

About LawPRO®

Lawyers' Professional Indemnity Company (LAWPRO) is licensed to provide professional liability insurance and title insurance in numerous jurisdictions across Canada.

In 2005, LAWPRO provided liability insurance to about 20,400 members of the Law Society of Upper Canada. Through our TitlePLUS® operation, LAWPRO also provides comprehensive title insurance and legal services coverage for residential and commercial purchase and mortgage-only/refinance transactions handled by lawyers.

Our mission

"To be an innovative provider of insurance products and services that enhance the viability and competitive position of the legal profession."



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chairman



LAWPRO's financial results in 2005 were again solid. The company was profitable, posting net income of \$7.3 million. We have assets of \$444 million, and equity of just under \$110 million. Our strong financial results and excellent capital position were acknowledged by A.M. Best Company which awarded LAWPRO an A rating for the sixth consecutive year.

LAWPRO also continues to set the standard on programs and services that expand the profession's horizons. For example, through the practicePRO® risk management program, LAWPRO took a leadership role last year in familiarizing the bar with electronic discovery. Numerous other risk management initiatives have earned the company international recognition. The TitlePLUS program is now a full-service conveyancing solution being used by more than 3,000 lawyers from "coast to coast to coast."

As a member of the bar, I am pleased to see the profession's positive response to these many initiatives. My peers have recognized the role that education plays in managing their exposure – as evidenced by the increase in the number of lawyers applying for LAWPRO's CLE premium credit; similarly, more lawyers are buying Excess Insurance, Innocent Partner coverage and Run-Off Buy-Up coverage – indications that there is a better understanding of potential exposures and that the risk management message is being heard.

Success of this kind does not come easily. It is the result of excellent management, talented and committed staff, and exemplary teamwork. Our Board commends and thanks all members of the LAWPRO team for their many contributions to the company's success.

Success however is also a double-edged sword: Weighing premiums and profits against predictions of risk is a fine balancing act. On the one hand, our Board members – practising lawyers, and insurance and financial professionals alike – are sensitive to the fact that premiums are a significant fixed cost for members of the bar. We are pleased that premiums have been maintained in the \$2,500 – \$2,700 range for the past three years.

Equally critical is the need to ensure the company is positioned to mitigate the potential for significant premium increases should claims and costs suddenly rise. The growing fraud risk makes this balancing act even more difficult. We have seen in several jurisdictions how millions of dollars in claims can be generated through the acts, oversights or omissions of a small number of practitioners. The company's fraud-related losses over the last three years have averaged in the \$7 million range annually: Experience tells us that a prudent approach is appropriate.

Striking the right balance is an ongoing challenge that will be expertly managed by President and CEO Michelle Strom and her management team; under their leadership, LAWPRO has earned a track record of success that is unusual in insurance circles today. I also would like to thank the members of our Board whose expertise, experience and insights into legal, insurance and financial matters benefit us all.

A handwritten signature in blue ink that reads "Kim A. Carpenter-Gunn".

Kim A. Carpenter-Gunn



president and CEO

Ontario lawyers have come to expect more from LawPRO than insurance protection and services: You look to us to monitor issues, interpret trends and innovate with programs and tools that support the bar. We will continue to rise to these challenges. We are not content to rest on our accomplishments, no matter how consistent or impressive.

Our TitlePLUS program is a good example. In 2005, our efforts to build a national, Bar-related™, technology-based conveyancing solution bore fruit: From Nunavut to Newfoundland, the real estate bar is acknowledging the vital role that our TitlePLUS initiative plays in guiding the bar through a time of change.

Similarly, the leading role we were asked to take on electronic discovery – at the the task force level and in educating the bar about E-Discovery – speak to our reputation, locally and internationally, as a leader in the field of risk management.

Within the insurance program itself, we are seeing more lawyers opt for optional coverages or buy up their coverage limits – an indication that our efforts to sensitize the bar to their potential exposures are being successful. More lawyers than ever are accessing web-based resource materials, electronic filings and other online services: Like LawPRO, they are walking the technology talk.

We attribute these successes to our focus on you, your needs and priorities: We are committed to helping lawyers anticipate and adapt to economic and environmental changes.

Experience tells us that claims, and insurance premiums, are a reflection of the larger economic environment. When the economy cools, problems percolate to the surface and lawyers' judgments are more likely to be challenged. The increased claims costs we saw in the real estate area of practice this year, despite a robust housing market in 2005, cause us some concern, given indications that the sustained growth of the past years is expected to slow in 2006. Similarly, the changing economic environment is redefining the types of activities in which lawyers engage: Complicated transactions result in complex, costly claims – with implications for both our claims portfolio and the scope of insurance coverage we provide.

Environmental factors also affect our program. Our demographic analysis indicates that the bar as a whole is aging, that young lawyers tend to gravitate to urban, large firm practices, at the expense of smaller real estate/family law-based practices outside of the larger centres. At the same time, our monitoring of the legal environment indicates that litigation costs are increasing – as is the number of unrepresented litigants. All of these trends have potential cost implications for the insurance program.

Many changes await the profession – and LawPRO – in the coming decade. What will not change is our focus on providing the best possible insurance programs and services to meet your needs, whether you're a lawyer on main street or Bay Street.

The team at LawPRO has the skills, experience and commitment to keep the program moving in the right direction, and I thank them for all their efforts.

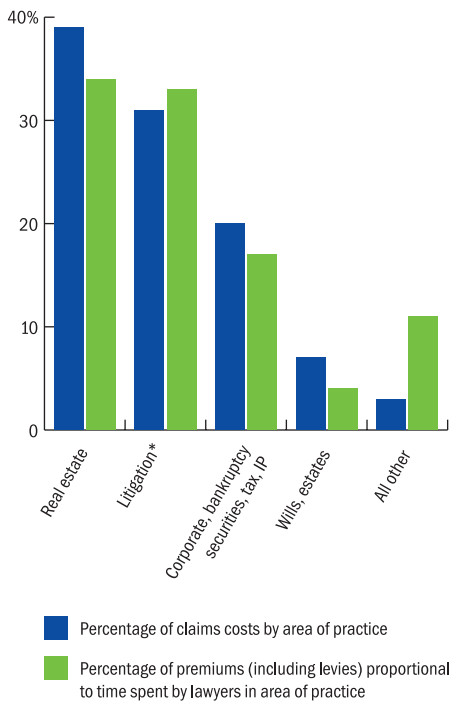
A handwritten signature in blue ink, appearing to read 'Michelle L.M. Strom'. The signature is fluid and cursive, with a large loop at the end.

Michelle L.M. Strom



Underwriting & Customer Service

Comparison of premium revenues and claim costs for 2005



* Includes plaintiff and defence litigation, family law and criminal law

Over the past decade, we have implemented numerous measures to ensure premiums and the risk associated with various types and areas of practice are in line. Because of their greater propensity for additional claims, lawyers with claims are required to pay a claims history surcharge; lawyers practising civil litigation and/or real estate law pay transaction levies as these two practice areas consistently account for the majority of our claims costs.

Part-time practitioners, lawyers newly called to the bar, and lawyers whose practice is restricted to the lower-risk areas of immigration and/or criminal law (i.e. restricted areas of practice) are eligible for significant premium discounts,

ensuring cost-effective insurance

As the professional liability insurer for Ontario lawyers, LAWPRO is charged with the responsibility of providing lawyers with access to cost-effective malpractice insurance. Our Underwriting and Customer Service department takes the lead in implementing this mandate: It monitors the changing practice environment to ensure policy coverage addresses the evolving needs of the bar, while at the same time assessing the implications of this changing environment on the program's exposure; it informs the bar about potential areas of liability and the flexibility in the program to tailor-make coverage to individual needs; and it manages the program so premiums that lawyers pay generally reflect the statistical risk that they represent.



consistent with statistics that indicate these categories represent a lower risk to the insurance program.

