

March 18, 2019

Plan Credit withheld for 2019. Premium increase of 5% continues for third year.

Continuing increases in claims expenses, increased length of time to reach settlements, and need to increase capital to meet regulatory requirements factor in the decisions.

PLAN CREDIT WITHHELD

Results for 2018 ended with a profit of \$730,000, a considerable improvement over last year's nominal profit of \$72,000. Despite the improved performance, the results were again impacted by a significant actuarial adjustment that increased the requirement for reserves for future unreported and unsettled claims to \$5.3 million, the highest in the Company's history. Two continuing issues identified by the actuary were:

- continuing growth in claims costs; and
- increase in the time it takes to reach a settlement of many claims.

Since the inception of the Indemnity Plan, over \$50 million has been returned to policyholders as a Plan Credit. However, the main issue facing Pro-Demunity today and for the foreseeable future will be the continuing need to

increase capital to enhance the Company's financial stability and meet regulatory requirements. Adding to this challenge is the scheduled introduction of new International Financial Reporting Standards for financial institutions starting in 2021.

In consequence, it is prudent to allocate any surplus to increase capital until this challenge has been met. Accordingly, the Plan Credit has been withheld to address this need.

The Plan Credit is based on the net profit for the last year after allowances for the retention of capital recommended by our independent actuary to comply with regulatory requirements and potential volatility in claims costs. The amount is distributed to policyholders in accordance with their pro-rata contribution towards that year's premium.

5% PREMIUM INCREASE CONTINUES FOR 2019

In response to the current and predicted need to increase the Company's capital to maintain an appropriate relationship between reserves for damages and claims expenses and its obligations to Ontario architects, Pro-Demunity has decided to continue the 5% increase in premiums for 2019.

As predicted last year, it is anticipated that the 5% increase will continue to be needed for several years until the aggregate premiums are sufficient to address

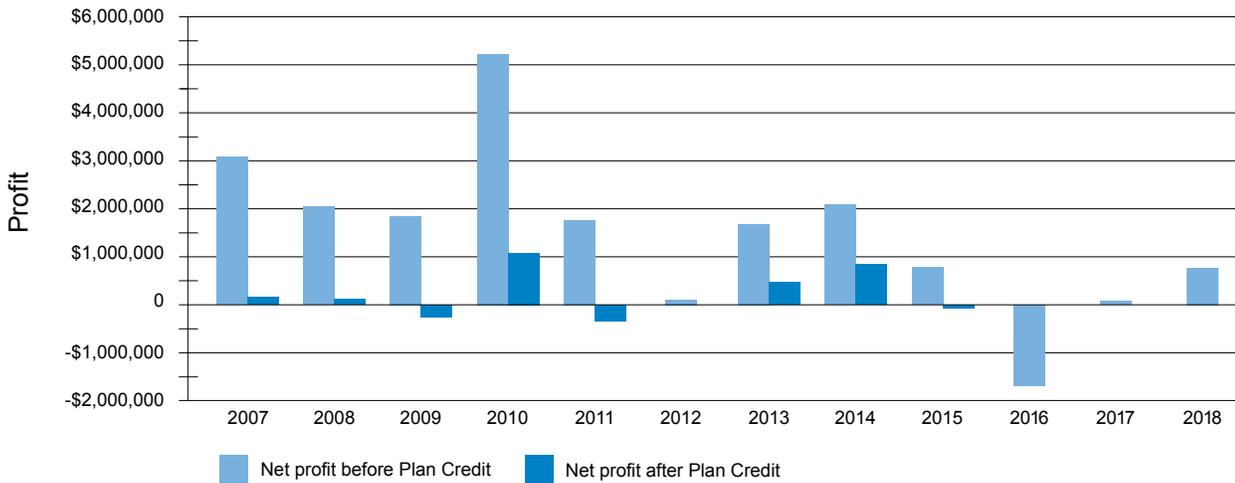
an annual claims exposure of about \$12.5 million. This approach will allow the Company to pay normal claims through annual premiums, and catastrophic losses by means of reinsurance and available capital.

