Halwell Mutual Insurance Company
Financial Statements
For the year ended December 31, 2018

Contents

Tel: 905 270-7700
Fax: 905 270-7915
Toll-free: 866 248 6660
www.bdo.ca

BDO Canada **LLP**
1 City Centre Drive, Suite 1700
Mississauga ON L5B 1M2 Canada

Independent Auditor's Report

To the Members of Halwell Mutual Insurance Company

Opinion

We have audited the financial statements of Halwell Mutual Insurance Company (the "Entity"), which comprise the statement of financial position as at December 31, 2018 and the statements of comprehensive income (loss), members' surplus and cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Entity as at December 31, 2018, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Basis for Opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Entity in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Entity's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Entity or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Entity's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Independent Auditor's Report (continued)

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Entity’s internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management’s use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Entity’s ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor’s report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor’s report. However, future events or conditions may cause the Entity to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

BDO Canada LLP

Chartered Professional Accountants, Licensed Public Accountants
Mississauga, Ontario
February 19, 2019

Halwell Mutual Insurance Company
Statement of Financial Position

December 31		2018		2017
Assets				
Cash	**$**	**1,631,598**	$	823,260
Due from policyholders		**7,094,219**		6,086,643
Income taxes recoverable		**55,936**		626,220
Due from reinsurer		**106,051**		54,180
Reinsurer's share of provision for unpaid claims (Note 4e)		**5,024,215**		8,950,378
Deferred policy acquisition expenses (Note 4b)		**2,461,979**		2,137,884
Investments (Note 5)		**35,595,951**		35,627,285
Investment income accrued		**181,325**		144,487
Property and equipment (Note 11)		**8,123,382**		8,255,384
Intangible assets (Note 11)		**-**		1,330
Other assets		**28,921**		25,852
Deferred income taxes		**95,843**		81,544
	$	**60,399,420**	$	62,814,447
Liabilities				
Accounts payable and accrued liabilities	**$**	**1,156,447**	$	1,178,464
Due to reinsurer		**222,392**		153,097
Unearned premiums (Note 4a)		**12,768,087**		11,295,728
Provision for unpaid claims (Note 4c)		**15,040,012**		19,287,746
		29,186,938		31,915,035
Members' Surplus				
Unappropriated members' surplus		**31,212,482**		30,899,412
	$	**60,399,420**	$	62,814,447

Signed on behalf of the Board by:

Director

Director

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

Halwell Mutual Insurance Company
Statement of Comprehensive Income (Loss)

For the year ended December 31	2018	2017
Underwriting income		
Gross premiums written	$ 24,459,393	$ 21,979,073
Less: change in unearned premiums	1,450,255	620,852
Less: reinsurance ceded	3,248,410	3,240,505
Net premiums earned	19,760,728	18,117,716
Service charges	306,445	291,028
	20,067,173	18,408,744
Direct losses incurred		
Gross claims and adjustment expenses	11,773,794	16,641,062
Change in reinsurer's share of provision for unpaid claims	(475,793)	3,410,440
	12,249,587	13,230,622
Underwriting income before expenses	7,817,586	5,178,122
Expenses		
Fees, commissions and other acquisition expenses (Note 8)	4,289,183	4,317,831
Other operating and administrative expenses (Note 9)	3,215,133	3,162,530
	7,504,316	7,480,361
Net underwriting income (loss)	313,270	(2,302,239)
Investment and other income (loss) (Note 6)	(60,495)	1,433,150
Income (loss) before income taxes	252,775	(869,089)
Income (loss) before income taxes	252,775	(869,089)
Income tax expense (recovery) (Note 10)		
Current	(45,996)	(431,853)
Future	(14,299)	35,000
	(60,295)	(396,853)
Comprehensive income (loss) for the year	$ 313,070	$ (472,236)

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

Halwell Mutual Insurance Company
Statement of Members' Surplus

For the year ended December 31	2018	2017
Unappropriated Members' Surplus		
Balance, beginning of year	**$ 30,899,412**	$ 31,371,648
Comprehensive income (loss) for the year	**313,070**	(472,236)
Balance, end of year	**$ 31,212,482**	$ 30,899,412