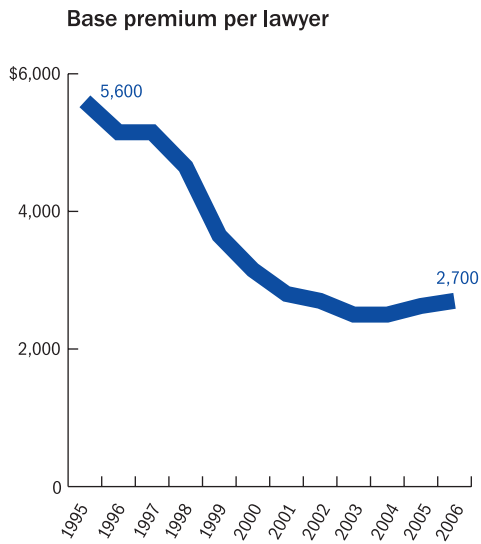
A number of coverage modifications have ensured that the program evolves with changing needs. Lawyers participating in the Pro Bono Ontario initiative now have enhanced coverage for their *pro bono* legal services. Those facing possible penalties under the *Income Tax Act* or *Excise Tax Act* now have limited defence cost protection, provided their defence is successful. To limit the program's exposure to claims arising out of services that do not fall within the intended scope of "professional services" insured under the program, we excluded from coverage claims arising out of investment advice or

services, and claims related to business ventures or investments that are not directly related to the practice of law.

LAWPRO announced in 2005 that insurance coverage will be modified to ensure our program is consistent with pending legislation regulating mortgage brokering and lending activities in Ontario. Once legislation is finalized and passed into law, we will insure lawyers for the specific legal services that fall within the exemption provisions for lawyers in the legislation.

Maintaining premium stability

Managing the program's exposure and risk rating measures are important components of maintaining a stable insurance premium.



Setting the premium each year is a complex process that takes into account projected claims costs, estimated revenues, and trends that could affect overall program costs and revenue sources. In recent years base premiums have been in the \$2,500 – \$2,700 range. The base premium in 2005 was \$2,625 per lawyer; the base premium for 2006 is \$2,700, which is less than half of the record high base premium of \$5,600 charged a decade ago when LawPRO commenced management of the program.

Year-end results for 2005 exceeded our projections. A robust housing market and healthy investment returns contributed to higher than expected net income. This cushion will provide us with some flexibility when it comes to determining premiums for 2007, although an important consideration will continue to be our increasingly complex claims portfolio, as more fully discussed on pages 10 and 11.

Many lawyers pay significantly less than the full base premium, consistent with the risk that they represent. For example, in 2005 about 4,500 lawyers qualified for premium reductions available to those in practice for less than four years; another 1,100 received the 40 per cent restricted area of practice premium discount, while about 1,200 qualified for the part-time practice discount.

Matching liability to coverage

LawPRO provides lawyers with a variety of tools and information to help them assess the liability associated with their law practice; for example, a series of booklets titled *Insurance Matters* details specific coverage provided to lawyers such as corporate counsel and retired lawyers exempt from paying the full premium, and explains the options available to tailor coverage based on their own assessment of their exposure.

The increase in the number of lawyers opting to increase certain coverage (sub)limits or securing our Excess coverage indicates that they are more attuned to their potential liabilities, and interested in ensuring they have adequate protection in place. Between 2005 and 2006, revenues from optional Run-Off Buy-Up insurance, for example, almost doubled; the number of lawyers buying additional Innocent Party protection is up about four per cent.

Participation in our optional Excess program continues to grow by about four per cent annually. In 2005, 1,188 firms representing 3,199 lawyers purchased our Excess insurance coverage, which provides limits of up to \$4 million per claim/\$8 million in the aggregate above the \$1 million per claim/\$2 million in the aggregate levels of the primary program.

For 2006 to date, 95 additional firms placed their excess coverage with LAWPRO, 94 per cent of which had no expiring excess coverage in place. This, coupled with a 97 per cent retention rate from 2005, brings the number of firms who have placed their excess coverage with LAWPRO to 1,235 (representing 3,338

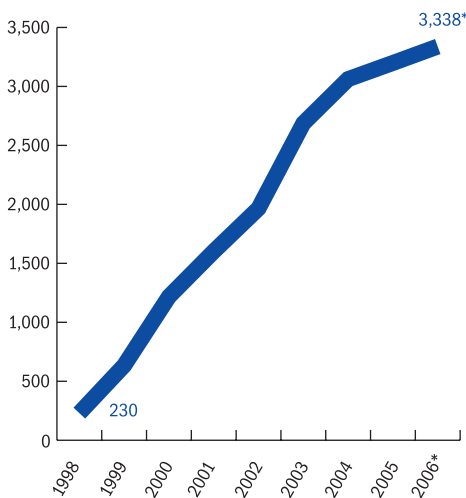
lawyers) for 2006. This steady growth reaffirms that our program is a valuable resource for the smaller firms of 15 or fewer lawyers that we specifically target with our Excess program.

Putting a face to the program: customer service

Our customer service team was on the front line of providing program information and services to approximately 20,400 lawyers insured under the LAWPRO program in 2005. Our customer service representatives fielded close to 44,700 calls – an eight per cent increase from the previous year, and handled about 17,400 pieces of correspondence, up four per cent from 2004. We attribute these increases to a more proactive stance on our part in contacting law firms on premium-related issues (such as outstanding transaction levies), as well as to modifications in policy coverage in 2005, which prompted calls from lawyers seeking advice with regard to coverage before undertaking specific duties. A significant number of inquiries came from lawyers retiring or planning to retire from practice and needing guidance on options available to them.

The increased use of technology-based processes has enabled us to respond quickly to these increased volumes of lawyer contacts. More than 17,800 lawyers – about 87 per cent of the practicing bar – filed their insurance applications online in 2005 (for the 2006 insurance year), using our streamlined, web-based filing system. Many of these lawyers were able to instantly access their insurance invoice and policy documents in the same online session, as well as authorizing payment for their premiums. In 2006, we will continue to expand the scope of information and transactions that lawyers can complete online.

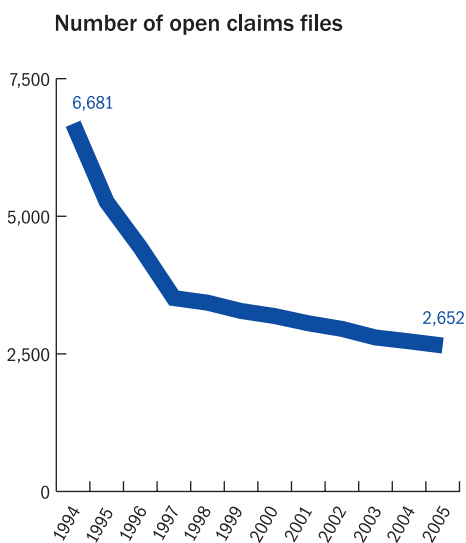
Lawyers insured under LAWPRO Excess Insurance program



* As of March 1, 2006



Claims



Our results for 2005 are consistent with these trends: We opened 1,855 new claims files, and closed 1,931 files, many of which related to claims from previous years. Drawing on the expertise and experience of our internal claims counsel, we were able to close more than 45 per cent of these files without making any defence or indemnity payment; as well, of the files closed, 85 per cent were closed without any indemnity payment made.

