Management Discussion and Analysis

The following Management Discussion and Analysis provides a review of the activities, results of operations and financial condition of Lawyers' Professional Indemnity Company ("LAWPRO" or the "Company") for the year ended December 31, 2010, in comparison with the year ended December 31, 2009. These comments should be read in conjunction with the corresponding audited financial statements, including the accompanying notes.

Financial Highlights

Statement of income and comprehensive income

In 2010, underwriting income increased year over year by $25.4 million while investment income increased by $7.4 million, with both items contributing to an increase in income before taxes of $32.7 million, resulting in an income of $22.1 million before taxes. In total, during 2010 the Company generated a net income of $15.2 million, an increase of $21.7 million over 2009, and earned comprehensive income of $18.2 million compared to a comprehensive income of $7.2 million during the prior year.

Net premiums earned

Premiums earned, net of reinsurance ceded, decreased by $1.1 million to $100.4 million in 2010. Premiums from the mandatory Ontario errors and omissions ("E&O") insurance program were $0.4 million lower than 2009 results, as a premium rate increase during the current year was more than offset by a $13.6 million drop in additional premium due from the Law Society of Upper Canada's (the "Law Society") Errors and Omissions Fund under the retrospective provisions of its insurance contract. Compared to budget, the mandatory professional liability premiums came in $0.6 million over anticipated levels as a result of a slightly higher than expected number of insured lawyers participating in the 2010 program. The optional excess insurance program experienced growth of $0.3 million in the year while the title insurance program experienced a decline of $0.7 million during the same period.

Net claims and adjustment expenses

Incurred claims and adjustment expenses in 2010, net of reinsurance recoveries, decreased by $28.8 million from 2009. While results varied significantly by policy year, during the current year the Company experienced net favourable development on prior years' claims of approximately $23.8 million (compared with net unfavourable development of almost $6 million during 2009), due in large part to the completion of a re-evaluation of the actuarial models used to estimate ultimate outstanding losses which allowed the Company to release a significant amount of prior year provisions. The prior year claims expense was affected by a significant drop in the discount rate and a $10.7 million one-time retrospective increase in the required provisions for the anticipated impact of the implementation of the HST in Ontario.

Reinsurance

Similar to recent years, the Company purchased excess of loss clash reinsurance coverage for 2010, which limits its exposure to one or more large aggregations of multiple claims arising from the same proximate cause. The optional excess program continued to be fully reinsured, significantly mitigating exposure to the Company from claims in this program.

General expenses

LAWPRO's general expenses in 2010 were $0.8 million lower than 2009, and were $1.8 million lower than budgeted, due to continued cost management efforts undertaken by the Company.

Commissions earned

The Company earned reinsurance commissions of $1.5 million on premium ceded in respect of its 2010 optional excess insurance program, representing a $0.2 million increase from 2009. In addition, the Company also earned $0.2 million of profit commissions for favourable claims development on the quota share reinsurance arrangements that it had prior to January 1, 2003, down from $2.0 million in 2009. As claims estimates become more certain with time, there is less potential for favourable development on claims relating to older fund years, resulting in a tendency towards lower profit commissions.

Investment income

Income generated from investments increased by $7.4 million in 2010. Investment income for 2010 included net capital gains of $1.4 million realized on disposition of assets, compared to $10.2 million of capital losses in 2009. Investment results for the prior year were impacted by a $9.0 million realized loss relating to the midyear transfer of investment management of the Company's surplus portfolio.

Other comprehensive income

During 2010 LAWPRO earned other comprehensive income of $3.0 million due to an increase in unrealized gains on its surplus investments, driven by a continued broad-based stock market rally. These results compare to the other comprehensive income of $13.7 million experienced during 2009 from an increase in unrealized gains as a result of the robust stock market rally following the fallout from the 2008 world credit crunch.

Balance Sheet

Overall, the Company ended the year of 2010 in a favourable position, with shareholder's equity up by $18.2 million year over year, as the net income incurred during the year was amplified by the other comprehensive income earned during the same period.