In addition, as discussed above, the need for the Company to increase and maintain adequate capital to comply with regulatory requirements, including the new International Financial Reporting Standards, will continue upward pressure on premiums for the foreseeable future.

Refer to Graphs 1, 2 and 3 on the following pages.

GRAPH 1: NET PROFIT COMPARISON

Key facts: Profits have fluctuated dramatically in recent years. 2018 shows a return to profitability after a loss in 2016 and break even in 2017.



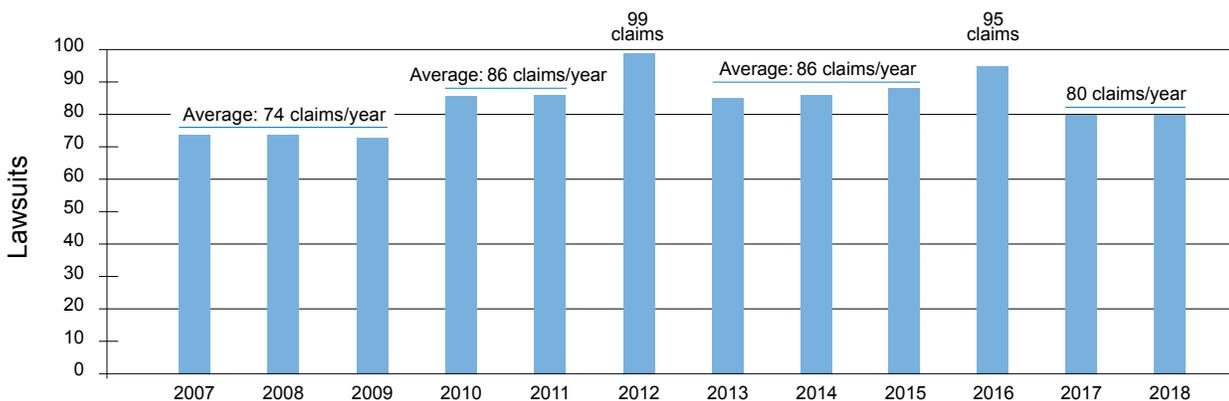
The Graph shows that in several prior years (2009, 2011, 2015) the funds allocated as a Plan Credit resulted in a minor loss; however, in each of those years there was a profit before a Plan Credit was determined. In 2016 there was an operating loss and no Plan Credit. In 2012, and 2017 there was no Plan Credit due to minimal net profit.

In 2018 there is no Plan Credit due to the need to increase the Company's capital.

Actuarial adjustments to reserves for claims expenses were significant factors impacting the results for 2016, 2017 and 2018. Refer to Graph 3.

GRAPH 2: NUMBER OF LAWSUITS

Key fact: Despite a spike in the numbers in 2012 and 2016, the number of lawsuits against architects has been relatively constant since 2010. Numbers for 2018 matched 2017 after the decline from the spike in 2016.