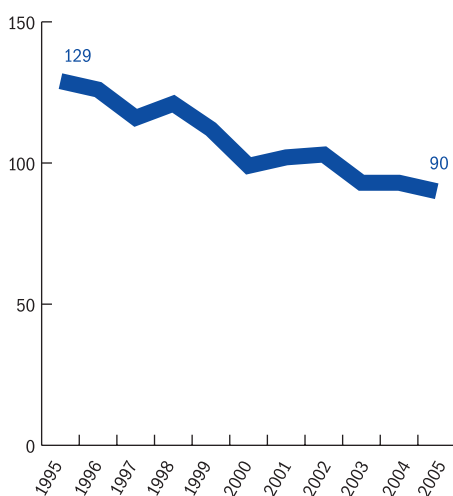
With the number of lawyers insured under the LawPRO program increasing by about two per cent in 2005 over 2004, and the number of claims reported remaining constant, there was a decrease in claims frequency, as illustrated in the graph on the next page.

defending insured lawyers

In each of the last six years, lawyers have reported between 1,800 and 2,000 new claims to LawPRO under the Ontario professional liability insurance program. In each of these years, we consistently closed more files than we opened, bringing the number of open claims files in our portfolio to a record low of 2,652 at the end of 2005. We attribute this ongoing success to the singular focus we bring to each file. We determine a resolution strategy as quickly as possible; and we assign the appropriate resources to implement that strategy quickly and effectively. This approach has consistently benefited the profession. Despite increasingly complex and challenging claims files, we have held claims costs in recent years on the professional liability insurance program to an average of about \$65 million annually.



Number of claims per thousand lawyers



A focused file management strategy

Our goal with each file is to determine a resolution strategy early in the life of the file, and then move quickly to implement this strategy. If there is liability on the part of the lawyer, we attempt to resolve the matter quickly and cost-effectively. On the other hand, if the claim is without merit, we will defend the insured, through the trial process if required: We will not make economic settlements. As well, we will take to trial those claims that can only be resolved in court.

Our track record when we do go to trial continues to be excellent. We were successful on 11 of 18 matters that went to trial in 2005 (five are under reserve); we were successful on all seven matters that had been taken to appeal by plaintiffs who had not been successful in their initial trial; and we won 14 of 17 summary judgment applications.

Question	Yes
Were you satisfied with the way LAWPRO handled your claim?	95%
Would you ask defence counsel firm to represent you again?	89%
Were you satisfied with selection of counsel?	89%
LAWPRO received value for defence monies spent?	86%

Another measure of the success of our focused approach to claims are the views of lawyers whose claims we have resolved. As in past years, lawyers who completed a survey in which they were asked to evaluate LAWPRO examiners/counsel and external defence counsel on their services gave both high marks.

New initiatives

A more challenging claims portfolio and a changing practice climate require ongoing innovation in claims management.

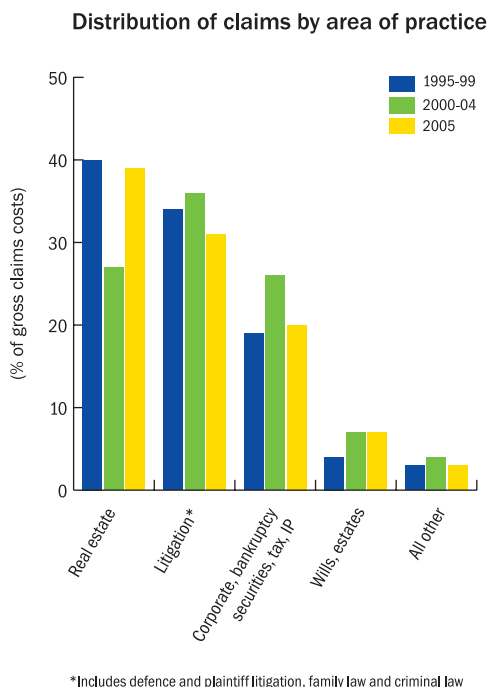
In 2005, we accelerated our transition to a “less paper” environment: Much of the communication between external defence counsel and our internal counsel is now captured electronically. The reams of paper normally associated with claims files are being replaced by electronic copies of documents which are easier to access, and significantly reduce the costs associated with paper-based files. We are examining the potential of websites and extranets as workspaces in which our internal and external counsel can work together in a secure environment.

We also continue to explore new opportunities to more effectively work with defence counsel. Clearly defined cost and budget guidelines and reporting requirements ensure active management of each file by our claims staff. As well, we continue to encourage external counsel to mentor junior counsel on our files, where appropriate. Assigning specific files to junior counsel and encouraging them to develop their own portfolios – and develop expertise in legal malpractice law – helps us better manage claims in both the short and long term.

A challenging claims portfolio

Claims trends, by their nature, are unpredictable and are influenced by factors that are inherently variable. Managing claims poses significant challenges as we have limited control over many of the factors that influence the portfolio.

Among the most unpredictable challenges are those presented by claims with a



fraud component. They are among the most complex of claims we receive, and often among the more costly to resolve. Although the LawPRO insurance policy excludes fraud, there are numerous situations in which coverage would be provided for claims with a fraud component. In some cases, lawyers are duped by employees, clients, or third parties who are involved with a client; even when lawyers are complicit in fraud, coverage could be provided to innocent partners who are named as parties in a claim. In 2005, about 10 per cent of our claims costs were attributed to fraud-related claims.

To combat fraud, our practicePRO risk management program has provided the bar with information to help lawyers identify fraudulent transactions; more stringent underwriting has helped our TitlePLUS title insurance program avoid the multi-million dollar fraud losses reported by other title insurers. We continue to work with industry and government groups to combat real estate fraud at all levels. However, reports from law enforcement agencies in Canada and the United States lead us to believe that we have not seen the last of fraud, and that we must continue to be vigilant.

Our ability to hold the line on costs is also being challenged by the increasingly complicated claims we see, often brought by very difficult claimants or self-represented plaintiffs. These files often require inordinate attention and time on the part of both internal and external counsel, take significantly longer to resolve and often result in increased legal fees.

Another trend that we are monitoring is the increase in complex claims that we expect will cost us \$250,000 or more to resolve. At present, these claims represent less than three per cent of the claims in our portfolio, but account for more than 40 per cent of anticipated claims costs. A small increase in the number of such claims could have a major impact on our claims costs and operating results.

These trends are making themselves felt in the changing mix in our claims portfolio. Although the number of real estate claims

reported in the past three years is stable, costs attributed to these claims have climbed from 23 per cent of total claims costs in 2003 to 40 per cent in 2005. While costly fraud claims account for some of this increase, we are also seeing much larger losses in individual real estate files than previously – a reflection of higher property values and active real estate development opportunities.

The global economy, the multi-million dollar transactions and complex dealings in which lawyers are involved mean that claims, when they result, are often complicated and costly. This will continue to put pressure on claims costs and consequently on future premiums.

TitlePLUS claims

Although fraud is a growing concern in our TitlePLUS claims portfolio, careful underwriting and other control measures have helped minimize its impact. In 2005, fraud-related claims accounted for less than 20 per cent of all TitlePLUS claims costs – significantly below levels of up to 40 per cent reported by other title insurers. Notably, almost three quarters of the fraud claims payments were made on claims generated by only two lawyers. Even when lawyers themselves are not implicated or culpable in a fraud, lack of sensitivity to the indicators of fraud or lack of attention to detail can have far-reaching consequences for all parties involved.

The majority of other TitlePLUS claims arise out of municipal issues such as realty tax arrears, building deficiency work orders, building code violations and the like. Less than 20 per cent of claims related to liens and encumbrances, and 14 per cent of TitlePLUS claims to date arise out of our legal services coverage. These legal services claims would not have been covered under the policies of most other title insurers, and are a special benefit of TitlePLUS coverage in purchase and mortgage-only policies. TitlePLUS claims are settled for an average of \$4,300 per claim, with close to 90 per cent of all TitlePLUS claims reported to date closed for under \$5,000 per claim.



Getting the word out

practicePRO focuses on getting the risk management message out to the legal profession. And lawyers are listening: In 2005, practicePRO delivered 30 presentations on risk management, electronic discovery and related topics at CLE programs, conferences, seminars and individual law firms. practicePRO reached thousands of lawyers across Ontario and beyond by producing articles and columns for both online and print publications.