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

Halwell Mutual Insurance Company
Statement of Cash Flows

For the year ended December 31	2018	2017
Operating activities		
Comprehensive (loss) income for the year	**$ 313,070**	$ (472,236)
Adjustments for:		
Amortization and depreciation of property, equipment and intangibles	**254,489**	232,710
Interest and dividend income	**(1,067,984)**	(1,075,068)
Recovery of income taxes	**(45,996)**	(431,853)
Provision (recovery) of deferred taxes	**(14,299)**	35,000
Realized losses (gains) on disposal of investments	**289,627**	(10,883)
Realized gain on disposal of property and equipment	**(25,314)**	(386,182)
Market value adjustment	**740,991**	(91,198)
	131,514	(1,727,474)
Changes in working capital and insurance contract related balances		
Change in due from policyholders	**(1,007,576)**	(358,653)
Change in reinsurer's share of provision for unpaid claims	**3,926,163**	(394,263)
Change in other assets	**(3,069)**	16,069
Change in accounts payable and accrued liabilities	**(22,017)**	105,647
Change in due to/from reinsurer	**17,424**	(121,795)
Change in deferred policy acquisition expenses	**(324,095)**	14,041
Change in unearned premiums	**1,472,359**	616,914
Change in provision for unpaid claims	**(4,247,734)**	2,187,906
	(188,545)	2,065,866
Cash flows related to interest, dividends and income taxes		
Interest and dividends received	**1,031,146**	1,061,650
Income taxes paid	**568,363**	269,609
	1,599,509	1,331,259
Total cash inflows from operating activities	**1,855,548**	1,197,415
Investing activities		
Sale of investments	**26,811,280**	20,496,004
Purchase of investments	**(27,762,647)**	(19,056,661)
Sale of property, equipment and intangibles	**25,314**	1,400,000
Purchase of property, equipment and intangibles	**(121,157)**	(3,753,400)
Total cash outflows from investing activities	**(1,047,210)**	(914,057)
Net increase in cash	**808,338**	283,358
Cash, beginning of year	**823,260**	539,902
Cash, end of year	**$ 1,631,598**	$ 823,260

1. Corporate Information

Halwell Mutual Insurance Company (the "Company") was incorporated without share capital under the laws governing Ontario on January 9, 1861. The Company is licensed to write property, liability, automobile and farmers' accident insurance in Ontario. The Company's head office is located at 535 Hanlon Creek Blvd., Guelph, Ontario.

The Company is subject to rate regulation on the automobile business that it writes. Before automobile insurance rates can be changed, a rate filing is prepared as a combined filing for most Ontario Farm Mutuals by the Ontario Mutual Insurance Association ("OMIA") . The rate filing must include actuarial justification for rate increases or decreases. All rate filings are approved or denied by the Financial Services Commission of Ontario (“FSCO”). Rate regulation may affect the automobile revenues that are earned by the Company. The actual impact of rate regulation would depend on the competitive environment at the time.

These financial statements have been authorized for issue by the Board of Directors on February 19, 2019.

2. Basis of Preparation

(a) Statement of Compliance

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board (the "IASB").

(b) Basis of Measurement

These financial statements were prepared under the historical cost convention, except for financial assets classified as fair value through profit or loss (“FVTPL”) (Note 5).

The financial statements are presented in Canadian Dollars ("CDN"), which is also the Company's functional currency.

(c) Judgment and Estimates

The preparation of financial statements in compliance with IFRS requires management to make certain critical accounting estimates. It also requires management to exercise judgment in applying the Company’s accounting policies. The areas involving critical judgments and estimates in applying accounting policies that have the most significant risk of causing material adjustment to the carrying amounts of assets and liabilities recognized in the financial statements within the next financial year are:

- The calculation of unpaid claims, including the determination of the initial claim liability, discount rates, the estimate of time until ultimate settlement and the performance of a liability adequacy test (Note 4);
- The determination of the recoverability of deferred policy acquisition expenses (Note 4), and;

2. Basis of Preparation (continued)

- The classification of financial assets at FVTPL, which includes assessing the business model within which the assets are held and whether the contractual terms of the assets are solely payments of principal and interest on the principal amount outstanding. (Note 5)

In addition, in preparing the financial statements, the notes to the financial statements were ordered such that the most relevant information was presented earlier in the notes and the disclosures that management deemed to be immaterial were excluded from the notes to the financial statements. The determination of the relevance and materiality of disclosures involved significant judgment.

3. Adoption of New Accounting Standards

Accounting standards, interpretations and amendments effective for accounting years beginning on or after January 1, 2018 did not materially affect the Company's financial statements other than those described below.

IFRS 9 *Financial Instruments* (IFRS 9)

On January 1, 2018, the Company adopted IFRS 9, *Financial Instruments* (IFRS 9), which supersedes IAS 39, *Financial Instruments: Recognition and Measurement* (IAS 39). IFRS 9 includes revised guidance on the classification and measurement of financial assets and liabilities; new guidance for measuring impairment on financial assets; and new hedge accounting guidance.