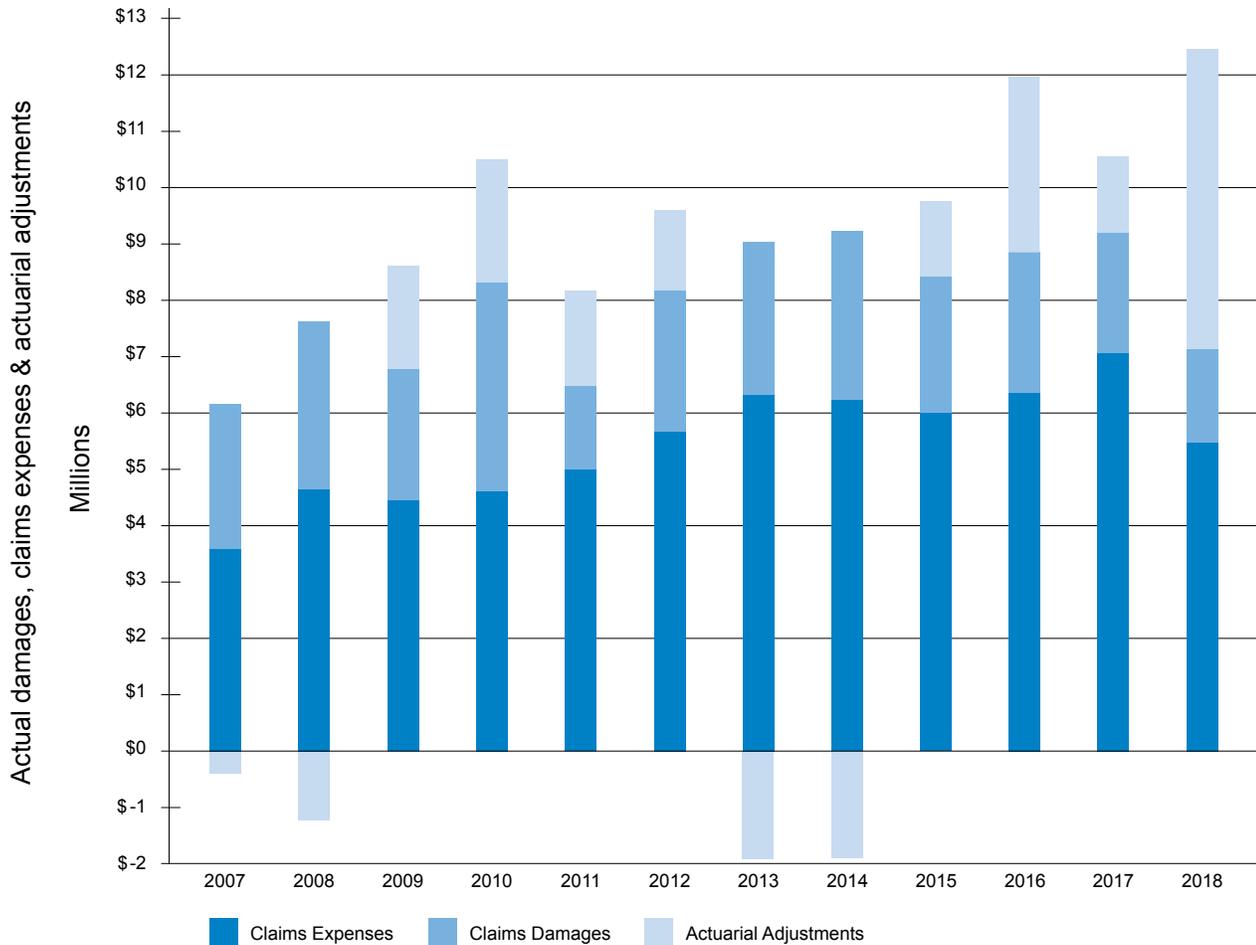
The number of lawsuits against policyholders increased gradually but steadily, almost doubling in number from the early 2000s – with a significantly smaller increase

in the number of policyholders paying the premiums. Except for spikes in 2012 and 2016, since 2007, the number of lawsuits has remained relatively constant.

GRAPH 3: COMBINED IMPACT: DAMAGES, CLAIMS EXPENSES & ACTUARIAL ADJUSTMENTS

Key Facts: Claims Expenses have gradually increased compared to Damages paid. In 2017 and 2018 Claims Expenses exceeded 75% of the total of Claims Expenses and Damages.

Actuarial Adjustments have been volatile, producing both increases and decreases in reserves. In 2018 the Actuarial Adjustment together with an increase in claims reserves reached \$5.3 million.



As Graph 3 illustrates, actual payments for damages and expenses declined from 2017, breaking the pattern since 2015. It is too early to assess whether the decrease in the total for claims expenses and damages in 2018 is an anomaly or indicates a change in the long-term trend.

Claims expenses as a percentage of the total of claims expenses and damages have been gradually increasing from approximately equal in the late 1990s to about 75% in 2017 and 2018. In contrast, damages actually paid have remained relatively static, suggesting that the vigorous defence approach has been successful.