The practicePRO website – one of our primary risk management tools – received almost 39,000 unique visitors who downloaded 57,600 copies of risk management materials: among the most popular were limitations-period related information, a booklet on security and privacy of electronic data, and client relationship materials, including sample retainer agreements. Daily site usage increased 30 per cent from 2004.

practicePRO showcased the benefits of technology in law practice by holding

regular technology breakfasts. To give a greater number of lawyers access to the information, the breakfasts are taped and available online through BAR-eX®.

LAWPRO Magazine and *managing* booklets

LAWPRO Magazine, our risk management publication, contains regular practicePRO columns and content on a wide variety of risk and practice management topics. In 2005, LAWPRO Magazine examined the future of practice areas such as family law and real estate law, and looked at electronic discovery and its implications for lawyers in all practice areas.

The practicePRO *managing* series of booklets is an essential reference to help lawyers manage the risks associated with specific practice issues. In 2005, practicePRO released the seventh in the series, *Managing the security and privacy of electronic data in a law office*.

communicating risk management

Today's practice environment involves more than straightforward legal expertise: The challenge for lawyers lies in developing 'soft skills' to better manage their law practices and client relationships. Our claims statistics show that poor communication, time management, procrastination and other soft skills are the most common causes of malpractice claims. practicePRO's tools and resources help lawyers develop these skills to assist them in reducing their exposure to claims. These initiatives have earned practicePRO an international reputation as a leading provider of risk management content and resources.



CLE Premium Credit

Through practicePRO, the LAWPRO CLE Premium Credit program has changed the face of continuing legal education in Ontario. The program offers a \$50 per course credit (to a maximum of \$100 per lawyer) applied to insurance premiums. The number of lawyers who attended approved programs increased to 14,300 in 2005 from 12,500 in 2004, and the number of approved courses increased to 92 from 87 the year before. Many CLE providers are specifically tailoring their course content in order to qualify for the credit. The risk management message is now a standard component of Ontario CLE programs.

E-Discovery

practicePRO has played a leadership role on educating the profession on evolving trends and issues in the area of electronic discovery. As part of the E-Discovery sub-committee of the Discovery Task Force, practicePRO helped develop guidelines for the handling of electronic documents. We

also helped educate lawyers on e-Discovery through articles and presentations at law firms and a joint OBA/Advocates Society CLE program. The September LAWPRO Magazine focused on E-Discovery issues. For practicePRO's Canadian-focused online E-Discovery reading list, visit: www.practicepro.ca/ediscovery.

A model for the profession

We serve as a resource for the legal community and have become recognized internationally as a model to emulate for other risk and practice management initiatives. Our materials are widely used, borrowed and adapted by other jurisdictions across North America. At home, practicePRO provided its risk management expertise to the Law Society through many CLE programs, the Bar Admissions Course material, the new Best Practices Self-Assessment tool and the Private Practice Refresher Program (PPRP) Technology Module.

The logo for TitlePLUS is displayed in a light green, sans-serif font. The word 'Title' is in a smaller size than 'PLUS'. The background of the logo area is a gradient of green and blue, with a small inset image of a family in the bottom right corner.

A number of new TitlePLUS initiatives in 2005 addressed the changing needs of the real estate marketplace.

In response to growing lawyer interest, we launched TitlePLUS commercial coverage (for purchases of less than \$2 million in Ontario only), and OwnerEXPRESS™ for current homeowners. OwnerEXPRESS, which is available nationally, lets lawyers meet a growing demand among consumers for post-closing coverage that homeowners can fall back on if they discover an issue, such as a fraud on title, weeks, months or years after their purchase has closed. Both products will help strengthen the TitlePLUS reach in the Ontario title insurance marketplace, where most recent estimates indicate

enhancing lawyers' role in real estate

Its focus on lawyers and mandate to provide the practising real estate bar with a full-service conveyancing package make our TitlePLUS program unique in the Canadian marketplace. A primary focus is to support and enhance the role of the lawyers in conveyancing. To this end, we have introduced web-based programs that streamline the transaction and meet the evolving needs of lenders and other parties. Expanding the TitlePLUS product line to include commercial purchases and current owners coverage lets lawyers better meet client needs. Providing lawyers in all provinces and territories (except Quebec) access to TitlePLUS meets the needs of the lending community, and makes the option of working with a Bar-related™ title insurer an option for more lawyers across the country.



14 per cent of transactions are now being insured with a TitlePLUS policy.

We also worked closely with the lending community and legal-related associations to address the need for streamlined reporting relationships between lenders and lawyers. The Virtual Intermediary Program™ (VIP), which provides lawyers and lenders with a centralized website on which they can exchange data, retrieve documents and generate reports, was expanded in 2005 to include a funds transfer component. VIP has been so successful that one national lender is now using TitlePLUS coverage, where available, exclusively on all of its mortgages (accounting for close to 10 per cent of policies sold). Other lenders are studying this option closely.

As well, 24 new lenders joined our growing roster of confirmed lenders, making TitlePLUS policies more accessible to lawyers and their clients.

Web-based access

In 2005, we made significant strides on expanding the web-based TitlePLUS system for mortgage-only transactions across the country. Scheduled for launch in early 2006 is an interactive, online program that lawyers in Western Canada can use to easily secure TitlePLUS coverage for purchases; the web-based program has been tailored to the unique underwriting and conveyancing needs of lawyers in each of the four western jurisdictions. As well, we secured TitlePLUS licences for the

Yukon, Northwest Territories and Nunavut; rollout of the program in these areas is planned for early 2006.

These initiatives have contributed to a steady growth in the TitlePLUS presence nationally. Despite a five per cent decline in the resale and new home market in Ontario, the TitlePLUS business grew.

A significant share of that growth came from Western Canada: Close to 25 per cent of the 3,200 lawyers who are TitlePLUS subscribers are located outside Ontario. Of the 800 lawyers who used a TitlePLUS policy for the first time in 2005, 360 were outside Ontario. Based on our Ontario experience, we expect the launch of a web-based TitlePLUS purchase system in the West will translate into significantly higher policy volumes from these jurisdictions in 2006.

A national, Bar-related Canadian presence

“Proudly made in Canada” has been very much part of our branding since the TitlePLUS launch in 1997. Our Canadian roots set us apart from our competitors in our promotional materials, in our presentations to members of the legal community across the country, and in our meetings with government officials.

Equally important and effective has been our emphasis on personal service. In 2005, our five consultants traveled coast to coast providing more than 900 law firms with in-office demonstrations on how to integrate TitlePLUS programs into their practices. Our analysts and underwriters

are often singled out for praise for the legal expertise and responsiveness they bring to their work; they responded to more than 40,600 calls and inquiries in 2005. We participated in and/or sponsored close to 160 events to bring the TitlePLUS message to lawyers, real estate agents, consumers and the lending community in all regions.

The TitlePLUS program has its roots in a need to counter the introduction of American-style title insurance models in conveyancing. It was developed by the real estate bar, for the real estate bar. Ongoing initiatives by lenders and other title insurers to develop processes that ultimately diminish the role of the real estate lawyer reinforce the need for a TitlePLUS program. Developing a national TitlePLUS presence not only addresses the needs of the lending community for this type of service, but also strengthens the ability of the real estate bar to thwart further attempts to undermine the viability of real estate practice.

This need was reinforced in 2005 in a series of extensive consultations with Canada Mortgage and Housing Corporation and others who were exploring the use of title insurance in their insured mortgage portfolios. We used this opportunity to reinforce the benefits of working with a uniquely Canadian title insurer, and the importance of the real estate lawyer as trusted advisor and fiduciary in a real estate transaction. We are confident that our representations have encouraged these organizations to consider carefully both their processes and potential suppliers of title insurance.



Financial Report 2005

management discussion and analysis

Statement of Income

In 2005, the Company generated net income of \$7.3 million, an increase of \$1.2 million over 2004. Income before taxes increased by \$1.8 million to \$10.9 million. Underwriting loss increased by \$1.7 million, offset by an increase of \$3.6 million in investment income.

