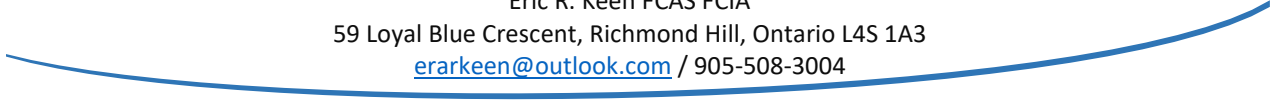


# **Canadian Lawyers Liability Assurance Society**

## **External Peer Review of the December 31, 2023 Valuation Report February 12, 2024**

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# Introduction and Scope

## Purpose

I have been retained by the Canadian Lawyers Liability Assurance Society (CLLAS) to complete a peer review of the December 31, 2023 valuation report completed by Ms. Julie-Linda Laforce FCAS FCIA of Axxima. In performing the peer review of the report, I have the following objectives:

- Assist CLLAS in its review of the valuation results recommended by Axxima.
- Be of benefit to CLLAS and Axxima by providing (i) a source of independent consultation advice, and (ii) an additional source of professional education: This aids in narrowing the range of practice by Axxima and improving the quality of their work.
- Satisfy the policy to have a review of the valuation every three years.

My name is Eric R. Keen, and I am a fellow in good standing of the Canadian Institute of Actuaries (CIA). When conducting reviews, I do not warrant or opine on the company's assets, liabilities, or ability to perform on obligations. Instead, I review the actuary's work for reasonableness within the standards of practice of the CIA.

My business address is:

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The intent of this report is to review the model and outline differences I may have with its components, assumptions, and procedures. It is not the intent of this report to come up with alternative valuation estimates.

## **Distribution and Use**

This report should be read in its entirety. This report is intended to be given to company management at CLLAS, its regulators, its auditor and to Axxima. It is not to be relied upon by any other person or entity or used for any other purpose. Eric R. Keen FCAS FCIA assumes no responsibility for the information provided to him by CLLAS or Axxima or for use by or disclosure to any other persons or entities for any other purpose.

## **Reliance**

I relied on CLLAS and Axxima for the accuracy of the data.

## **Definitions**

In this report, the definition of Incurred but not Reported includes both development on outstanding case reserves and unreported claims. This is usually understood as the IBNR definition, broad form.

Actuarial policy liabilities refer to the policy liabilities valued based on accepted actuarial practice as defined by the Actuarial Standards Board. In particular, it recognizes the time value of money and the need for risk adjustments in valuing the policy obligations.

Policy liabilities include claims liabilities, premium liabilities, and other policy liabilities. Within the context of this report, claims liabilities refer to liabilities related to claims incurred on or before December the relevant valuation date. Premium liabilities refer to liabilities related to the unexpired portion of the policies in force at the relevant valuation date. Other policy liabilities relate to liabilities originating from policies, including reinsurance on same, written on or before the relevant valuation date, but not incurred in claims or premium liabilities.

## **Materiality**

The actuary selects a materiality standard of \$250,000, based on 4.1% of the net liability for incurred claims before payables and receivables. The auditor's materiality is \$720,000.

## Expression of Opinion

To the Canadian Lawyers Liability Assurance Society:

I have completed an external peer review of the December 31, 2023 Valuation of Policy Liabilities Report for the Canadian Lawyers Liability Assurance Society authored by the Appointed Actuary, Ms. Julie-Linda Laforce FCIA FCAS MAAA, dated January 17, 2024. My review was completed in accordance with accepted actuarial practice.

In my opinion,

- The work that I reviewed was performed in accordance with accepted actuarial practice;
- The procedures, systems and work of others relied upon were adequate for her work;
- The assumptions made and procedures employed were appropriate, and
- The report accurately describes the assumptions and methodology employed by the Appointed Actuary.

Signature

A handwritten signature in black ink, appearing to read 'Eric R. Keen', with a horizontal line drawn underneath it.

