938 million (December 31, 2011 - \$2.212 million; January 1, 2011 - \$2.433 million).

To recognize the uncertainty in establishing these best estimates, to allow for possible deterioration in experience, and to provide greater comfort that the actuarial liabilities are adequate to pay future benefits, the Fund includes a Provision for Adverse Deviations (PFAD) in some assumptions relating to claims development, reinsurance recoveries and future investment income. The PFAD is selected based on guidance from the Canadian Institute of Actuaries.

The effects of discounting and the application of PFAD are as follows (in thousands of dollars):

	2012 \$	2011 \$
Undiscounted	55,090	57,799
Effect of present value	(7,133)	(8,045)
PFADs	10,157	10,187
Discounted	58,114	59,941

Claims development tables

A review of the historical development of the Fund's insurance estimates provides a measure of the Fund's ability to estimate the ultimate value of claims. The top half of the following tables illustrate how the Fund's estimate of total undiscounted claims 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 consolidated statements of financial position.

Part A insurance claims (in thousands of dollars)

Claims year	2003 \$	2004 \$	2005 \$	2006 \$	2007 \$	2008 \$	2009 \$	2010 \$	2011 \$	2012 \$	Total \$
Estimate of undiscounted ultimate claims costs											
At end of claims year	16,800	12,990	17,150	12,260	13,580	13,670	11,520	13,650	14,560	13,390	
One year later	12,880	9,360	14,730	12,770	14,980	13,230	11,310	12,990	13,550		
Two years later	11,410	9,450	12,470	11,530	15,250	13,470	11,500	12,610			
Three years later	10,390	9,430	11,080	9,960	14,940	13,360	13,470				
Four years later	10,050	9,350	10,500	9,650	14,820	13,170					
Five years later	9,080	8,760	10,320	8,960	14,610						
Six years later	7,980	9,370	9,910	8,560							
Seven years later	7,770	10,150	9,710								
Eight years later	7,370	10,050									
Nine years later	6,970										
Current estimate of cumulative claims	6,970	10,050	9,710	8,560	14,610	13,170	13,470	12,610	13,550	13,390	116,090
Cumulative payments to date	(5,992)	(9,168)	(8,011)	(6,792)	(12,139)	(9,656)	(9,571)	(5,857)	(4,368)	(429)	(71,983)
Undiscounted unpaid liability	978	882	1,699	1,768	2,471	3,514	3,899	6,753	9,182	12,961	44,107
Undiscounted unpaid liability in respect of 2002 and prior years											3,910
Undiscounted unallocated loss adjustment expense reserve											6,786
<b>Total undiscounted unpaid claims liability</b>											<b>54,803</b>
Discounting adjustment include Claim PFAD											3,014
<b>Total discounted unpaid claims liability</b>											<b>57,817</b>

## Part B insurance claims (in thousands of dollars)

Claims year	2004 \$	2005 \$	2006 \$	2007 \$	2008 \$	2009 \$	2010 \$	2011 \$	2012 \$	Total \$
Estimate of undiscounted ultimate claims costs										
At end of claims year	82	334	189	251	8	107	23	28	18	
One year later	65	134	229	250	7	196	19	24		
Two years later	64	109	222	274	9	197	22			
Three years later	39	12	221	322	9	197				
Four years later	1	15	279	353	9					
Five years later	1	16	297	375						
Six years later	1	16	336							
Seven years later	1	16								
Eight years later	1									
Nine years later										
Current estimate of cumulative claims	1	16	336	375	9	197	22	24	18	998
Cumulative payments to date	(1)	(16)	(336)	(121)	(9)	(197)	(22)	(10)	-	(712)
Undiscounted unpaid liability	-	-	-	254	-	-	-	14	18	286
Undiscounted unpaid loss adjustment expense reserve										-
<b>Total undiscounted unpaid claims liability</b>										<b>286</b>
Discounting adjustment include Claim PFAD										10
<b>Total discounted unpaid claims liability</b>										<b>296</b>

The expected maturity of the unpaid claims provision is analyzed below (undiscounted and gross of reinsurance):

(in thousands of dollars)	Less than one year \$	One to two years \$	Two to three years \$	Three to four years \$	Four to five years \$	Over five years \$	Total \$
December 31, 2012	13,565	10,410	7,796	4,738	4,177	14,404	55,090
December 31, 2011	13,103	10,609	7,195	5,564	4,563	17,142	58,176
January 1, 2011	13,867	10,671	7,878	5,800	4,989	19,208	62,413