Net premiums earned

Premiums earned, net of reinsurance ceded, decreased by \$1.3 million to \$72.8 million in 2005. Effective January 1, 2005, the Company ceased underwriting of the Law Society of Newfoundland's professional liability insurance program. While both the optional Excess and title insurance programs experienced growth in the year, premiums from the mandatory Ontario professional liability insurance program were stable.

Net claims and adjustment expenses

Overall, incurred claims and adjustment expenses, net of reinsurance recoveries are consistent with the prior year. During 2005, there was favourable development of prior years' claims in the amount of \$8.6 million.

Reinsurance

The Company has purchased excess of loss reinsurance coverage for 2005, which limits its exposure to large aggregation of multiple claims arising from the same proximate cause. The optional Excess program continues to be fully reinsured, removing exposure to the Company from claims in this program.

Prior to January 1, 2003, the Company had quota share reinsurance arrangements on the mandatory Ontario professional liability insurance program.

General expenses

The increase in general expenses in 2005 over 2004 is as anticipated, with personnel-related costs accounting for a significant portion of the increase.

Commissions earned

The Company earns commissions on premium ceded in respect of reinsurance of its optional Excess insurance program. In addition, the Company earns commissions for profitable results on the quota share reinsurance arrangements that it had prior to January 1, 2003. The increase in commissions earned of \$0.4 million primarily relates to increased profit commissions in 2005.

Investment income

Income generated from investments increased by \$3.6 million in 2005. Investment income includes net capital gains of \$6.3 million realized on disposition of assets (\$4.3 million in 2004). At December 31, 2005 the market value of the investment portfolio exceeds book value by \$14.0 million (\$12.6 million in 2004).

Balance Sheet

Shareholder's equity increased by \$7.3 million, the net income earned during the year.

Investments

Investment assets, inclusive of cash and cash equivalents, increased by \$36.9 million to \$343.6 million at December 31, 2005. The increase was primarily the result of cash provided by operations and investment income generated by the portfolio. The investment portfolio is managed in accordance with investment policy approved by the Company's Board of Directors in diversified, high quality assets. A portion of the investment portfolio, comprising primarily fixed income securities, is invested in a manner that is expected to substantially match in maturity to the payment of claim liabilities in future.

The portion of the Company's investment portfolio, which is considered surplus to the requirements of settling claim liabilities, is managed separately and includes fixed income securities and equity investments in publicly traded companies, the values of which are 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 has increased by \$5.8 million. Reinsurance recoveries have declined by \$18.0 million and accordingly the net increase in the provision is \$23.8 million. Much of this growth arises from the changes in reinsurance arrangements made since 2002. The percentage ceded under quota share reinsurance in respect of the Ontario mandatory professional liability insurance program declined from 57% in 1995 to nil effective January 1, 2003.

The determination of the provision of unpaid claims and adjustment expenses involves significant estimation. The process of determination of the provision is based on known facts currently available, interpretations and judgments and is influenced by factors that are inherently variable.

management discussion of risk

The Company is exposed to various risks in its business activities. Accordingly, we take care to recognize, assess and manage the risks taken by the organization. The principal risks inherent in our operations are described below.

Product design and pricing risk

Insurance industry and practice environment changes are regularly assessed to ensure appropriate coverage and limits are available at an affordable cost for the insured and an acceptable return for the Company.

The process of designing and pricing products includes the estimation of many factors including future investment yields, claims experience, and expenses. Product design and pricing risk is the risk that actual experience will not match the assumptions made at the time pricing was determined, and as a result, financial losses will occur. The risk is managed through detailed scenario analysis, and testing for acceptable results within a range of possible outcomes.

Claims management

Claims management is the procedure by which an insurance company determines the validity and amount of a claim. Effective claims management through prompt handling of files and use of expertise is fundamental to the success of our business. Claims trends are monitored on an ongoing basis so that timely and appropriate actions can be taken to minimize costs. Risk management efforts are also used to educate the profession and lower the risk of future claims.

The process of quantifying claim liabilities necessarily requires estimation of future costs and outcomes. Factors such as settlement patterns, litigation trends, claims payment patterns, claims severity and claims frequency may have an impact on the actual claims experience.

Investment portfolio risk

A significant portion of the Company's assets is held in the investment portfolio. Income generated by the portfolio is used to meet claims obligations and contributes to the Company's net income. There is the risk that our investment objectives, which are affected by general economic conditions beyond our control, will not be achieved. In an effort to limit investment risk, claims obligations are matched with investment assets which have maturities that roughly mirror their expected payment.

The Company engages professional investment managers who manage the portfolio in accordance with specific investment mandates consistent with the goals of the organization. Performance is monitored on a regular basis.

Reinsurance risk

The Company's reliance on reinsurance has decreased in recent years. However, a significant portion of the existing provision for unpaid claims continues to be reinsured as a result of our arrangements in past years. Reinsurance in itself does not relieve us of our liability to insureds. Should a third party reinsurer become insolvent, the Company's results and financial position could be negatively affected. To minimize the risk of potential default, reinsurers participating in our programs must pass stringent financial quality thresholds and are subject to annual reviews.

Regulatory and legislative compliance

The Company is provincially licensed to provide insurance and is subject to legislative rules and regulations. These regulations, designed to protect the insured, are becoming increasingly complex, and cover a wide range of areas including complaints resolution, privacy, solvency standards, investment restrictions, adequacy of reserves, and financial reporting. Failure to comply with applicable laws or regulations could result in the imposition of fines or significant restrictions on our ability to conduct business. Management keeps abreast of changes in regulatory requirements and has systems in place to ensure compliance.

Capital management

The Company has procedures to ensure that there is adequate capital to meet statutory requirements with appropriate safety margins. Forecasting models and sensitivity analysis are used to establish whether expected results will conform to industry norms. All significant financial initiatives are subject to stress tests to ensure compliance with solvency and capital requirements.

Operational risk

Operational risk is the risk of loss resulting from inadequate or failed processes, technology, or human performance. We endeavour to minimize operational risk by ensuring that effective infrastructure, controls, systems and individuals are in place. Internal controls, consisting of policies and procedures established and maintained by management, are in place to ensure the orderly and efficient conduct of our business. These controls are regularly reviewed and updated to follow best business practices and to minimize unintended practices or events from taking place.

Reputation

The biggest risk that any company faces is the loss of its good name. We strive to operate at the highest levels of professionalism, integrity and good practice.

management statement on responsibility for financial information

The preparation of the annual financial statements, Management's Discussion and Analysis (MD&A) and all other information in the Company's Annual Report is the responsibility of the Company's management and has been approved by the Board of Directors.

The financial statements have been prepared in accordance with Canadian generally accepted accounting principles. Financial statements, by their very nature, include amounts and disclosures based on estimates and judgments. Where alternative methods or interpretations exist, management has chosen those it deems most appropriate in the circumstances, including appropriate consideration to relevance and materiality. Actual results in the future may differ materially from management's current assessment given the inherent variability of future events and circumstances. Financial information appearing elsewhere in the Company's Annual Report is consistent with the financial statements.

Management maintains the necessary system of internal controls over financial reporting to meet its responsibility for the reliability of the financial statements. These controls are designed to provide management with reasonable assurance that the financial records are reliable for preparing financial statements and other financial information, assets are safeguarded against unauthorized use or disposition and liabilities are recognized.

The Board of Directors is responsible for ensuring that management fulfils its responsibilities for financial reporting and is ultimately responsible for reviewing and approving the financial statements. The Board carries out its responsibility, primarily through its Audit Committee, which is independent of management. The Audit Committee reviews the financial statements and recommends them to the Board for approval. The Audit Committee also reviews and monitors the Company's system of internal controls over financial reporting in the context of reports made by management or the external auditors.