Investments

As at December 31, 2010, the market value of the Company's investment portfolio exceeded its cost by $19.1 million, compared to 2009 where the market value exceeded cost by $13.4 million. Investment assets, inclusive of cash and cash equivalents and investment income due and accrued, increased by $44.7 million to $494.4 million at December 31, 2010. The increase was primarily the result of the positive cash flow provided by operations and investment income generated by the portfolio.

The investment portfolio is managed in accordance with the investment policy approved by the Company's Board of Directors in diversified, high quality assets. A portion of the investment portfolio, which is comprised primarily of fixed income securities, is invested in a manner that is expected to substantially match in maturity to the payment of claims liabilities in future years. The portion of the Company's investment portfolio which is considered surplus to the requirements of settling claims liabilities is managed separately and includes fixed income securities and equity investments in publicly traded companies, the values of which are more subject to market volatility.

Provision for unpaid claims and adjustment expenses and reinsurers' share thereof

The provision for unpaid claims represents the amount required to satisfy all of the Company's obligations to claimants prior to reinsurance recoveries. This balance has decreased by $2.3 million. Reinsurance recoveries have declined by $5.1 million and accordingly the net increase in the provision is $2.8 million. This increase is attributable to the fact that the claims expense relating to the additional risk associated with the 2010 program more than offset the reductions to the claims provision from both the settlement of prior year claims during 2010 and the net favourable development of prior years' reserves experienced during the year.

Report On LAWPRO Operations

LAWPRO is an insurance company with three product lines: A mandatory E&O insurance program (as required by the Law Society for all its practising members); an optional excess insurance program that enables Ontario law firms to increase their insurance coverage limit to a maximum of $9 million per claim/$9 million in the aggregate above the $1 million per claim/$2 million aggregate levels provided by the mandatory E&O program; and an optional TitlePLUS title insurance product that real estate practitioners across Canada can make available to their clients.

The mandatory E&O insurance program

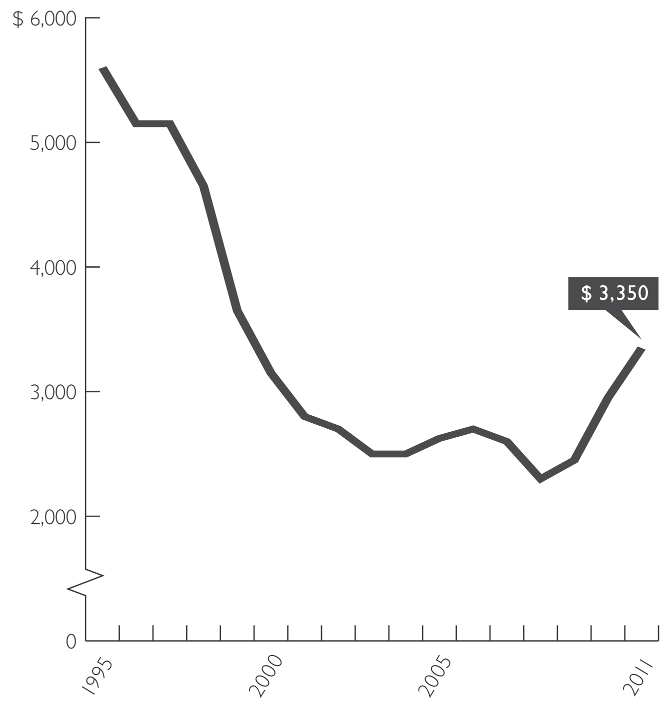
In each of the last two years, the number of lawyers insured under the LAWPRO program has increased about two per cent: In 2010, the Company provided E&O coverage to just over 22,500 lawyers, up from about 22,000 in 2009.

The E&O base premium has varied since the Company assumed active responsibility for the Law Society's insurance operations in 1995 (see graph 1), depending on the outlook of key factors such as claims costs and investment income. In order to address rising claims trends, the base premium was increased by $500 to $2,950 per lawyer in 2010. For 2011, the base premium was further increased an additional $400 to $3,350 per lawyer, a level that represents the average premium over the preceding fifteen years of the program.