The significance of the actuarial adjustments has varied considerably over the period, producing both increases and decreases in the results reported in the Company's annual Financial Statements. However, recent adjustments have consistently increased the funds required for reserves for future damages and claims

expenses. For 2018, the actuary increased the reserves to \$5.3 million, almost equal to the actual claims expenses incurred in the year.

As a result of the adjustment, the total in claims costs, damages and actuarial adjustments for 2018 reached almost \$12.5 million, the highest in the Company's history.

ACTUARIAL ADJUSTMENTS

The actuary's valuations of claims liabilities is based on analysis of the approximately 475 claims files that were open at the end of the Company's financial year. The actuary's valuation represents an assessment of the anticipated funds necessary to pay damages and claims expenses for these claims in order to provide assurance that the Company can meet its obligations to its policyholders. This independent valuation of outstanding claims by the actuary is not optional. It is a requirement of the insurance regulator.

What is Pro-Demnity doing to address claims expenses?

Already done...

In-house litigation department

Pro-Demnity has established an in-house litigation department as part of a strategy to reduce claims expenses. Our in-house lawyer has assumed responsibility for claims that do not require the resources available from an outside law office. Additionally, she is assisting claims personnel with legal aspects of other claims files, including early assessment of lawsuits to assist with identification of legal risks, and consultation with architects to identify and explain potential contractual issues and consequences.

Although only in place since May 2018, the initiative is already generating tangible savings and the intention is to add to this in-house capability.

Changes to cap on claims expenses

Pro-Demnity has made a change to the existing cap and added a new cap on claims expenses and defence costs paid by Pro-Demnity, where an architect purchases excess outside the Pro-Demnity program. The intention is to “even the playing field” respecting

claims expenses, so that the excess insurer will pay claims expenses as incurred at the time the cap is reached, instead of waiting until the claim is settled, and then only contributing if damages are paid by them.

Pro-Demnity will continue to honour its commitment to defend claims against our policyholders without subtracting the claims expenses from the claim limit. However, good business practice and fairness to Ontario architects dictates that we not indirectly finance the activities of competing insurers.

This change will impact any Ontario architect that purchases any amount of excess insurance from an insurer other than Pro-Demnity, such as where an Ontario architect opts to purchase higher limits from the recently announced RAIC-sponsored program or from any of the other “Excess” insurers currently active in the Ontario market.

Refer to the Pro-Demnity Notice: *Impact of changes to the cap on Claims Expenses* dated March 31, 2019 that includes a chart illustrating the impact of the changes, explanatory notes and the related amendments to the Pro-Demnity policy wordings.

Under consideration...

Restricting foreign jurisdiction coverage

Foreign work can prove to be foreign!

A few Ontario architects have aggressively pursued work outside Canada. Others have taken on foreign work that has come to them through competitions or relationships with established clients. Foreign jurisdiction insurance requirements and related issues are not well understood by most architects, notwithstanding the attractions of the opportunities to work abroad. In a handful of countries, sanctions may apply to insurance coverage.

Although Pro-Demnity has faced relatively few claims on projects outside Canada, the experience has proved remarkably costly, particularly in countries where the legal system is incompatible with the principles of English common law, and the ability to provide an effective defence or attain a settlement of the claim has proven elusive. The impact of these foreign jurisdiction claims on the claims expenses has become an unfair financial

burden to all Ontario architects and an unreasonable risk to the Pro-Demnity program – funded by you!

To address the lessons learned, consideration is being given to:

- limiting foreign jurisdiction coverage to circumstances where claims resolution is based on the principles of English common law;
- changing foreign jurisdiction coverage to mirror that presently applicable to USA claims;
- provision of coverage in Civil Code jurisdictions on a case-by-case basis;
- encouraging purchase of insurance locally, from insurers familiar with the foreign jurisdiction’s legal and claims resolution systems.

Any changes to coverage for foreign jurisdictions will be reviewed by the OAA before implementation, for input and to ensure they are fully informed of material changes in coverage provided by the mandatory program.

