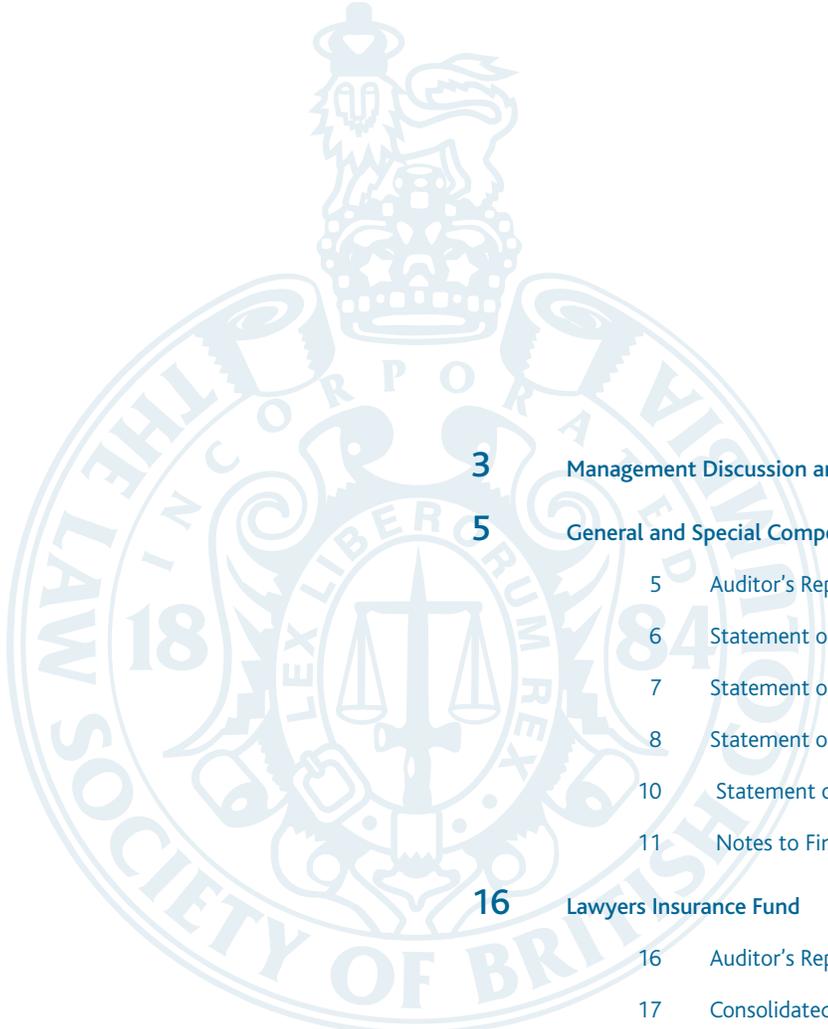




THE LAW SOCIETY OF BRITISH COLUMBIA

Financial Statements

December 31, 2011



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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 2011 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 2011, 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 Lawyers Insurance Funds
- 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 2012 practice fees and assessments, and reviewing corresponding budgets

### General Fund

#### Overview

Revenue for the year was just over \$1 million higher than 2010, while expenses for the year also increased due to higher than expected external counsel costs and additional expenses authorized by the Benchers in 2011 relating to the implementation of a new regulatory department plan and costs associated with the establishment of the new hearing panel structure. Despite the increased expenses, net income for the year was \$420,000 and net assets increased to \$7.1 million.

#### Revenues

General Fund revenue was \$21.5 million, \$1,066,000 more than 2010 due largely to continued growth in the number of lawyers and an increase in the practice fee. During 2011, net growth in the number of practising lawyers was 2% resulting in a total of 10,564 practising lawyers for the year. The increase in the practice fee covered additional operating expenses, including the transferred costs arising from a decision by the Benchers in November 2009 to fund the Forensic Accounting program through the practice fee rather than the Trust Administration Fee. Professional Legal Training Course (PLTC) enrolment revenue was as expected, with approximately 385 PLTC students attending during the year. Late penalties relating to Continuing Professional Development resulted in \$125,000 of additional revenue. E-filing revenue increased \$119,000 from 2010 due to greater participation in the land title e-filing initiative, likely in anticipation of the implementation of required e-filing in early 2012.

Offsetting these increases was a decline of \$64,000 in investment income on General Fund balances invested during the year due to the lower prevailing market interest rates. There was also a slight decline in trust administration fee revenue of \$50,000 compared to 2010. Application fees also decreased slightly over 2010 due to a decline in the number of members transferring to BC from other locations.

The Special Compensation Fund and the Lawyers Insurance Fund contributed \$2.22 million for co-sponsored programs and for general program and administrative expenses attributable to their operations.

The net operating revenue from the Law Society building at 845 Cambie Street increased by \$160,000 to \$386,000, due to a market-based increase in the internal allocation of rent to Law Society departments, which was partially offset by an increase in building maintenance costs and property taxes.

#### Expenses

The 2011 General Fund expenses were \$23.7 million, compared to \$21.6 million in 2010. The increase cost was attributable to enhancements to our regulatory programs and functions, including increased staff support for the professional conduct and discipline departments and the introduction of non-Bencher and non-lawyers as members of hearing panels, along with market-based salary adjustments.