Role of the Auditor

The external auditors, Deloitte and Touche LLP, have been appointed by the shareholder. Their responsibility is to conduct an independent and objective audit of the financial statements in accordance with Canadian generally accepted auditing standards, and to report thereon to the Company's shareholder. In carrying out their audit, the auditors make use of the work of the appointed actuary and his report on the policy liabilities of the Company. The external auditors have full and unrestricted

access to the Audit Committee and the Board of Directors to discuss audit, financial reporting and related findings. The auditors' report outlines the scope of their audit and their opinion.

Role of the Appointed Actuary

The actuary is appointed by the Board of Directors of the Company. With respect to the preparation of these financial statements, the appointed actuary is required to carry out a valuation of the policy liabilities and to report thereon to the Company's shareholder. The valuation is carried out in accordance with accepted actuarial practice and regulatory requirements. 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 regulators. The policy liabilities consist of a provision for unpaid claims and adjustment expenses on the expired portion of policies, a provision for future obligations on the unexpired portion of policies, and other policy liabilities that may be applicable to the specific circumstances of the Company.

In performing the valuation of the policy liabilities, which are by their very nature inherently variable, the appointed actuary makes assumptions as to the future rates of claims severity, inflation, reinsurance recoveries, expenses and other matters, taking into consideration the circumstances of the Company and the nature of the insurance coverage being offered. The valuation is necessarily based on estimates; consequently, the final values may vary significantly from those estimates. The appointed actuary also makes use of management information provided by the Company, and uses the work of the auditor with respect to the verification of the underlying data used in the valuation.

Toronto, Ontario
January 30, 2006



Michelle Strom
President and CEO



Akhil J. Wagh
Vice-President, Finance and Treasurer

auditors' report

Deloitte.

To the Shareholder of Lawyers' Professional Indemnity Company

We have audited the balance sheet of Lawyers' Professional Indemnity Company as at December 31, 2005 and the statements of income and retained earnings and of cash flows for the year then ended. These financial statements are the responsibility of the Company's management. 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 plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2005 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Toronto, Ontario
January 30, 2006

Deloitte & Touche LLP
Chartered Accountants

appointed actuary's report

INTERNATIONALLY MILLIMAN GLOBAL



Eckler Partners Ltd.
Consultants and Actuaries

To the Shareholder of Lawyers' Professional Indemnity Company

I have valued the policy liabilities of the Lawyers' Professional Indemnity Company for its balance sheet as at 31 December 2005, and their changes in its statement of income and retained earnings for the year then ended, in accordance with accepted actuarial practice, including selection of appropriate assumptions and methods.

In my opinion, the amount of the policy liabilities makes appropriate provision for all policyholder obligations, and the financial statements fairly present the results of the valuation.

Toronto, Ontario
January 30, 2006

B. G. Pelly

Brian G. Pelly
Fellow, Canadian Institute of Actuaries

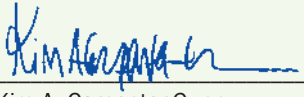
balance sheet

Stated in thousands of Canadian dollars
As at December 31

	2005	2004
Assets		
Cash and cash equivalents	1,820	27,721
Investments (note 2)	341,812	278,978
Investment income due and accrued	3,056	1,781
Due from reinsurers	7,695	12,145
Due from insureds	2,222	2,822
Reinsurers' share of provisions for:		
Unpaid claims and adjustment expenses (note 4)	79,650	97,663
Other receivable	1,032	882
Other assets	307	386
Capital assets (note 3)	589	729
Income taxes recoverable	—	3,224
Future income taxes (note 7)	6,177	5,495
Total assets	444,360	431,826
Liabilities		
Provision for unpaid claims and adjustment expenses (note 4)	321,689	315,845
Due to reinsurers	754	815
Due to insureds	1,467	2,008
Due to the Law Society of Upper Canada (note 5)	5,708	5,976
Expenses due and accrued	3,439	3,829
Income taxes due and accrued	64	—
Other taxes payable	954	478
Unearned premiums	664	589
	334,739	329,540
Shareholder's Equity (note 8)		
Capital stock issued and paid	5,000	5,000
Contributed surplus	30,645	30,645
Retained earnings	73,976	66,641
	109,621	102,286
Total liabilities and shareholder's equity	444,360	431,826

See accompanying notes to financial statements

On behalf of the Board


Kim A. Carpenter-Gunn
Director


Michelle L.M. Strom
Director

statement of income and retained earnings

Stated in thousands of Canadian dollars
Year ended December 31

	2005	2004
Premiums earned – gross	77,388	79,342
Premiums earned – ceded	(4,632)	(5,304)
Net premiums earned	72,756	74,038
Net claims and adjustment expenses (note 4)	69,686	69,265
Premium taxes	2,325	2,405
General expenses	13,446	12,953
Commissions earned	(3,205)	(2,803)
	82,252	81,820
Underwriting loss	(9,496)	(7,782)
Investment and other income	20,388	16,836
Income before income taxes	10,892	9,054
Income tax expense/(recovery) (note 7)		
Current	4,239	4,231
Future	(682)	(1,265)
Net income for the year	7,335	6,088
Retained earnings, beginning of year	66,641	60,553
Retained earnings, end of year	73,976	66,641

See accompanying notes to financial statements

statement of cash flows

Stated in thousands of Canadian dollars

Year ended December 31	2005	2004
Operating Activities		
Net income	7,335	6,088
Items not affecting cash:		
Future income taxes	(682)	(1,265)
Amortization of capital assets	469	684
Realized gains	(6,282)	(4,338)
Amortization of premiums and discounts on bonds	(788)	101
	52	1,270
Change in non-cash balances:		
Other taxes payable	476	(257)
Income taxes due and accrued	3,288	(4,694)
Due to/from reinsurers and insureds	4,448	(314)
Provision for unpaid claims and adjustment expenses	5,844	17,798
Reinsurers' share of provisions	18,013	11,998
Unearned premiums	75	(3)
Expenses due and accrued	(390)	679
Investment income due and accrued	(1,275)	138
Other receivables	(150)	144
Other assets	79	(66)
Due to/from the Law Society of Upper Canada	(268)	12,429
Net cash inflow from operating activities	30,192	39,122
Investing Activities		
Purchase of capital assets	(329)	(337)
Purchase of investments	(129,010)	(174,368)
Proceeds of sale of investments	73,246	154,101
Net cash outflow from investing activities	(56,093)	(20,604)
Increase/(decrease) in cash and cash equivalents during the year	(25,901)	18,518
Cash and cash equivalents, beginning of year	27,721	9,203
Cash and cash equivalents, end of year	1,820	27,721
Cash and cash equivalents at end of year consists of:		
Cash	676	4,775
Cash equivalents	1,144	22,946
	1,820	27,721

See accompanying notes to financial statements

notes to financial statements

As at December 31, 2005

Amounts stated in thousands of Canadian dollars (except per share amounts)

Lawyers' Professional Indemnity Company (the "Company") is an insurance company, incorporated in Ontario and licensed to provide lawyers' professional liability insurance and title insurance. The Company is a wholly-owned subsidiary of the Law Society of Upper Canada ("LSUC"), which is the governing body of lawyers in Ontario.

1. Significant Accounting Policies

These financial statements have been prepared under the Insurance Act of Ontario (the "Act") and related regulations which require that except as otherwise specified by the Company's regulator, the Financial Services Commission of Ontario ("FSCO"), the financial statements of the Company are to be prepared in accordance with Canadian generally accepted accounting principles. The significant accounting policies used in the preparation of these financial statements are summarized below. These accounting policies conform, in all material respects, to Canadian generally accepted accounting principles.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, balances with banks, and short-term investments with maturities of three months or less at the time of acquisition. The fair value of cash and cash equivalents approximates the amounts shown in the financial statements.