Specific underwriting criteria... for the firms with the greatest disparity between premiums paid and costs incurred

Since the founding of the Indemnity Plan, a fundamental principle has been that all architects are subject to the same formula for calculating premiums, regardless of claims experience. However, analysis of the available data has established that a handful of firms have consistently generated much higher costs for claims expenses and damages than the amounts they have contributed to the Plan through their premiums. In effect, the costs generated by these few firms have placed an unfair burden on the rest of the profession in Ontario, subsidized by the premiums being paid by other Ontario architects.

Accordingly, consideration is being given to establishing a separate underwriting category for the practices generating the highest costs for damages and defence in excess of premiums paid

over a number of years. The few practices that meet the specific criteria would be subject to special underwriting criteria such as:

- premium surcharges reflecting the consistently higher costs generated by the firms;
- required quality assurance and risk management programs;
- imposition of deductibles applicable to all costs including claims expenses and legal costs. Currently the deductible applies only to damages actually paid.

Any changes to the underwriting criteria for the firms that fall into this category will be reviewed by the OAA before implementation, for input and to ensure they are fully informed of material changes in the coverage provided by the mandatory program.

How do our circumstances compare to other insurers?

We are not alone. Damages and claims expenses incurred by other insurers and inadequate return on investment linked to underpricing have become a critical concern in the insurance industry generally.

The professional liability insurance market in Canada is dominated by the Lloyd's marketplace, and Lloyd's syndicates have suffered financial loss related to the underwriting of professional liability insurance globally. It is understood that Lloyd's is monitoring and cracking down on syndicates that are writing professional liability insurance without assurance of adequate return on investment to ensure the financial viability of the syndicates and adequate reserves to meet their

commitments. The result has been withdrawal of a number of syndicates from the professional liability market in favour of more profitable lines, and more cautious underwriting by others.

The reduction in providers and poor financial results heralds what is called a "Hard Market", where the insurers who remain active in the North American market will be increasing premiums.

It is anticipated that the upward pressure on premiums will impact availability and pricing of professional liability insurance in Canada.

Help control your premiums – support the company you own!

Ontario architects own Pro-Demnity Insurance Company. Pro-Demnity's sole objective is the protection of Ontario architects.

Do yourself and your colleagues a favour and support your own insurance company by purchasing required increased limits from Pro-Demnity. When you purchase higher limits from another provider, the commission income lost to the "Excess" insurer reduces revenue to Pro-Demnity that is used to offset the costs for the mandatory program provided to every Ontario architect. Every dollar of premium paid to others needs to be offset

by higher premiums paid by every Ontario architect. For example, to the extent it is successful, the diversion of commission income for the recently announced RAIC-sponsored efforts to attract Excess insurance business away from Pro-Demnity's Increased Limits program will cost every Ontario architect additional premium to offset the loss of revenue. The same applies to any other excess insurers already active in the Ontario market.

And importantly, by supporting your own company, you will not be faced with the changes to the cap on claims expenses described on page 4.

The Pro-Definity Advantage: Why Ontario Architects have a Mandatory Insurance Plan



		OTHER INSURERS
Owned by Ontario Architects	✓	No
Interests of Ontario Architects come first	✓	No
Must insure every holder of a Certificate of Practice upon approval by OAA Registrar	✓	No
Same rules for every Architect	✓	No
No limitations on types of buildings or areas of architectural practice	✓	No
Plan Credit available	✓	No
Premiums determined solely by claims experience of Ontario Architects <i>Catastrophic insurance industry losses have no impact on premiums</i>	✓	No
Insurance cannot be cancelled by the insurer <i>Other than for non-payment of premium, deductible, tax or levy</i>	✓	No
Retirement from Practice Insurance <i>Premium is zero – for life plus 6 years for estate resolution</i>	✓	No
Experienced Architects manage claims	✓	No
Reluctant to deny coverage	✓	It depends
Vigorous defence of claims	✓	It depends
Claims Expenses in addition to limits for damages	✓	Sometimes

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