Regulatory programs saw the most significant increase year over year, as a result of a greater focus on the timeliness and effectiveness of our discipline processes. The Benchers approved a regulatory department plan, implemented in 2011, which is intended to improve the effectiveness and efficiency of the regulatory process. Changes were made to the structure of our complaints and investigations areas to help reduce complaint resolution time and enhance investigations and disciplinary actions. A number of staff were added to ensure these changes were implemented. Other improvements were made, such as a greater focus on early resolution of complaints, greater use of interviews and introduction of new Conduct Assessment and Discipline Guidelines. A number of complaint files were sent to external counsel to ensure they were dealt with in a timely manner, which resulted in higher external counsel fees. Forensic accounting costs also increased due to a number of complex forensic investigation files during the year. As detailed in [The 2011 Law Society Report on Performance](#), the higher complainant satisfaction with the timeliness of complaints handling suggests that the changes are working along with the lowest number of open complaints at year end in ten years. The increase in costs was offset somewhat by a decrease in Discipline department external counsel fees as, with the addition of another staff discipline counsel, more files were dealt with by staff.

Policy and Legal Services expenses were also higher in 2011 due to the recruitment, travel and training costs for the non-Bencher lawyers and members of the public who are now sitting as hearing panel members. Unauthorized practice costs were also higher due to a staff position vacancy being filled in 2011. These increases were offset by a reduction in expenditures for litigation and intervention files.

Additional information services costs were incurred in moving Law Society computer servers offsite to improve security and availability and reduce future capital costs, in addition to the transfer of a staff member from another Law Society department. The increases were offset somewhat by the provision of the Annual Report on Performance and Financial Statements solely in electronic form, which resulted in significant savings in printing costs over 2010.

Education and Practice expenses increased due to the addition of one staff position to support the Continuing Professional Development program, as well as PLTC contractor costs to provide coverage during an employee disability leave. There was also a fairly significant increase in the use of the member assistance program by lawyers during the year.

General and Administrative department costs increased due to a change in the internal rent allocation and market-based staff salary increases, along with additional costs related to recruiting professional regulation staff.

Benchers Governance expenses were lower as a result of reduced travel costs during the year. These savings were offset by an increase in the contributions to the Federation of Law Societies of Canada, CanLII and Pro Bono.

### Net Assets

Overall, the General Fund remains financially sound. As of December 31, 2011, net assets in the General fund were \$7.1 million, which includes \$1.9 million allocated for planned capital expenditures, which include the implementation of an electronic document and records management system and capital projects for the 845 Cambie building.

## Special Compensation Fund

### Overview

The Special Compensation Fund had minimal activity during the 2011 year.

### Revenues

The Special Compensation Fund was funded through a \$5 assessment from each practising lawyer, resulting in total revenue of \$53,000. The assessment was used to pay the administrative costs of the Fund.

### 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 \$71,000 were incurred, offset by \$93,000 in cost recoveries and \$26,000 in interest income.

### Net Assets

At the end of 2011, the Special Compensation Fund net assets were \$932,000. Due to the discretionary nature of the Special Compensation Fund, the Law Society does not set a claims reserve. All claim expenses are shown as an expense in the year incurred, net of any recoveries from the insurer or the lawyer against whom the claim is made. As at December 31, 2011, there were eleven claims for a total of \$783,000 for which statutory declarations have been received and which are expected to be reviewed by the Special Compensation Fund committee in due course.

## Lawyers Insurance Fund

### Overview

Overall, the Lawyers Insurance Fund remained in a healthy financial position relative to the previous year. Investment returns were slightly less than our benchmark which was offset somewhat by a lower actuarial estimate for prior year's losses.

### Revenues

The insurance assessment was \$1,750 per insured member in 2011, resulting in total revenue of \$13.4 million, compared to \$12.1 million in 2010. During 2011, the long-term investment portfolio earned a return of 1.3%, compared to a benchmark return of 1.6%. In the year, the value of the investment portfolio increased by \$1.1 million, which has been recognized through the statement of revenue and expenses and the statement of changes in net assets and reflected on the balance sheet.

### Expenses

LIF general operating costs (excluding claims payments and ULAE) for 2011 were \$4.9 million, compared to \$4.5 million in 2010. This increase reflects market-based salary increases, increased investment management fees as a result of the growth in the investment portfolio and an increased contribution to the program and administrative costs of the General Fund.

The 2011 actuarial provision for settlement of claims was \$11.0 million, a decrease of \$1.4 million over 2010. The provision for claims on the balance sheet at the end of 2011 was \$54.5 million, compared to \$57.6 million in 2010.

### Net Assets

As of December 31, 2011, the LIF net assets were \$44.3 million, a decrease of \$1.2 million from 2010.