One of the hallmarks of the mandatory LAWPRO E&O insurance program is its flexibility. Lawyers have a number of options to tailor their insurance coverage to their specific needs – often with the added benefit of reducing the actual premium payable below the base premium level. As indicated on the chart to the right, the number of lawyers availing themselves of these options continues to increase.

LAWPRO's sustainability initiative, combined with its program of encouraging lawyers to use its comprehensive website to access information and complete insurance-related filings, also continues to yield solid results. A record 96 per cent of lawyers – 21,100 – filed their insurance applications online for the 2010 insurance program; 83 per cent of them did so in time to qualify for the $25 per lawyer e-filing discount. For the 2011 program, those numbers increased again, with 97 per cent of lawyers choosing to e-file applications.

1. Base premium per lawyer



Coverage Option	Feature	No. of lawyers participating (as of Jan. 31, 2010)	No. of lawyers participating (as of Jan. 31, 2011)
New call discount	10-40 per cent base premium discount for those called in the last one to four years	3,592	3,772
Part-time practice	40 per cent base premium discount for eligible lawyers	1,442	1,466
Restricted area of practice option	40 per cent base premium discount for immigration/ criminal law practitioners	1,320	1,343
Innocent Party buy-up	Increase in Innocent Party sublimits up to as much as $1 million per claim/aggregate	3,193 (based on $249/lawyer)	3,268
Run-off buy-up	Increase limits for past services from $250,000 per claim/aggregate to as much as $1 million per claim/ $2 million aggregate	772	867
Real Estate practice coverage	Required for all lawyers practising real estate law in Ontario. Sublimit coverage of $250, 000 per claim/ $1 million aggregate	7,093	7,171

E&O Claims

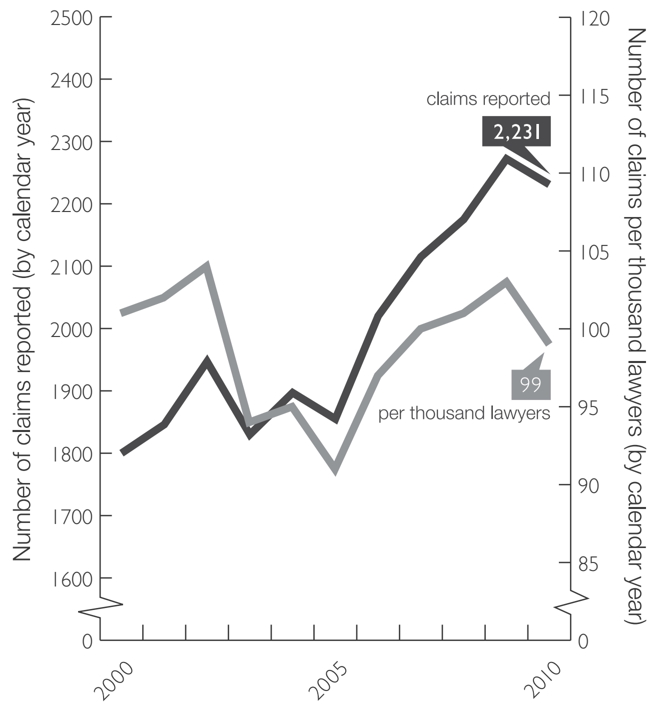
The numbers

In addition to the favourable actuarial changes realized during 2010, LAWPRO experienced – at the very least – a temporary reprieve from a rather troubling recent trend. The number of claims reported to LAWPRO decreased slightly to 2,231 (see graph 2).