Investments

The Company carries its investments in debt securities at amortized cost with premiums and discounts on the par value of the securities amortized on a straight-line basis over the term to maturity. Investments in common and preferred shares are carried at cost. Realized gains and losses on investments are calculated using the carrying value of securities sold.

Investment income includes interest and dividends earned, amortization of premiums and discounts on debt securities and realized gains and losses. Any loss in value of an investment, which is considered other than temporary in nature, is also recognized in income.

Capital assets

Capital assets are carried at amortized cost. Amortization is charged to expense on a straight-line basis over the estimated useful lives of the assets as follows:

Leasehold improvements	Term of lease
Furniture and equipment	3 to 5 years
Computer equipment and software	1 to 3 years

Premium-related balances

Insurance policies under the professional liability insurance program are effective on a calendar year basis. Professional liability insurance premium income is earned on a *pro-rata* basis over the term of coverage of the underlying insurance policies; generally one year, except for policies for retired lawyers, which have terms of up to five years. The portion of premiums related to the unexpired term of coverage at the balance sheet date is recorded as unearned premiums.

Title insurance premiums are earned at the inception date of policies.

Premiums receivable are recorded as amounts due from insureds in the balance sheet, net of any required provision for doubtful amounts. Premiums received from insureds in advance of the effective date of the insurance policy are recorded as amounts due to insureds in the balance sheet.

The Company defers policy acquisition costs, primarily premium taxes on its written professional liability insurance premiums, to the extent these costs are considered recoverable. These costs are expensed on the same basis that the related premiums are earned. The method to determine recoverability of deferred policy acquisition costs takes into consideration future claims and adjustment expenses to be incurred as premiums are earned and anticipated investment income. Deferred policy acquisition costs are not considered material at year-end.

Other income

Other income is miscellaneous income other than premium income or investment income and is recognized when it is earned.

Claims-related balances

a) Provision for unpaid claims and adjustment expenses

The provision for unpaid claims and adjustment expenses is based on an estimate of the ultimate cost of all insurance claims as at the balance sheet date, and is determined using case-basis evaluations and an amount for the expected future development of claims incurred as at the balance sheet date. The provision takes into account the time value of money.

b) Deductibles

The professional liability insurance policy requires insureds to pay deductibles to the maximum extent of \$25 each on individual claims. Expected deductible recoveries on paid and unpaid claims are recognized net of any required provision for uncollectible accounts at the same time as the related claims liability.

notes to financial statements

As at December 31, 2005

Amounts stated in thousands of Canadian dollars (except per share amounts)

Reinsurance

Net premiums earned and claims incurred are recorded net of amounts ceded to, and recoverable from, reinsurers in the statement of income.

Amounts relating to reinsurance in respect of the premiums and claims related balances in the balance sheet are recorded separately. Amounts recoverable from reinsurers are estimated and recognized in a manner consistent with the Company's method of determining the related policy liability associated with the reinsurance policy.

Employee future benefits

The Company maintains a defined contribution pension plan for its employees as well as a supplemental defined benefit pension plan for certain designated employees which provides benefits to those employees in excess of the benefits provided by the Company's defined contribution pension plan. The benefit liability under the supplemental defined benefit pension plan is actuarially determined using the projected benefit method pro-rated on service and management's assumptions about discount rates, expected plan assets' performance, salary growth and retirement ages of employees. The discount rate is determined on the basis of market conditions at year-end and other assumptions are based on long term expectations.

Adjustments for plan amendments, changes in assumptions and actuarial gains and losses are recognized fully into income in the year to which they relate.

Income taxes

The Company uses the asset and liability method of accounting for income taxes. Under this method of tax allocation, future income tax assets and liabilities are determined based on the differences between the financial reporting and tax basis of assets and liabilities, and are measured using the tax rates and laws that are expected to be in effect in the periods in which the future income tax assets or liabilities are expected to be settled or realized, where those tax rates and laws have been substantively enacted.

Use of estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses

during the year. Actual results could differ from these estimates, and changes in estimates are recorded in the year in which they are determined. The most significant assets and liabilities which require estimation in their determination are the provision for unpaid claims and adjustments and reinsurers' share thereof (note 4).

2. Investments

The Company holds a diversified portfolio consisting of equities and fixed income debt securities with investment grades of "BBB" or better.

Estimated fair values and unrealized gains and losses

The carrying value, estimated fair value, yield and unrealized gains (losses) on investments at December 31 were as follows:

	2005			
	Carrying Value	Unrealized Gains	Unrealized Losses	Estimated Fair Value
Debt Securities	\$ 293,913	6,838	—	300,751
Common Shares	45,300	8,462	(1,448)	52,314
Preferred Shares	2,599	129	—	2,728
	<u>\$ 341,812</u>	<u>15,429</u>	<u>(1,448)</u>	<u>355,793</u>

	2004			
	Carrying Value	Unrealized Gains	Unrealized Losses	Estimated Fair Value
Debt Securities	\$ 240,247	6,042	(29)	246,260
Common Shares	36,132	7,255	(863)	42,524
Preferred Shares	2,599	154	—	2,753
	<u>\$ 278,978</u>	<u>13,451</u>	<u>(892)</u>	<u>291,537</u>

The effective yield on debt securities as at December 31, 2005 is 4.21% (2004: 4.50%).

The estimated fair values of debt securities, common and preferred shares are based on quoted market values.

notes to financial statements

As at December 31, 2005

Amounts stated in thousands of Canadian dollars (except per share amounts)

Liquidity and interest rate risk

The maturity profile of debt securities as at December 31, 2005 is as follows:

	Within 1 Year	1 to 5 Years	Over 5 Years	Carrying Value
Debt Securities	\$ 33,304	146,400	114,209	293,913
Percent of total	11%	50%	39%	

The weighted average duration of debt securities at December 31, 2005 is 5.18 years (2004: 4.40 years). A portion of these debt securities is invested in a manner that substantially matches their duration to the expected duration over which the provision for claims and adjustment expenses is payable in future. Shares have no specific maturities.

3. Capital Assets

	2005			2004
	Cost	Accumulated Amortization	Carrying Value	Carrying Value
Furniture & Fixtures	\$ 1,151	(1,081)	70	99
Computer Equipment	2,342	(2,068)	274	281
Computer Software	2,214	(2,038)	176	244
Leasehold Improvements	933	(864)	69	105
Total	\$ 6,640	(6,051)	589	729

4. Provision for Unpaid Claims and Adjustment Expenses

The determination of the provision for unpaid claims and adjustment expenses is a complex process based on known facts, interpretations and judgment and is influenced by a variety of factors. Consequently, the measurement of the ultimate settlement costs of claims made to date that underlies the provision for unpaid claims and adjustment expenses and any related recoveries for reinsurance and deductibles, involves estimates and measurement uncertainty. The amounts are based on estimates of future trends in claim severity and other factors, which could vary as claims are settled.

Variability can be caused by several factors including the emergence of additional information on claims, changes in judicial interpretation, and significant changes in severity or frequency of claims from historical trends. Ultimate costs incurred could vary

from current estimates. Although it is not possible to measure the degree of variability inherent in such estimates, management believes that the methods of estimation that have been used will produce reasonable results given the current information. An actuary performs a valuation of claim liabilities at least annually. As adjustments to estimated claim liabilities become necessary, they are reflected in current operations.

To limit losses through the spreading of risks, the Company cedes reinsurance to other insurers. In the event that a reinsurer is unable to meet obligations assumed under reinsurance agreements, the Company is liable for such amounts. The Company has guidelines and a review process in place to ascertain the credit worthiness of the companies to which it cedes. Based on current information of the financial health of the reinsurers, no provision for doubtful debts has been made in the financial statements in respect of reinsurers.