May 8, 2012

## **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 statement of financial position as at December 31, 2011 and the statements of changes in net assets, revenue and expenses, and cash flows for the year then ended, 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 generally accepted accounting principles, 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 audit. We conducted our audit 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 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, 2011 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

*PricewaterhouseCoopers LLP*

**Chartered Accountants**

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

Statement of Financial Position  
As at December 31, 2011

	2011		2010	
	General Fund \$	Special Compensation Fund \$	Total \$	Total \$
<b>Assets</b>				
<b>Current assets</b>				
Cash	279,155	500	279,655	177,871
Unclaimed trust funds (note 2)	1,847,851	-	1,847,851	1,681,796
Accounts receivable and prepaid expenses (note 3)	1,129,062	-	1,129,062	1,242,948
B.C. Courthouse Library Fund (note 2)	677,718	-	677,718	635,094
Due from Lawyers Insurance Fund (notes 5 and 9)	19,331,087	949,898	20,280,985	18,472,549
	23,264,873	950,398	24,215,271	22,210,258
<b>Non-current assets</b>				
Cambie Street property - net (note 4)	11,739,231	-	11,739,231	12,002,361
Other property and equipment - net (note 4)	1,021,642	-	1,021,642	1,035,279
Intangible assets - net (note 4)	340,826	-	340,826	336,950
	36,366,572	950,398	37,316,970	35,584,848
<b>Liabilities</b>				
<b>Current liabilities</b>				
Accounts payable and accrued liabilities	4,038,520	8,195	4,046,715	3,978,948
Liability for unclaimed trust funds (note 2)	1,847,851	-	1,847,851	1,681,796
Current portion of building loan payable (note 8)	500,000	-	500,000	500,000
Claims payable (note 10)	-	-	-	-
Deferred revenue (notes 2 and 5)	17,491,097	10,450	17,501,547	16,065,782
Deferred capital contributions (notes 2 and 6)	69,751	-	69,751	81,129
B.C. Courthouse Library Grant (note 2)	677,718	-	677,718	635,094
Deposits	29,399	-	29,399	19,700
	24,654,336	18,645	24,672,981	22,962,449
<b>Building loan payable</b> (notes 8 and 9)	4,600,000	-	4,600,000	5,100,000
	29,254,336	18,645	29,272,981	28,062,449
<b>Net assets</b>				
Unrestricted	7,112,236	931,753	8,043,989	7,522,399
	36,366,572	950,398	37,316,970	35,584,848

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

Statement of Changes in Net Assets  
For the year ended December 31, 2011

	2011		2010	
	General Fund - Unrestricted \$	Special Compensation Fund - Unrestricted \$	Total \$	Total \$
<b>Net assets - Beginning of year</b>	6,692,044	830,355	7,522,399	5,939,237
Net excess of revenue over expenses for the year	420,192	101,398	521,590	1,583,162
<b>Net assets - End of year (note 7)</b>	<u>7,112,236</u>	<u>931,753</u>	<u>8,043,989</u>	<u>7,522,399</u>

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

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

Statement of Revenue and Expenses  
For the year ended December 31, 2011

	2011		2010	
	General Fund \$	Special Compensation Fund \$	Total \$	Total \$
<b>Revenue</b>				
Practice fees	15,956,108	-	15,956,108	14,792,133
Annual assessments	-	53,377	53,377	525,651
Trust administration fees	2,315,568	-	2,315,568	2,364,862
Enrolment fees	965,542	-	965,542	1,010,802
Interest and other income (note 9)	779,865	-	779,865	844,237
E-filing revenue	725,546	-	725,546	606,931
Fines and penalties	393,018	-	393,018	424,287
Application fees	400,040	-	400,040	426,005
	<u>21,535,687</u>	<u>53,377</u>	<u>21,589,064</u>	<u>20,994,908</u>
<b>Expenses</b>				
Bencher Governance				
Bencher, AGM and other committees	1,019,072	-	1,019,072	1,032,908
Federation of Law Societies' contribution	215,753	-	215,753	209,167
CanLII's contribution	366,792	-	366,792	316,714
Pro Bono contribution	157,900	-	157,900	139,993
Communication and Information Services				
Communications and publications	1,037,341	-	1,037,341	1,043,320
Information services	1,291,539	-	1,291,539	1,097,960
Education and Practice				
Credentials	380,460	-	380,460	405,157
Ethics	107,457	-	107,457	102,553
Member services	682,322	-	682,322	621,645
Membership assistance programs	189,860	-	189,860	153,038
Practice advice	528,878	-	528,878	473,355
Practice standards	541,855	-	541,855	549,615
Professional Legal Training Course and Education	1,890,182	-	1,890,182	1,767,082
General and Administrative				
Accounting	792,519	-	792,519	706,513
Amortization of other property and equipment	426,333	-	426,333	474,768
General administration	1,587,268	-	1,587,268	1,557,229
Human resources	860,759	-	860,759	682,492
Records management and library	285,809	-	285,809	244,298
Policy and Legal Services				
Policy and tribunal counsel	1,392,808	-	1,392,808	1,165,877
External litigation and interventions	164,872	-	164,872	272,743
Unauthorized practice	318,006	-	318,006	236,224
Regulation				
Custodianship costs	1,371,615	-	1,371,615	1,296,781
Discipline	1,131,044	-	1,131,044	1,159,548
Professional conduct - intake and investigations	4,106,300	-	4,106,300	3,267,930
Forensic accounting	948,353	-	948,353	751,450
Trust assurance	1,930,828	-	1,930,828	1,894,716
	<u>23,725,925</u>	<u>-</u>	<u>23,725,925</u>	<u>21,623,076</u>
Carried forward				