## Role of the actuary

The actuary is appointed to fulfill reporting requirements pursuant to the Insurance (Captive Company) Act of B.C. With respect to preparation of these financial statements, the actuary is required to carry out a valuation of the Fund's policy liabilities and to provide an opinion regarding their appropriateness at the date of the statement of financial position. The factors and techniques used in the valuation are in accordance with accepted actuarial practice, applicable legislation and associated regulations. The scope of the valuation encompasses the policy liabilities as well as any other matter specified in any direction that may be made by the regulatory authorities. The policy liabilities consist of a provision for unpaid claims and adjustment expenses. In performing the valuation of the liabilities for these contingent future events, which are by their very nature inherently variable, the actuary makes assumptions as to future loss ratios, trends, reinsurance recoveries, expenses and other contingencies, taking into consideration the circumstances of the Fund and the nature of the insurance policies.

The valuation is based on projections for settlement of reported claims and claim adjustment expenses. It is certain that actual claims and claim adjustment expenses will not develop exactly as projected and may, in fact, vary significantly from the projections. Further, the projections make no provision for new classes of claims or claims categories not sufficiently recognized in the claims database.

The actuary relies on data and related information prepared by the Fund. The actuary also analyzes the Fund's assets for their ability to support the amount of policy liabilities.



**9. Interfund transactions**

The operations of the Fund, the General Fund and the Special Compensation Fund are administered by the management of the Society. Balances between the funds arise from transactions of an operating nature and are recorded at exchange amounts at the dates of the transactions. Surplus funds are invested in the Fund's investment portfolio.

Amounts due to and from the General Fund and the Special Compensation Fund are due on demand and have no fixed terms of repayment. The Fund has authorized a loan facility of up to \$1 million to the General Fund to fund capital expenditures in accordance with the 10-year capital plan. The Fund has also authorized a loan facility of up to \$8 million to the Special Compensation Fund. As of December 31, 2012, no amounts have been drawn on the facilities (2011 - \$nil).

Monthly interest on the Fund's net loan position with the General Fund and Special Compensation Fund is paid to the Fund at a rate equal to the stated monthly bond yield to maturity earned on the Fund's investment portfolio. The average bond yield for 2012 was 2.39% (2011 average rate - 2.81%). The Fund's net loan position of \$16,198,052 (2011 - \$15,180,985) includes the General Fund building loan, other operating balances with the General Fund and the loan with the Special Compensation Fund. This net loan position fluctuates during the year as amounts are transferred between the General Fund, the Special Compensation Fund and the Fund to finance ongoing operations.

During 2012, interest revenue of \$110,293 was received on the General Fund building loan and interest of \$245,839 was paid on General Fund cash balances held by the Fund and \$27,760 was paid on the Special Compensation Fund cash balances held by the Fund for a net interest expense of \$163,306.

During 2011, interest revenue of \$143,709 was received on the General Fund building loan and interest of \$263,604 was paid on General Fund cash balances held by the Fund and \$26,318 was paid on the Special Compensation Fund cash balances held by the Fund for a net interest expense of \$146,213.

Other interfund transactions are disclosed elsewhere in these consolidated financial statements.

**10. Internally restricted net assets**

The Benchers have allocated \$17,500,000 (2011 - \$17,500,000) of the net assets to the Part B defalcation coverage.

**11. Regulatory requirements and capital management**

The Captive is required to maintain a minimum of \$200,000 in shareholder's equity and \$100,000 in reserves under the regulations of the Insurance (Captive Company) Act of B.C. The Captive was in compliance with these regulations throughout the year and as at December 31, 2012.

**12. Related parties**

The elected Benchers include members drawn from law firms across the province. These law firms may at times be engaged by the Society in the normal course of business. During the year ended December 31, 2012, expenses of \$101,190 (2011 - \$332,818) were incurred by the Fund with these law firms.

**13. Contingencies**

During the 2011 year, a Tax Auditor for the Ministry of Finance informed the Captive that the Ministry contended that the annual assessments contributed by members to the Lawyers Insurance Fund constituted premiums payable to the Captive for purposes of the Insurance Premium Tax Act and that the Ministry proposed to adjust the Captive's net taxable premiums from 2005 to 2009 to reflect this. The proposed additional tax was \$2 million. The Captive maintains that it is liable for premium tax only on amounts received by it from the Lawyers Insurance Fund as a reimbursement of reinsurance premiums and general and administrative costs. That premium tax has been paid in full. The Captive has disputed the Ministry's proposal and the Ministry of Finance has taken no further action to date. The Captive has accounted for this matter using the contingent liability method, whereby a provision is established only when it is considered likely that a liability will be incurred. Management considers that the outcome of this matter is not determinable at this time and therefore no provision has been established. If any amounts become due, the Lawyers Insurance Fund will reimburse the Captive.