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Eric R. Keen, FCAS FCIA  
Consulting Actuary  
February 12, 2024

# Commentary and Approach

## Historical Background

CLLAS was formed in 1986 and licensed in Ontario as an insurer in 1987 with the first policies issued with an effective date of July 1, 1987. Effective July 1, 2012, CLLAS's lead regulator was changed from Ontario to Alberta. CLLAS is licensed in Alberta, British Columbia and Ontario, and since March 4, 2015, it is also licensed in Nova Scotia.

CLLAS provides professional liability insurance to subscribing law firms in excess of the compulsory coverage provided by the various law societies. Since inception, coverage provided by CLLAS has been on a claims-made basis. For the first policy term (i.e., July 1, 1987 to June 30, 1988), coverage was in excess of \$600,000. Coverage in subsequent policy terms is in excess of \$1,000,000.

On July 1, 2022 CLLAS introduced a Cyber Insurance policy of up to \$10,000,000 aggregate per insured firm. CLLAS retains the first \$1,000,000.

CLLAS cedes paid losses, case reserves and provisions for IBNR in three ways:

1. **Proportional reinsurance:** The amounts ceded to proportional reinsurance in each layer vary according to the reinsurance arrangements effective in each policy period.
2. **Aggregate reinsurance:** CLLAS's aggregate reinsurance with Colchester Reinsurance Limited ("Colchester") is applicable to its retention after reflection of proportional reinsurance. The amounts ceded to aggregate reinsurance vary according to the reinsurance arrangements effective in each policy period.
3. **Loss portfolio transfer:** At June 30, 2012, CLLAS entered into a loss portfolio transfer agreement with Colchester which covers all outstanding claim obligations on policies written between July 1, 1987 and June 30, 2012.

CLLAS's net obligations for losses and loss adjustment expenses are therefore limited to those on policy periods after June 30, 2012.

Further information on coverages offered, retentions and applicable reinsurance can be found on pages 6-9 of the report.

## **Previous Peer Reviews**

Summaries of the previous peer reviews in 2015, 2018 and 2021 are included on pages 12-13 of the report. According to Ms. Laforce, the recommendations were appropriately considered.

## **Comparison of Actual and Expected Experience**

Ms. Laforce tests the runoff of the estimates of the previous report and finds net favourable runoff of \$1,177k and attributes this to release of IBNR for the Cyber line and lower than expected claims emergence for professional liability. Gross runoff is also favourable at \$7,464k.

## **Liability for Incurred Claims (Professional Liability)**

As noted on page 18, the LIC is made up of Future Cash Flows, discounted for the time value of money reflecting timing, currency and liquidity, and including a risk adjustment factor.

With regard to claims, *“CLLAS becomes actively involved when the law society concedes that it is unlikely or unable to settle a matter within its available limits or exhausts its limits. The law society will frequently “tender” (i.e., control of the defence to CLLAS). CLLAS’s claims managers makes recommendations for their own indemnity reserves to the CLLAS Claims Committee based upon counsel assessments and/or damage expert report.”*

The IBNR component is estimated using the Bornhuetter Ferguson (B-F) method related to the anticipated development of expected losses based upon a separate study prepared by Axxima. In this study, professional liability expected losses are determined by fiscal year and by layer. This study was most recently completed March 23, 2023 and is beyond the scope of this review.

It is interesting to note that in most actuarial reports the B-F is usually applied to expected losses generated by the gross and net earned premiums times their respected loss ratios. Ms. Laforce prefers her approach stating, *“Using premiums as an input into the gross IBNR valuation is not reasonable or appropriate unless a pricing that is independent of market conditions can be obtained.”* Ms. Laforce’s approach is appropriate and reasonable.

Another input into the determination of the IBNR is the computation of loss development factors. In my opinion, the incurred loss development factors selected in Exhibit 1.3 should be higher, particularly for periods 78-90 and 90-102, if used to determine gross or ceded IBNR. Despite this observation, there appears to be sufficient conservatism in the expected losses to offset potentially higher loss

development factors. If the selected factors are used to determine net IBNR, they are likely to be conservative.

Ms. Laforce appropriately selected the payment patterns, discount curves and adjustments for the LIC and AIC. I have not checked these calculations as they are mechanical in nature, however the results appear reasonable.