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

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

Statement of Revenue and Expenses ...continued  
For the year ended December 31, 2011

	2011		2010	
	General Fund \$	Special Compensation Fund \$	Total \$	Total \$
Brought forward	23,725,925	-	23,725,925	21,623,076
<b>Special Compensation Fund</b>				
Claims and costs (note 10)	-	(93,100)	(93,100)	(48,974)
General and administrative costs	-	71,397	71,397	141,647
Loan interest income from Lawyers Insurance Fund (note 9)	-	(26,318)	(26,318)	(33,126)
	23,725,925	(48,021)	23,677,904	21,682,623
<b>Costs recovered from Special Compensation and Lawyers Insurance Funds</b>				
Co-sponsored program costs	(717,773)	-	(717,773)	(625,768)
Program and administrative costs	(1,506,600)	-	(1,506,600)	(1,418,734)
	21,501,552	(48,021)	21,453,531	19,638,121
<b>Excess of revenue over expenses before the following</b>	34,135	101,398	135,533	1,356,787
<b>845 Cambie net results</b>				
Rental revenue	418,113	-	418,113	478,807
Allocated rental revenue (note 2)	1,732,329	-	1,732,329	1,366,208
	2,150,442	-	2,150,442	1,845,015
<b>Expenses</b>				
Amortization	546,908	-	546,908	489,164
Insurance	66,027	-	66,027	78,322
Loan interest expense (note 8)	143,709	-	143,709	181,674
Property management	198,479	-	198,479	226,793
Property taxes	430,332	-	430,332	409,713
Repair and maintenance	553,124	-	553,124	464,453
Utilities	142,865	-	142,865	132,403
Recovery from tenants	(317,059)	-	(317,059)	(363,882)
	1,764,385	-	1,764,385	1,618,640
<b>Net 845 Cambie operating revenue</b>	386,057	-	386,057	226,375
<b>Net excess of revenue over expenses for the year</b>	420,192	101,398	521,590	1,583,162

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

## Statement of Cash Flows

For the year ended December 31, 2011

	2011		2010	
	General Fund \$	Special Compensation Fund \$	Total \$	Total \$
<b>Cash flows from operating activities</b>				
Net excess of revenue over expenses for the year	420,192	101,398	521,590	1,583,162
Items not affecting cash				
Amortization of Cambie Street building and tenant improvements	546,908	-	546,908	489,164
Amortization of other property and equipment	332,144	-	332,144	349,738
Amortization of intangible assets	94,189	-	94,189	125,030
Amortization of deferred capital contributions	(11,378)	-	(11,378)	(11,379)
Loss on disposal of capital assets	8,529	-	8,529	43,324
	1,390,584	101,398	1,491,982	2,579,039
Decrease (increase) in current assets				
Unclaimed trust funds	(166,055)	-	(166,055)	(242,223)
Accounts receivable and prepaid expenses	113,886	-	113,886	(186,864)
B.C. Courthouse Library Fund	(42,624)	-	(42,624)	88,573
Increase (decrease) in current liabilities				
Accounts payable and accrued liabilities	75,518	(5,552)	69,966	(310,686)
Liability for unclaimed trust funds	166,055	-	166,055	242,223
Deferred revenue	1,476,661	(40,896)	1,435,765	879,010
B.C. Courthouse Library Grant	42,624	-	42,624	(88,573)
Deposits	7,500	-	7,500	4,700
Decrease in claims payable	-	-	-	(1,885,882)
	3,064,149	54,950	3,119,099	1,079,317
<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, equipment and intangible asset additions	(708,879)	-	(708,879)	(1,057,000)
<b>Interfund transfers</b>	(1,753,486)	(54,950)	(1,808,436)	652,474
<b>Increase (decrease) in cash</b>	101,784	-	101,784	174,791
<b>Cash - Beginning of year</b>	177,371	500	177,871	3,080
<b>Cash - End of year</b>	279,155	500	279,655	177,871
<b>Supplementary cash flow information</b>				
Interest paid	143,709	-	143,709	181,674
Interest income received	336,127	26,318	362,445	348,162

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. The 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. Significant accounting policies

These financial statements are prepared in accordance with Canadian generally accepted accounting principles.

### 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 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 prepaid expenses, and accounts payable and accrued liabilities correspond to their carrying values due to their short-term nature.

The carrying values of the building loan payable and other balances with related parties approximate fair values based upon the interest rate applied.

### Financial instruments

The Society's financial instruments consist of cash, accounts receivable and accounts payable. Financial instruments are initially recognized at fair value with subsequent measurement depending on classification as described below. Classification of financial instruments depends on the purpose for which the financial instruments were acquired or issued, their characteristics, and the Society's designation of such instruments.

The Society has made the following classifications for its financial instruments:

- Cash is classified as assets held for trading and is measured at fair value at the end of each period with any resulting gains or losses recognized in operations;
- Accounts receivable are classified as receivables and loans and are recorded at amortized cost using the effective interest rate method, which upon their initial measurement is equal to their fair value. Subsequent measurement of trade receivables is at amortized cost, which usually corresponds to the amount initially recorded less any allowance for doubtful accounts;
- Accounts payable and other liabilities are classified as other financial liabilities and are measured at amortized cost using the effective interest rate method.