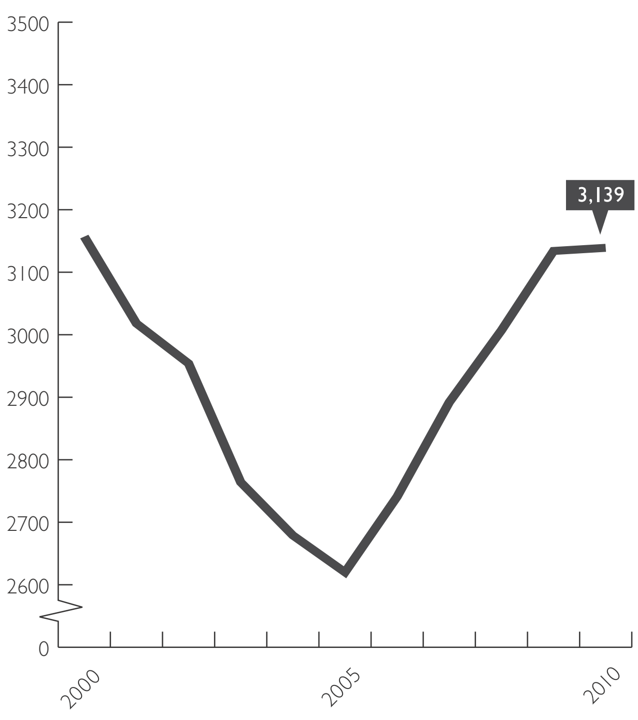
Beyond the fact that much of the actuarial gains enjoyed in 2010 are one-time in nature (resulting from the enhancement of the Company's principal actuarial model for the professional liability program), a number of trends continue to be of concern. Despite a concerted and successful effort on the part of the Company's claims group to close more files than the previous year, the number of open files managed by the claims team continues to stand at over 3,100 – the highest it has been in the last decade (see graph 3).

A very important measure is to compare the average cost of claims for each policy year at a specific point in time: As graph 4 shows, between 2005 and 2008 the average severity (i.e., the average cost per claim) was close to $37,000 compared to an average severity at beginning of decade of only about $30,000. These figures have been affected by the growing number of large claims received by the Company, which continues to exceed 200 per annum (see graph 5). As a result of these pressures, similar to the 2007 through 2009 programs, the 2010 program is expected to ultimately cost between $80 to $90 million in claims expenses.

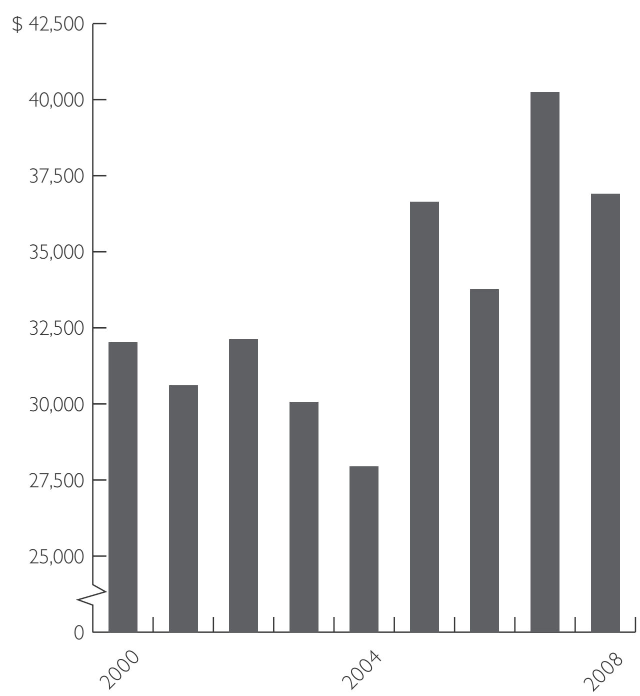
2. Number of claims reported & frequency (by calendar year as at December 31, 2010)



3. Number of open claims files



4. Average cost per claim at 38 months after start of year in which claim was reported



Although the estimated costs attached to 2010 claims are still relatively new at this point, a clear trend is evident. As in the past, real estate and litigation claims continue to account for the bulk of claims costs, with real estate claims representing over 35 per cent of claims costs, on average, for the past five years. The rise in cost of real estate claims is a reflection of both the more complex practice environment and the high underlying values associated with alleged errors in these areas (see graph 6).

Managing costs

LAWPRO's focused claims management philosophy – which sees us resolve claims quickly in situations where there is liability, defend vigorously if the claim has no merit and avoid economic settlements – yields solid results.

In 2010, LAWPRO won 12 of the 13 matters that the Company took to trial, was successful on seven of the eight matters that went to appeal and won 19 of 25 summary judgment applications.