Changes in provisions for unpaid claims and adjustment expenses recorded in the balance sheet comprise the following:

	2005	2004
Provision for unpaid claims and adjustment expenses - beginning of year - net	\$ 218,182	188,386
Change in provision for claims and adjustment expenses:		
Prior years	(8,638)	(5,771)
Current year	78,333	77,575
Claims and adjustment expenses paid in relation to:		
Prior years	(39,933)	(35,094)
Current year	(5,796)	(5,279)
Impact of Discounting	(109)	(1,635)
Provision for unpaid claims and adjustment expenses - end of year - net	242,039	218,182
Reinsurers' share of provision for unpaid claims and adjustment expenses	79,650	97,663
Provision for unpaid claims and adjustment expenses - end of year - gross	\$ 321,689	315,845

As the provision for unpaid claims and adjustment expenses is recorded on a discounted basis and reflects the time value of money, its carrying value is expected to provide a reasonable basis for the determination of fair value. However, determination

notes to financial statements

As at December 31, 2005

Amounts stated in thousands of Canadian dollars (except per share amounts)

of fair value also requires the practical context of a buyer and seller, both of whom are willing and able to enter into an arm's length transaction.

5. Related Party Transactions

Pursuant to a service agreement implemented January 1, 1995, the Company administers the Errors and Omissions Insurance Fund (the "Fund") of the LSUC and provides all services directly related to the operations and general administration of the Fund in consideration for LSUC insuring its mandatory professional liability insurance program with the Company.

The insurance policy under the mandatory professional liability insurance program of the LSUC is written by the Company and is effective on a calendar year basis. The insurance policy is renewed effective January 1 each year subject to the LSUC's acceptance of the terms of renewal submitted by the Company.

For the year ended December 31, 2005, 88% of the premiums written related to mandatory insurance coverage provided to LSUC and its members. Under the insurance policy in force between July 1, 1990, and December 31, 1994, the Company is responsible for claims in excess of LSUC and member deductibles. The provision for unpaid claims and adjustment expenses is net of amounts relating to policies for years prior to 1995 that are payable by the LSUC.

Commencing January 1, 1995, there is no longer the LSUC deductible and 100% of the risk over the individual member deductible is insured through the Company. The annual policy limits for each of the years effective January 1, 1995, to December 31, 2005, are \$1,000 per claim and \$2,000 in aggregate per member.

In 2005, the Company refunded \$7,027 (2004: \$5,071) in premiums to the LSUC pursuant to the retrospective premium rating provisions of its insurance policy. These amounts are held in the Fund for future insurance purposes.

6. Employee Future Benefits

The Company has a defined contribution pension plan which is available to all its employees upon meeting the eligibility requirements. Each employee is required to contribute 4.5% of yearly maximum pensionable earnings and 6% in excess thereof, of an employee's annual base earnings. Under the plan, the Company matches all employee contributions. The Company made payments of \$385 in 2005 (2004: \$345) and recorded pension expense of \$394 (2004: \$353).

The Company also has a supplemental defined benefit pension plan. Funding for the supplemental plan commenced in 2005. Funding requirements are reviewed annually with an actuarial valuation for funding purposes effective as at December 31. The most recent actuarial valuation for funding purposes was at an effective date of December 31, 2004. For reporting purposes, all assets and liabilities associated with pension benefits have been measured using values as at December 31, 2005.

Defined benefit plan obligations

	2005	2004
Accrued benefit obligation		
Balance, beginning of year	\$ 1,264	697
Current service cost	110	103
Interest cost	79	69
Actuarial loss	252	140
Plan amendments	—	255
Balance, end of year	\$ 1,705	1,264

Defined benefit plan assets

	2005	2004
Fair value of plan assets		
Market value of plan assets - beginning of year	\$ —	—
Actual return on plan assets, net of expenses	8	—
Employer contribution	636	—
Market value of plan assets - end of year	\$ 644	—

The defined benefit plan assets arise primarily from employer contributions that are originally allocated equally between deposits held with the Government of Canada and investments in the units of a balanced pooled fund, representing a portfolio mix of equities and debt securities.

Reconciliation of funded status surplus (deficit) of the benefit plans to the amounts recorded in the financial statements

	2005	2004
Fair value of plan assets	\$ 644	—
Accrued benefit obligation	(1,705)	(1,264)
Funded status deficit	(1,061)	(1,264)
Unamortized net actuarial loss	259	—
Accrued benefit liability	\$ (802)	(1,264)

The accrued benefit liability is included in expenses due and accrued in the Company's balance sheet.

notes to financial statements

As at December 31, 2005

Amounts stated in thousands of Canadian dollars (except per share amounts)

Components of defined benefit costs recognized in the year

	2005	2004
Current service cost	\$ 110	103
Interest cost	79	69
Actual return on assets	(8)	—
Actuarial losses	252	140
Past service costs	—	255
Difference between actual and recognized actuarial losses	(252)	—
Difference between actual and expected return on assets	(8)	—
Defined benefit costs recognized in the statement of income	\$ 173	567

The significant assumptions used by the Company are as follows (weighted average):

	2005	2004
Discount rate	5.00%	5.75%
Expected long term rate of return on plan assets	6.00%	6.00%
Rate of compensation increase	3.50%	3.50%
Estimated average remaining service life	11.0 years	12.0 years

7. Income Taxes

The Company's effective tax rate does not differ significantly from the applicable Canadian statutory income tax rate of 36.12%.

The Company's future income tax asset is the result of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The sources of these temporary differences and the tax effects for each year are as follows:

	2005	2004
Investments	\$ 1,376	987
Claim liabilities	4,371	3,940
Other	430	568
Total	\$ 6,177	5,495

During the year the Company made payments of \$4,188 to and received refunds of \$3,236 from tax authorities.

8. Shareholder's Equity

Capital stock of the Company represents:

- 30,000 Common Shares of par value of \$100 each – authorized, issued and paid.
- 20,000 6% non-cumulative, redeemable, non-voting Preferred Shares of par value of \$100 each – authorized, issued and paid.

9. Statutory Insurance Information

The Company is the beneficiary of a trust account in the amount of \$7,605 (2004: \$7,483) which is held as security for reinsurance ceded to unregistered reinsurers. This trust balance is not reflected in these financial statements but is considered in determining statutory capital requirements.

In accordance with licensing requirements, the Company has deposited securities with the regulatory authorities having a market value of \$57 (2004: \$334).

10. Operating Lease Rentals

The Company is committed to monthly lease payments in respect of the premises from which it operates. The lease expires on January 31, 2008. Lease payment obligations are as follows:

2006	\$ 1,362
2007	1,362
2008	114

11. Fair Value Disclosure

The fair value of the Company's financial assets and liabilities other than investments (note 2) and the provision for unpaid claims and adjustment expenses (note 4) approximates their carrying value.

12. Comparative Information

Certain comparative amounts have been reclassified to conform to the current year's financial statement presentation.

board of directors



Kim A. Carpenter-Gunn*
Chairman, LawPRO Board of Directors;
Partner, Waxman, Carpenter-Gunn

Abdul A. Chahbar*
Councillor,
City of London

Malcolm L. Heins
CEO,
Law Society of Upper Canada

Laurie H. Pawlitz*
Partner,
Goodman and Carr LLP

Ian D. Croft
Vice-Chairman, LawPRO Board of Directors;
Chartered Accountant

Douglas F. Cutbush
Insurance Consultant,
Arbitrator & Mediator

Rita Hoff
Vice-President & Director,
Canaccord Capital Corporation

Michelle L.M. Strom
President & CEO,
LawPRO

George D. Anderson
Retired President and Chief Executive Officer,
Insurance Bureau of Canada

Lawrence A. Eustace
Principal,
Lawrence A. Eustace

William G. Holbrook
President,
W.G. Holbrook & Associates Inc.

Gerald A. Swaye, Q.C.*
Principal,
Gerald A. Swaye & Associates

Constance B. Backhouse*
Professor, Faculty of Law,
University of Ottawa

Frederick W. Gorbet
Principal,
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