#### 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	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 a corresponding liability for unclaimed trust funds 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 Canadian generally accepted accounting principles 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.

#### Comparative figures

Certain comparative figures in these statements have been reclassified to conform to the current year's presentation.

### 3. Accounts receivable

Accounts receivable are presented net of the allowance for doubtful accounts of \$629,727 (2010 - \$661,115).

4. Property, equipment and intangible assets

a) 845 Cambie Street property

	2011			2010	
	Cost \$	Accumulated amortization \$	Net \$	Net \$	
Land	4,189,450	-	4,189,450	4,189,450	
Buildings	12,010,577	5,705,653	6,304,924	6,688,392	
Leasehold improvements	5,708,696	4,465,705	1,242,991	1,121,091	
Tenant improvements	989,565	987,699	1,866	3,428	
	<u>22,898,288</u>	<u>11,159,057</u>	<u>11,739,231</u>	<u>12,002,361</u>	

b) Other property and equipment

	2011			2010	
	Cost \$	Accumulated amortization \$	Net \$	Net \$	
Furniture and fixtures	2,441,025	1,731,594	709,431	689,224	
Computer hardware	1,214,322	902,112	312,210	346,054	
Law libraries - at nominal value	1	-	1	1	
	<u>3,655,348</u>	<u>2,633,706</u>	<u>1,021,642</u>	<u>1,035,279</u>	

c) Intangible assets

	2011			2010	
	Cost \$	Accumulated amortization \$	Net \$	Net \$	
Computer software	<u>805,792</u>	<u>464,966</u>	<u>340,826</u>	<u>336,950</u>	

In 2011, intangible assets, consisting entirely of computer software, with an aggregate amount of \$98,066 (2010 - \$64,065) was purchased.

5. Deferred revenue

As at December 31, 2011, fees and assessments of \$17.5 million (2010 - \$16.1 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.

6. 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:

	2011	2010
	\$	\$
Balance - Beginning of year	81,129	92,508
Less: Amortization for the year	<u>(11,378)</u>	<u>(11,379)</u>
Balance - End of year	<u>69,751</u>	<u>81,129</u>

**7. Unrestricted net assets**

The General Fund unrestricted net assets include \$238,835 (2010 - \$221,683) which has been appropriated for contribution to future trust administration fee related expenses. During the year, \$2.3 million (2010 - \$2.4 million) in trust administration fee revenue was collected, and \$2.3 million (2010 - \$2.3 million) in trust administration fee expenses were incurred.

The General Fund unrestricted net assets also include \$1,870,561 (2010 - \$1,220,052) which has been allocated to capital expenditures in accordance with the capital plan.

**8. 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 9. The outstanding building loan balance at the end of the 2011 year is \$5.1 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 2011, principal of \$500,000 (2010 - \$500,000) was repaid.

	2011 %	2010 %
Weighted average rate of interest	2.81	3.23

**9. 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, 2011 (2010 - \$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, 2011 (2010 - \$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 2011 was 2.81% (2010 - average rate - 3.23%). 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 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.

During 2010, interest of \$181,674 was paid on the building loan and interest revenue of \$294,991 was received from General Fund cash balances held by the Lawyers Insurance Fund and \$33,126 was received from Special Compensation Fund cash balances held by the Lawyers Insurance Fund for a net interest income of \$146,443.

Other interfund transactions are disclosed elsewhere in these financial statements.

**10. Special Compensation Fund claims**

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, 2011, there were 11 claims amounting to approximately \$783,000 for which statutory declarations had been received. All claims for which statutory declarations are received will be reviewed by the Special Compensation Fund Committee in due course. These amounts are not recorded in the financial statements and do not include an estimate for claims attributable of which the Society is unaware.

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 10(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. Since then, the Society has continued to investigate the various claims attributed to Mr. Wirick's practice activities. Information continues to be received to assist in the investigation of claims. The Benchers are updated as required.

At December 31, 2011, there were eight claims still under consideration with total reported losses of \$696,000. These amounts have not been recorded in the financial statements.

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 2011, the Special Compensation Fund recovered \$94,100 (2010 - \$51,474) related to the Wirick case.

**11. 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, 2011, expenses of \$188,949 (2010 - \$176,968) were incurred by the General Fund during the normal course of business with these law firms.

**12. 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.

**13. Future accounting pronouncements**

In December 2010, the Canadian Institute of Chartered Accountants (CICA) in conjunction with the Accounting Standards Board (AcSB) issued new accounting standards for not-for-profit organizations. Going forward, private sector not-for-profit organizations will be required to adopt either Part I of the CICA Handbook - International Financial Reporting Standards (IFRS) or Part III of the CICA Handbook - Accounting Standards for Not-for-Profit Organizations.

The Society will be adopting Part III of the CICA Handbook - Accounting Standards for Not-for-Profit Organizations for its fiscal year ending December 31, 2012. The financial reporting impact of the transition is currently under review.