Another important tool – and a measure of success – is feedback the Company receives from lawyers. A survey conducted of insured lawyers with a closed claim demonstrates that the Company is meeting lawyers' needs and expectations. For details see below.

Helping lawyers avoid claims

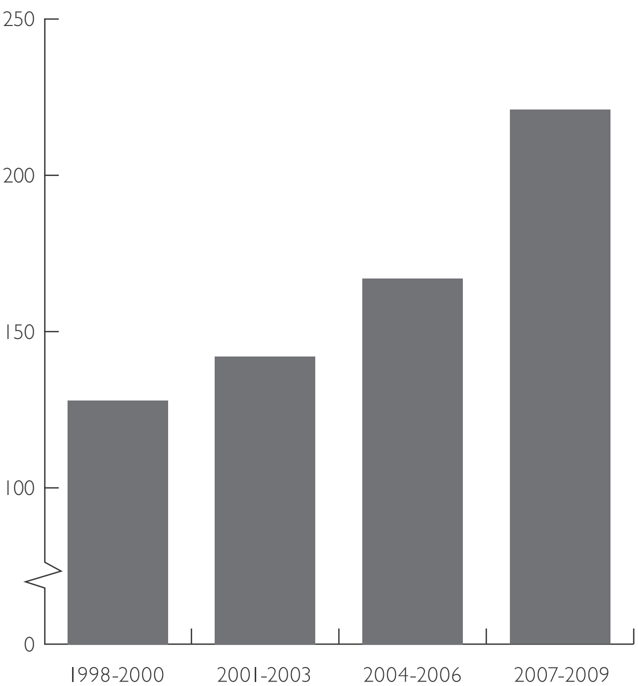
An important focus for LAWPRO is to help lawyers avoid claims in the first place. The Company's practicePRO risk management program provides the practising bar with tools and resources to help lawyers identify practice risks and take steps to minimize their claims exposure.

LAWPRO SURVEY RESULTS

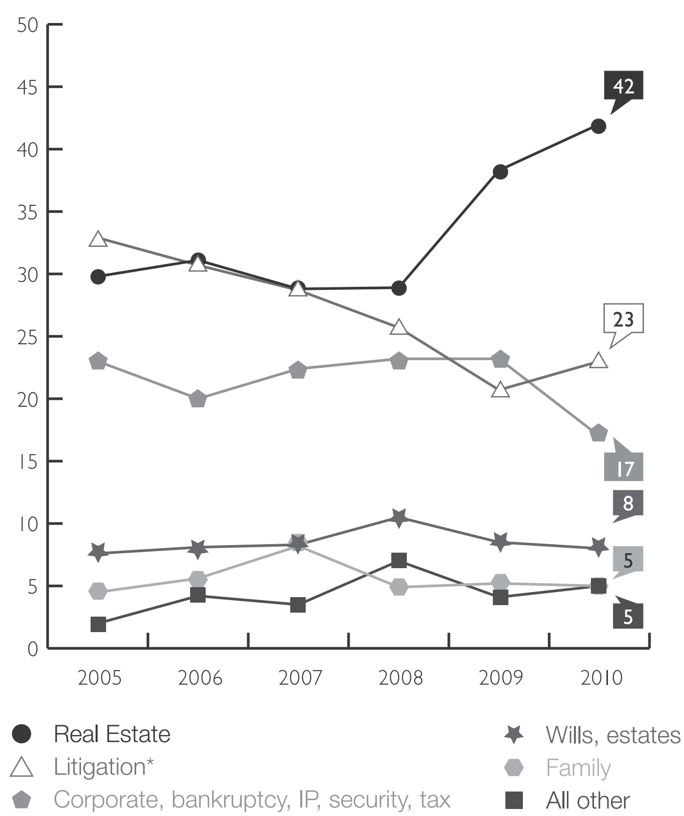
The annual survey of LAWPRO E&O insureds with a closed claim indicated the following:

- 98 per cent said that they were satisfied with how LAWPRO handled the claim;
- 88 per cent said they were satisfied with our selection of counsel;
- 86 per cent said they would have the defence counsel firm represent them again; and
- 84 per cent said LAWPRO received good value for defence monies spent.