(i) Classification and measurement of financial instruments

Under IFRS 9, financial assets are classified and measured based on the business model in which they are held and the characteristics of their contractual cash flows. IFRS 9 contains three primary measurement categories for financial assets: measured at amortized cost, fair value through other comprehensive income (FVTOCI), and FVTPL.

The original classification and carrying amount under IAS 39 and the new classification and carrying amount under IFRS 9 for each class of the Company's financial assets and financial liabilities as at January 1, 2018 remained the same, with exception of cash and accounts receivable changing classification from loans and receivables to amortized cost, and accounts payable changing classification from other financial liabilities to amortized cost.

3. Adoption of New Accounting Standards (continued)

(ii) Impairment of financial assets

IFRS 9 replaces the incurred loss model in IAS 39 with an expected credit loss (“ECL”) model. This applies to financial assets classified at amortized cost and debt instruments classified at FVTOCI. Under IFRS 9, credit losses are recognized earlier than under IAS 39. This change did not have an impact on the Company’s financial statements.

(iii) Hedge Accounting

The new hedge accounting model which replaces hedge accounting guidance in IAS 39 did not impact the Company’s financial statements.

(iv) Disclosure

Amendments were also made to IFRS 7 introducing expanded qualitative and quantitative disclosures related to IFRS 9, which the Company has also adopted for the annual period beginning January 1, 2018.

4. Insurance Contracts

In accordance with IFRS 4, Insurance Contracts, the Company has continued to apply the accounting policies it applied in accordance with pre-changeover Canadian generally accepted accounting principles.

Balances arising from insurance contracts primarily include unearned premiums, provision for unpaid claims, the reinsurer's share of provision for unpaid claims, and deferred policy acquisition expenses.

(a) Premiums and unearned premiums

Premiums written comprise the premiums on contracts incepting in the financial year. Premiums written are stated gross of commissions payable to agents and exclusive of taxes levied on premiums.

The Company recognizes premium income evenly over the term of the insurance policy using the pro rata method. The portion of the premium related to the unexpired portion of the policy at the end of the fiscal year is reflected in unearned premiums (UEP). Changes in unearned premiums recorded in the statement of financial position for the year-ended December 31, 2018 and 2017 and their impact on net premiums earned for the two years follow:

4. Insurance Contracts (continued)

(a) Premiums and unearned premiums (continued)

Unearned premiums (UEP)	2018	2017
Balance, beginning of the year	**$ 11,295,728**	$ 10,678,814
Premiums written	**24,459,393**	21,979,073
Premiums earned during the year	**(24,437,289)**	(21,983,011)
Changes in UEP recognized in income	**1,450,255**	620,852
Balance, end of the year	**$ 12,768,087**	$ 11,295,728

Pricing of property and liability policies are based on assumptions in regard to trends and past experience, in an attempt to correctly match policy revenue with exposed risk. Automobile premiums are subject to approval by the Financial Services Commission of Ontario and therefore may result in a delay in adjusting the pricing to exposed risk.

The Company is exposed to a pricing risk to the extent that unearned premiums are insufficient to meet the related future policy costs. Evaluation is performed regularly to estimate future claims costs, related expenses, and expected profit in relation to unearned premiums. There was no premium deficiency at December 31, 2018 and 2017.

Amounts due from policyholders are short-term in nature consisting of a large number of policyholders, and are not subject to material credit risk. Regular review of amounts outstanding is performed to ensure credit worthiness.

4. Insurance Contracts (continued)

(b) Deferred policy acquisition expenses

Acquisition costs are comprised of commissions, premium taxes, and other incremental costs of acquiring and renewing policies. These costs are deferred and amortized over the terms of the related policies to the extent that they are considered to be recoverable from unearned premiums, after considering the related anticipated claims and expenses. Changes in deferred policy acquisition expenses recorded in statement of financial position for the years-ended December 31, 2018 and 2017, and their impact on fees, commissions and other acquisition expenses for the two years follow:

	2018	2017
Balance, beginning of the year	**$ 2,137,884**	$ 2,151,925
Acquisition costs incurred	**8,480,583**	7,567,275
Expensed during the year	**(8,156,488)**	(7,581,316)
Balance, end of the year	**$ 2,461,979**	$ 2,137,884

Deferred policy acquisition expenses will be recognized as an expense within one year.