May 8, 2012

## **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, which comprise the consolidated statement of financial position as at December 31, 2011 and the consolidated statements of changes in net assets, revenue and expenses, and cash flows for the year then ended, 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 consolidated financial statements in accordance with Canadian generally accepted accounting principles, 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 audit. We conducted our audit 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 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 as at December 31, 2011 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

*PricewaterhouseCoopers LLP*

#### **Chartered Accountants**

*PricewaterhouseCoopers LLP, Chartered Accountants  
PricewaterhouseCoopers Place, 250 Howe Street, Suite 700, Vancouver, British Columbia, Canada V6C 3S7*

THE LAW SOCIETY OF BRITISH COLUMBIA – LAWYERS INSURANCE FUND

Consolidated Statement of Financial Position  
As at December 31, 2011

	2011 \$	2010 \$
<b>Assets</b>		
Cash	5,133,153	2,806,770
Accounts receivable	1,176,607	685,508
Prepaid expenses	25,272	115,962
Short-term investments (note 3)	18,585,598	18,727,783
Reinsurers' share of provision for claims (note 1)	423,000	825,000
Members' share of provision for claims	1,231,902	1,105,231
General Fund building loan (note 5)	5,100,000	5,600,000
Investments (note 4)	<u>102,895,235</u>	<u>108,286,716</u>
	<u>134,570,767</u>	<u>138,152,970</u>
<b>Liabilities</b>		
Accounts payable and accrued liabilities	1,614,420	2,339,524
Deferred revenue	6,812,979	6,706,891
Due to General Fund (note 7)	19,331,087	17,577,601
Due to Special Compensation Fund (note 7)	949,898	894,948
Provision for claims (note 6)	54,530,489	57,582,333
Provision for ULAE (note 6)	<u>7,065,000</u>	<u>7,618,000</u>
	<u>90,303,873</u>	<u>92,719,297</u>
<b>Net assets</b>		
Unrestricted net assets	26,766,894	27,933,673
Internally restricted net assets (note 8)	<u>17,500,000</u>	<u>17,500,000</u>
	<u>44,266,894</u>	<u>45,433,673</u>
	<u>134,570,767</u>	<u>138,152,970</u>
Commitments (note 7)		
Contingencies (note 11)		

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 Statement of Changes in Net Assets  
For the year ended December 31, 2011

	2011			2010
	Unrestricted \$	Internally restricted \$	Total \$	Total \$
<b>Net assets - Beginning of year</b>	<b>27,933,673</b>	<b>17,500,000</b>	<b>45,433,673</b>	<b>42,803,297</b>
<b>Excess (deficiency) of revenue over expenses for the year</b>	<b>10,305,018</b>	-	<b>10,305,018</b>	<b>(2,447,061)</b>
<b>Change in unrealized gains</b>				
Unrealized gains on available-for-sale financial assets arising during the year	1,078,638	-	1,078,638	7,359,380
Realized gain on distribution of Pooled fund income	(2,883,750)	-	(2,883,750)	(1,542,569)
Realized gain on disposal of investments recognized in the statement of revenue and expense	(9,666,685)	-	(9,666,685)	(739,374)
<b>Net (decrease) increase in unrealized gains on available-for-sale financial assets</b>	<b>(11,471,797)</b>	-	<b>(11,471,797)</b>	<b>5,077,437</b>
<b>Net assets - End of year</b>	<b>26,766,894</b>	<b>17,500,000</b>	<b>44,266,894</b>	<b>45,433,673</b>

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

THE LAW SOCIETY OF BRITISH COLUMBIA – LAWYERS INSURANCE FUND

Consolidated Statement of Revenue and Expenses  
For the year ended December 31, 2011

	2011 \$	2010 \$
<b>Revenue</b>		
Annual assessments	13,436,523	12,099,297
Investment income (note 4)	12,841,417	2,526,036
Other income	30,827	42,332
	<u>26,308,767</u>	<u>14,667,665</u>
<b>Insurance expenses</b>		
Actuary, consultant and investment manager fees	433,126	373,317
Allocated office rent from General Fund	148,280	116,164
Contribution to program and administrative costs of General Fund	1,515,668	1,423,207
Office	532,897	485,068
Premium taxes	13,448	13,441
Provision for settlement of claims (note 6)	10,960,438	12,394,950
Recovery of ULAE (note 6)	(553,000)	(455,000)
Salaries, wages and benefits	2,234,875	2,132,358
	<u>15,285,732</u>	<u>16,483,505</u>
<b>Loss prevention expenses</b>		
Contribution to co-sponsored program costs of General Fund	713,023	625,768
	<u>15,998,755</u>	<u>17,109,273</u>
<b>Excess (deficiency) of revenue over expenses before the following</b>	10,310,012	(2,441,608)
<b>Provision for current income taxes</b>	4,994	5,453
<b>Excess (deficiency) of revenue over expenses for the year</b>	<u>10,305,018</u>	<u>(2,447,061)</u>