5. Number of claims reported with a value greater than $100,000 (as at February 28, 2011)



6. Distribution of claims by area of practice (% of gross claims costs as at February 28, 2011)



In 2010, the practicePRO website recorded an 11 per cent increase in traffic to 229,000 visits from 205,000 the previous year. More than 287,000 LAWPRO articles and resources were downloaded, up from 244,000 in 2009.

A principal tool to communicate risk management content is *LAWPRO Magazine*, which is distributed to all practising insured lawyers. Complementing the printed magazine are electronic newsletters and alerts on active frauds, evolving risk issues, and insurance program-related information.

The practicePRO Avoid A Claim blog enables LAWPRO to provide lawyers with tips and insights into practice issues as they develop, including real-time warnings on active frauds targeting lawyers. Through Twitter feeds and LinkedIn the Company and practicePRO ensure lawyers know when new content is available on our website, on the blog or in our magazine. By the end of 2010, the number of those following LAWPRO and practicePRO on Avoid A Claim and our Twitter feeds topped the 1,000 mark.

LAWPRO also works behind the scenes to ensure the risk management message is getting heard. As a result of its CPD Credit program, through which lawyers taking LAWPRO-approved continuing professional development programs receive a $50 per course credit on their insurance premium (to a maximum of $100), the Company has ensured CPD providers include a significant risk management component in their programs. In 2010, the Company approved 184 programs attended by more than 24,000 lawyers. LAWPRO and practicePRO content was included in the materials for many of these programs.

Active participation in the work of the Law Society and of law-related associations is yet another way that the Company spreads the risk management message.

In 2010, for example, the Company prepared a submission to the Law Society on the challenges of unbundled legal services. As well, the Company showed leadership in working with the development of a model file retention policy for large law firms and helped the CBA Conflicts of Interest Task Force with a conflicts resources toolkit.

practicePRO delivered 35 presentations on risk management-related topics to various law associations, law firms and CLE programs. LAWPRO's practicePRO director co-chaired the Law Society/ Ontario Bar Association's annual Solo and Small Firm Conference (for the fifth year), and co-chaired the 2010 CBA Annual Conference and Meeting.

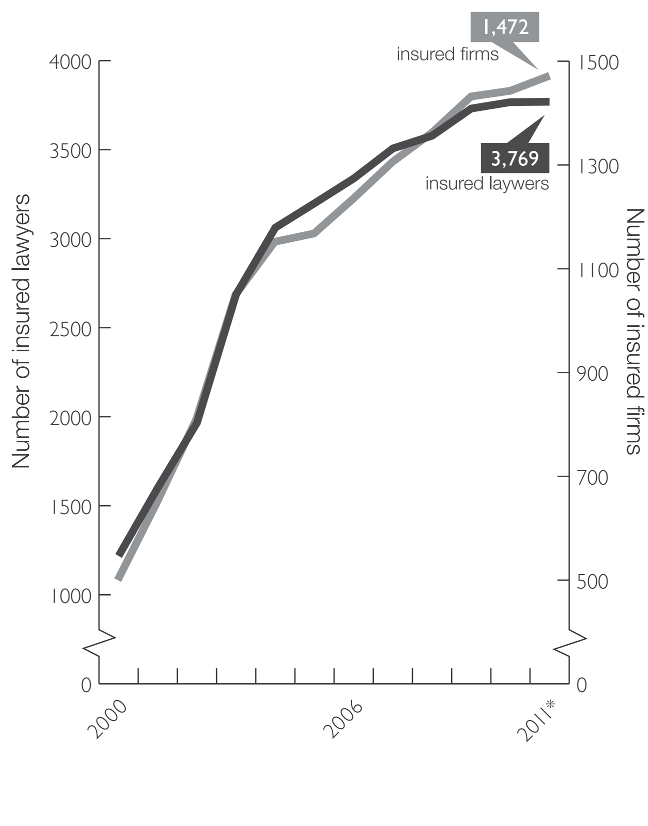
The LAWPRO Excess program

Since it was established in 1997, LAWPRO's optional excess insurance program has posted consistent annual growth in revenues and numbers of law firms (and lawyers) insured under the program. A record 1,448 firms representing 3,768 lawyers elected LAWPRO as their excess insurance provider for 2010 (see graph 7); 113 firms chose the maximum $9 million limit option.