The final ingredient in the LIC is the Risk Adjustment (RA) factor. Under IFRS 4, the actuary would normally decide upon this factor. IFRS 17 gives license to the insurance company to select the RA, which “reflects the compensation required by the entity to bear the uncertainty about the amount and timing of the cash flows that arise from non-financial risk.”

CLLAS selected the Margin approach was selected with the RA margin set at 9%. According to the actuary, the discounted reserves plus the RA results in a confidence interval of 65-70%.

The overall approach for determining the Asset for Incurred Claims is similar.

### **Liability for Remaining Claims (Professional Liability)**

Despite an expected loss ratio to unearned premiums of 104%, the LRC including attributable expenses on an IFRS 17 discounted basis is less than 100% (not onerous) and is underwritten on a 12 month basis and thus qualifies for PAA. Therefore, the treatment of LRC is straightforward and reasonable.

The ARC would have an even greater expected loss ratio, but Ms. Laforce points out “*ARC works interestingly that it can only be onerous if the LRC of CLLAS is onerous.*”

### **Cyber Insurance**

The Cyber insurance liabilities are much more straightforward. When queried about the factors used, Ms. Laforce stated: “*As mentioned in the report, we used actuarial judgment, we did some research and attended various continuing education sessions on cyber claims to help determine expected duration of this type of claim, etc. Having said that there is no industry claims database or CLLAS specific data used to derive these.*” This is reasonable.

### **Observation**

After the loss portfolio transfer and reinsurance by Colchester, admitted and non-admitted reinsurers, CLLAS net unpaid losses appear restricted to their retention of the drop-down layer of \$975k xs \$25k (where the first \$1m is covered by law



societies mandatory coverage) for when the mandatory retention does not respond. Ms. Laforce expects very low claims activity in this layer in the future. My assessment of the recommended net IBNR for professional liability for CLLAS is that it is quite conservative and likely to continue to produce favourable net runoff.

The following table compares gross and net expected losses, earned premiums and projected loss ratios in the report:

From	To	Gross Expect. Loss (1)	Gross Earned Prem. (2)	Expect. Loss Ratio (3)	Gross Ultimate Loss (4)	Proj. Loss Ratio (5)	Net Expect. Loss (6)	Net Earned Prem. (7)	Expect. Loss Ratio (8)	Net Ultimate Loss (9)	Proj. Loss Ratio (10)
2012-2	2013-1	16,622	14,229	117%	1,654	12%	506	3,352	15%	203	6%
2013-2	2014-1	14,738	13,954	106%	12,580	90%	457	3,155	14%	2	0%
2014-2	2015-1	15,503	12,896	120%	1,897	15%	483	2,452	20%	1,224	50%
2015-2	2016-1	14,770	12,439	119%	13,281	107%	464	2,414	19%	11	0%
2016-2	2017-1	15,074	10,610	142%	4,151	39%	483	2,177	22%	671	31%
2017-2	2018-1	13,408	7,138	188%	1,194	17%	419	2,014	21%	37	2%
2018-2	2019-1	14,126	7,391	191%	4,416	60%	452	1,873	24%	109	6%
2019-2	2020-1	15,884	9,288	171%	12,159	131%	475	1,995	24%	603	30%
2020-2	2021-1	15,864	10,667	149%	10,438	98%	485	2,016	24%	289	14%
2021-2	2022-1	15,980	12,593	127%	15,495	123%	511	2,010	25%	373	19%
2022-2	2023-1	16,238	14,320	113%	14,240	99%	526	2,294	23%	462	20%
2023-2	2024-1	8,489	8,271	103%	8,192	99%	275	1,139	24%	266	23%
2012-2	2024-1	176,696	133,797	132%	99,697	75%	5,536	26,891	21%	4,250	16%

(1) Exhibit 2

(2) Exhibit 3

(3) (1)/(2)

(4) Exhibit 3

(5) (4)/(2)

(6) Exhibit 2

(7) Exhibit 5

(8) (6)/(7)

(9) Exhibit 5

(10) (9)/(7)

## Peer Review Recommendations

The subject report follows accepted actuarial practice, and the results are not unreasonable.

1. I recommend the actuary revisit the selected incurred loss development factors for future reports, potentially using different factors for net and ceded IBNR.
2. I recommend an independent review of the annual pricing report.