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

Consolidated Statement of Cash Flows  
For the year ended December 31, 2011

	2011 \$	2010 \$
<b>Cash flows from operating activities</b>		
Excess (deficiency) of revenue over expenses for the year	10,305,018	(2,447,061)
Items not affecting cash		
Realized gain on disposal of investments	(9,666,685)	(739,374)
Amortization of 750 Cambie Street building	439,188	452,018
Amortization of deferred tenant inducement	38,486	25,659
	<u>1,116,007</u>	<u>(2,708,758)</u>
Decrease (increase) in assets		
Accounts receivable	(491,099)	(387,534)
Prepaid expenses	90,690	(65,843)
Short-term investments	142,185	(11,819)
Reinsurers' share of provision for claims	402,000	914,000
Members' share of provision for claims	(126,671)	115,492
Increase (decrease) in liabilities		
Accounts payable and accrued liabilities	(725,104)	649,525
Deferred revenue	106,088	705,647
Provision for claims	(3,051,844)	212,031
Provision for ULAE	(553,000)	(455,000)
	<u>(3,090,748)</u>	<u>(1,032,259)</u>
<b>Cash flows from investing activities</b>		
Purchase of investments	(44,702,858)	(1,541,474)
Proceeds from disposal of investments	47,811,553	3,675,700
Decrease in General Fund building loan	500,000	500,000
	<u>3,608,695</u>	<u>2,634,226</u>
<b>Cash flows from financing activities</b>		
Interfund transfers (note 7)	1,808,436	(652,474)
<b>Increase in cash</b>	2,326,383	949,493
<b>Cash - Beginning of year</b>	<u>2,806,770</u>	<u>1,857,277</u>
<b>Cash - End of year</b>	<u>5,133,153</u>	<u>2,806,770</u>
<b>Supplementary cash flow information</b>		
Interest paid	<u>289,925</u>	<u>328,117</u>
Interest income received	<u>143,907</u>	<u>216,702</u>

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.

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 barristers and solicitors and in relation to the provision of professional services.

The Society's members have current coverage as follows:

**Part A**

	\$	2011 \$
Deductible - member	5,000	or 10,000
The Fund	995,000	or 990,000
Total coverage per error or related errors		1,000,000
Annual aggregate 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. The Captive has not entered into reinsurance contracts for claims reported since January 1, 1997. All losses on claims since 1997 are fully reimbursed by the Fund on behalf of the Society under agreement.

**Part B**

For the 2011 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. This reinsurance attaches above a \$3,000,000 deductible and is re-insured such that amounts over the deductible are 80% covered by the reinsurer to a maximum of \$5,000,000, with the remaining 20% covered by the Fund.

**2. Significant accounting policies**

These financial statements are prepared in accordance with Canadian generally accepted accounting principles (GAAP).

**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 value due to their short-term nature.

The carrying values of the General Fund building loan receivable and other balances with related parties approximate fair values based upon the interest rate applied.

#### Short-term investments

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

#### Investments

The Fund has designated all of its bond and equity investments as available-for-sale investments and reports them at fair value. Changes in the fair value of available-for-sale investments are reported within the statement of changes in net assets, until the financial asset is disposed of or becomes other than temporarily impaired at which time the gain or loss is recognized in the statement of revenue and expenses. Investment transactions are recorded on a trade date basis and transaction costs are included in the determination of excess of revenue over expenses for the year.

The fair value of investments is market value. The market value of publicly traded investments is based on closing bid prices.

#### Investment income

Investment income is 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 Canadian GAAP 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 provisions for claims and unallocated loss adjustment expenses 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 and are initially recognized at fair value with subsequent measurement depending on classification as described below.

The Fund has made the following classifications for its financial instruments:

Cash is classified as assets held for trading and is measured at fair value

Accounts receivable are classified as loans and receivables and are recorded at amortized cost using the effective interest rate method. Initial measurement is equal to the fair value at the date of origin and subsequent measurement is at amortized cost, which usually corresponds to the amount initially recorded less any allowance for doubtful accounts.

Short-term investments are classified as available for trading and are carried at cost since their book value equals their fair market value

Long-term investments are classified as available for trading and are accounted for at fair value. Changes in fair value are recognized in the statement of revenue and expenses

Accounts payable and accrued liabilities are classified as other financial liabilities and are measured at amortized cost using the effective interest rate method

### Comparative figures

Comparative figures for accounts receivable, reinsurers share of provision for claims and members' share of provision for claims in these statements have been reclassified to conform to the current year's presentation.

### 3. Short-term investments

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

	2011 \$	2010 \$
Money market funds	18,585,598	18,727,783

### 4. Investments

	2011 \$	2010 \$
Investments - at fair value	90,831,371	95,745,177
750 Cambie Street Building	12,063,864	12,541,539
	<u>102,895,235</u>	<u>108,286,716</u>

	Carrying cost \$	Gross unrealized gains \$	Gross unrealized losses \$	2011 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>

The effective yield on the investment portfolio was 2.68% (2010 - 2.38%).

	2010			
	Carrying cost \$	Gross unrealized gains \$	Gross unrealized losses \$	Estimated fair value \$
<b>Bonds</b>				
Pooled Funds	37,676,943	3,437,687	-	41,114,630
<b>Equities</b>				
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.

#### Credit risk

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

The maximum exposure to credit risk arising from the above noted items is \$66,708,217 (2010 - \$65,264,922).

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's investment portfolio is classified as available for sale; therefore, changes in the fair value of investments are reported within the statement of changes in net assets, until realized or deemed to be other than temporary.