We have seen similar growth in the 2011 program. The number of firms insured under the LAWPRO Excess program for 2011 has increased to 1,472, representing 3,769 lawyers. Of 57 new firms opting to buy excess coverage from LAWPRO for 2011, 84 per cent did not already carry excess coverage. The Company's retention rate on excess business was 97 per cent for the second consecutive year, a clear indication that this program meets the needs of the market it is aimed at – small and medium-sized firms of fewer than 50 lawyers. LAWPRO's excess program insures, on average, 15 per cent of lawyers employed in firms of 50 or fewer lawyers.

To date, the Company has not paid any indemnity amount under its excess program, a reflection of LAWPRO's ability to carefully manage costs within the insurance program's primary limits. There are, however, some Excess claims files with provisions. Prudent underwriting and solid claims management have helped ensure that our excess program is a profitable line of business for LAWPRO.

7. LAWPRO Excess Insurance Program
(as at February 28, 2011)



The TitlePLUS program

In part due to a difficult real estate market, the TitlePLUS title insurance program posted a modest decrease in gross written premiums in 2010 compared to 2009. Although our national purchase market penetration fell slightly, there was a significant increase in policy sales relating to residential properties in many provinces outside Ontario as well as commercial properties.

Our subscriber base in 2010 increased to well over 4,700 lawyers and Quebec notaries, with new applications continuing to be received, and the Company issuing TitlePLUS policies for approximately 790 lenders across Canada. These results indicate that our vision of real estate practice continues to gain traction: The higher level of legal expertise and professionalism that LAWPRO expects from both lawyer/notary subscribers and our TitlePLUS staff sets it apart from other providers.

TitlePLUS claims

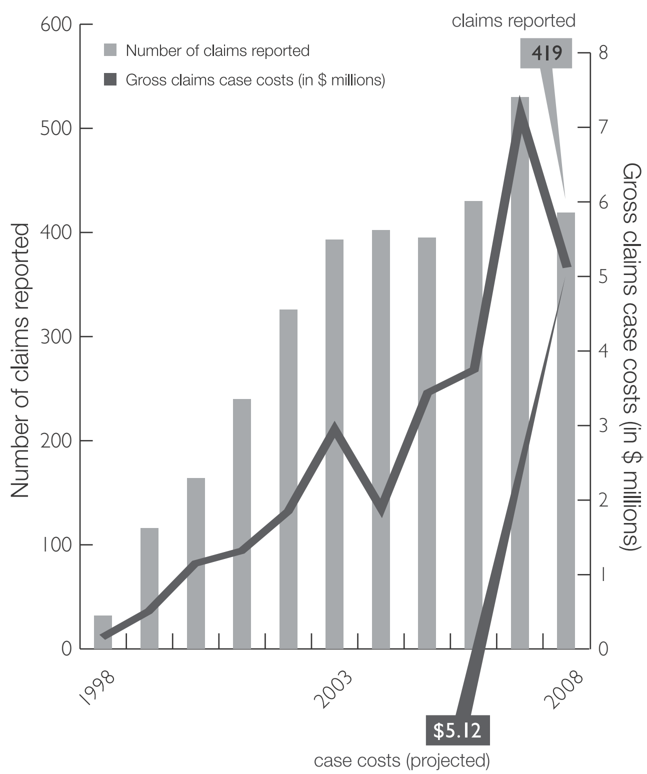
The legal expertise and experience of the TitlePLUS team referenced earlier not only helped alert lawyers to potential claims issues, but also strengthened its stringent underwriting measures. The result: Over 90 per cent of TitlePLUS claims are minor with payments of less than $10,000, and the average indemnity payment on a TitlePLUS claim is approximately $4,650 (based on claims closed as of December 31, 2010).

It should be noted that over the history of the TitlePLUS program, our claims paid ratio (the ratio of claims paid to premiums) stands at 40 per cent.

Building compliance-related claims continue to have a significant impact on the program. For policies sold in the years since 2000, the TitlePLUS program has had 856 building compliance related claims, costing a total of $13.1 million (payments plus reserves on claims in progress). So, although only 23 per cent of the TitlePLUS claims by count arise from this area of coverage, 46 per cent of the claims costs reside here. These trends have placed significant pressures on the program's claims costs (see graph 8).

The TitlePLUS underwriting team is working on methods to better detect building compliance risks before a policy is approved. Also, the TitlePLUS claims team is focusing additional efforts on recovery initiatives where a past property owner should be bearing responsibility for the problem, as well as on salvage opportunities.

8. TitlePLUS claims (as at February 28, 2011)



Transition to International Financial Reporting Standards ("IFRS")

Publicly accountable enterprises in Canada are required to adopt IFRS for periods beginning on or after January 1, 2011. LAWPRO will adopt IFRS as a replacement of current Canadian GAAP for fiscal periods beginning the first quarter of 2011, with corresponding comparative financial information for 2010.

Our IFRS transition plan includes the education, review, approval and implementation of any accounting policy changes. Additionally, the transition plan includes ensuring that project resourcing remains adequate, modifying internal controls over financial reporting as appropriate, frequent communication with our external auditor as well as the Audit Committee and Board of Directors which includes a review of transition progress, discussion of potential transition and ongoing reporting changes, and an overview of developments in accounting and regulatory guidance related to IFRS. As we implement IFRS, we continue to monitor ongoing changes to IFRS and adjust our transition and implementation plans accordingly.

Our transition project status is currently on-track in accordance with our overall transition plan. We have completed our assessment of the preliminary IFRS first-time adoption elections, identified the key applicable accounting policy differences, finalized the opening IFRS balance sheet and quantified the quarterly comparative results. The most significant remaining milestone in our plan is to prepare the note disclosures under IFRS, which will be completed in 2011.

In general, an entity is required to apply the principles under IFRS on a retrospective basis. Any difference between the carrying value of assets, liabilities and equity determined in accordance with Canadian GAAP and IFRS, as at January 1, 2010 will be recorded in opening retained earnings. However, certain optional exemptions from retrospective application exist for certain areas where the International Accounting Standards Board ("IASB") has determined that it would be operationally impracticable. The key preliminary first time adoption election under IFRS 1 – "First Time Adoption of IFRS" that is applicable to LAWPRO relates to employee benefits. After careful consideration, we do not expect to recognize the unamortized actuarial gains and losses associated with our defined benefit pension plan in retained earnings upon transition to IFRS, as is afforded by the IFRS 1 election, and instead will apply the IFRS requirements retrospectively as sufficient data exists to perform this calculation and it is not operationally impracticable to do so.

Based on our current analysis of the identified differences between Canadian accounting requirements and existing IFRS, there are a very limited number of differences with any significance. However, one key difference that is applicable to LAWPRO's operations relates to the impairment of financial instruments. Impairment charges under IFRS are recorded for available for sale ("AFS") equity instruments if declines in the carrying value are significant or prolonged, irrespective of future expectations for recovery. Under Canadian GAAP, impairment charges are not recorded when such declines in value are considered to be temporary. This change may result in more frequent impairment charges recorded under IFRS.

The net result after considering any applicable IFRS 1 elections, as well as all Canadian GAAP and IFRS accounting differences, is that LAWPRO does not have any material adjustments upon adoption of IFRS to either its opening January 1, 2010, balance sheet or fiscal 2010 financial statements. Furthermore, we do not expect that the initial adoption of IFRS will have a significant impact on our disclosure controls and procedures, information technology systems or our business activities.

On July 30, 2010, the IASB issued its Insurance Contracts (Phase II) Exposure Draft which outlines a proposed framework for a single standard for the measurement of insurance contracts to be applied across all jurisdictions adopting IFRS as published by the IASB. The changes contained in these proposed standards may lead to a significant initial adjustment to reported insurance liabilities upon adoption, and may create significant ongoing volatility in our reported results. This standard is currently being developed and is not expected to be in effect until at least 2014.