The Fund manages market risk by diversifying investments within the various asset classes 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 equity and pooled 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, 2011, if pooled fund prices increased or decreased by 10% with all other factors remaining constant, net assets would have increased or decreased by approximately \$9.1 million (2010 - \$9.6 million).

**Liquidity risk**

Liquidity risk is the risk that the Fund will not be able to meet all cash outflow requirements. At December 31, 2011, the sum of the Fund's cash, short-term investments and pooled fund investment, at fair value, which are available to settle the liabilities of the Society as they come due, exceeded the sum of the liabilities by \$24.3 million, or 27% (2010 - \$24.6 million, or 26%).

**Investment income**

	2011 \$	2010 \$
Interest on cash and cash equivalents	198	35,023
Pooled distributions	2,883,750	1,542,569
Net interfund loan interest expense (note 7)	(146,213)	(146,444)
Realized gain on disposal of investments	9,666,685	739,374
Realized gain on disposal of short-term investments	92,282	-
Building income - 750 Cambie Street (revenue of \$1,673,811; net of expenses of \$1,329,096)	344,715	355,514
	<u>12,841,417</u>	<u>2,526,036</u>
Net investment income		

**750 Cambie Street Building**

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

	2011		2010	
	Cost \$	Accumulated amortization \$	Net \$	Net \$
Land	4,299,850	-	4,299,850	4,299,850
Building	4,971,376	940,579	4,030,797	4,156,759
Base building improvements	3,219,651	571,912	2,647,739	2,730,468
Tenant improvements	2,314,520	1,382,988	931,532	1,162,028
Deferred tenant inducements	408,705	254,758	153,947	192,434
	<u>15,214,102</u>	<u>3,150,237</u>	<u>12,063,865</u>	<u>12,541,539</u>

**5. 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, 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 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 2011, principal of \$500,000 (2010 - \$500,000) was repaid.

	2011 %	2010 %
Weighted average rate of return	<u>2.81</u>	<u>3.23</u>

**6. 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:

	2011 \$	2010 \$
<b>Part A Insurance Coverage</b>		
Provision for claims - Beginning of year	57,145,957	56,873,478
Provision for losses and expenses for claims occurring in the current year	14,993,997	14,033,000
Decrease in estimated losses and expenses for losses occurring in prior years	<u>(3,628,000)</u>	<u>(1,848,000)</u>
Provision for claims liability	<u>68,511,954</u>	<u>69,058,478</u>
Less:		
Payments on claims incurred in the current year	(2,299,008)	(813,336)
Payments on claims incurred in prior years	(12,040,278)	(10,260,200)
Recoveries on claims	145,803	130,450
Change in reinsurers' share of recovery of claims	(402,000)	(880,000)
Change in due from members	<u>126,672</u>	<u>(89,435)</u>
Claim payments - net of recoveries	<u>(14,468,811)</u>	<u>(11,912,521)</u>
Provision for claims - End of year	54,043,143	57,145,957
<b>Part B Insurance Coverage</b>	<u>487,346</u>	<u>436,376</u>
<b>Total provision for Part A and B Insurance Coverage</b>	<u>54,530,489</u>	<u>57,582,333</u>

The determination of the provision for unpaid claims and adjustment expenses and the related reinsurer's 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 reinsurer's 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 4.22% (2010 - 4.02%). 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.

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):

	2011 \$	2010 \$
Undiscounted	57,799	61,636
Effect of present value PfADs	<u>(8,045)</u>	<u>(8,536)</u>
	<u>10,187</u>	<u>10,171</u>
Discounted	<u>59,941</u>	<u>63,271</u>

**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.

**7. 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, 2011, no amounts have been drawn on the facilities (2010 - 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 2011 was 2.81% (2010 average rate - 3.23%). The Fund's net loan position of \$15,180,985 (2010 - \$12,872,549) 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 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.

During 2010, interest revenue of \$181,674 was received on the General Fund building loan, interest of \$294,991 was paid on the General Fund cash balances held by the Fund and \$33,126 was paid on the Special Compensation Fund cash balances held by the Fund for a net interest expense of \$146,444.

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

**8. Internally restricted net assets**

The Benchers have allocated \$17,500,000 (2010 - \$17,500,000) of the net assets to the Part B defalcation coverage.

**9. 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, 2011.

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

**10. 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, 2011, expenses of \$332,818 (2010 - \$272,072) were incurred by the Fund with these law firms.

## 11. Contingencies

During the year, a tax auditor for the Ministry of Finance informed the LSBC Captive Insurance Company Ltd. 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.

## 12. Future accounting pronouncements

In December 2010, the Canadian Institute of Chartered Accountants (CICA) in conjunction with the Accounting Standards Board (AcSB) issued new accounting standards for not-for profit organizations. Going forward, private sector not-for-profit organizations will be required to adopt either Part I of the CICA Handbook - International Financial Reporting Standards (IFRS) or Part III of the CICA Handbook - Accounting Standards for Not-for Profit Organizations.

The Society will be adopting Part III of the CICA Handbook - Accounting Standards for Not-for-Profit Organizations for its fiscal year ending December 31, 2012. The financial reporting impact of the transition is currently under review.