(c) Provision for unpaid claims

Individual loss estimates are provided on each claim reported. In addition, provisions are made for adjustment expenses, claims development changes in reported claims and for claims incurred but not reported, based on past experience and business in force. The estimates are regularly reviewed and updated, and any resulting adjustments are included in current income.

Claim liabilities are carried on a discounted basis to reflect the time value of money. As required by actuarial standards in Canada, claims liabilities also include a provision for adverse deviation (PFAD), which represents an additional margin on valuation variable factors, which are claims development, reinsurance recoveries and interest rates used in discounting claims liabilities.

4. Insurance Contracts (continued)

(c) Provision for unpaid claims (continued)

A summary of the Company's outstanding gross unpaid claims liabilities, related reinsurer's share of unpaid claims and the net insurance liabilities follows:

	December 31, 2018			December 31, 2017		
	Gross	**Re-insurance**	**Net**	Gross	Re-insurance	Net
Outstanding claims provision						
Long-term	**$ 6,729,082**	**$ 2,354,282**	**$ 4,374,800**	$ 6,710,376	$ 3,656,829	$ 3,053,547
Short-term	**2,965,744**	**691,933**	**2,273,811**	6,895,594	3,020,549	3,875,045
Facility Association and other residual pools	**369,186**	**-**	**369,186**	343,776	-	343,776
	10,064,012	**3,046,215**	**7,017,797**	13,949,746	6,677,378	7,272,368
Provision for claims incurred but not reported	**4,976,000**	**1,978,000**	**2,998,000**	5,338,000	2,273,000	3,065,000
	$ 15,040,012	**$ 5,024,215**	**$ 10,015,797**	$ 19,287,746	$ 8,950,378	$ 10,337,368

4. Insurance Contracts (continued)

(c) Provision for unpaid claims (continued)

The ultimate cost of long settlement general liability claims are difficult to predict for several reasons. Claims may not be reported until many years after a policy expires. Changes in the legal environment can create further complications. Court decisions and federal and provincial legislation may dramatically increase the liability between the time a policy is written and associated claims are ultimately resolved. For example, liability for exposure to toxic substances and environmental impairment, which did not appear likely or even exist when the policies were written, has been imposed by legislators and judicial interpretation. Tort liability has been expanded by some jurisdictions to cover defective workmanship. Provisions for such difficult-to-estimate liabilities are established by examining the facts of tendered claims and adjusted in the aggregate for ultimate loss expectations based upon historical experience patterns and current socioeconomic trends.

The Company must participate in industry automobile residual pools of business, and recognizes a share of this business based on its automobile market share. The Company records its share of the assets, liabilities, revenue, and expenses provided by the actuaries of the pools.

Changes in claim liabilities recorded in the statement of financial position for the years-ended December 31, 2018 and 2017 and their impact on claims and adjustment expenses for the two years follow:

	2018	2017
Unpaid claim liabilities - beginning of year – net of reinsurance	**$ 10,337,368**	$ 8,535,668
Increase (decrease) in estimated losses and expenses, for losses occurring in prior years	**5,017,384**	3,427,293
Provision for losses and expenses on claims occurring in the current year	**6,154,586**	8,195,631
Increase in provision for claims incurred but not reported	**(67,000)**	525,000
Payment on claims:		
Current year	**(7,233,116)**	(6,849,853)
Prior years	**(4,193,425)**	(3,496,371)
Unpaid claims – end of year - net	**10,015,797**	10,337,368
Reinsurer's share and subrogation recoverable	**5,024,215**	8,950,378
	$ 15,040,012	$ 19,287,746

The change in estimate of losses occurring in prior years is due to changes arising from new information received.

4. Insurance Contracts (continued)

(c) Provision for unpaid claims (continued)

Claim development

The principal risk the Company faces under insurance contracts is that the actual claims and benefit payments or the timing thereof, differ from expectations. This is influenced by the frequency of claims, severity of claims, actual benefits paid and subsequent development of long-term claims. Therefore, the objective of the Company is to ensure that sufficient reserves are available to cover these liabilities.

The Company writes insurance primarily over a twelve month duration. The most significant risks arise through high severity, low frequency events such as natural disasters or catastrophes. A concentration of risk may arise from insurance contracts issued in a specific geographic location since all insurance contracts are written in Ontario.

The above risk exposure is mitigated by diversification across a large portfolio of insurance. The variability of risks is also improved by careful selection and implementation of underwriting strategy guidelines, as well as the use of reinsurance arrangements.

The estimation of claim development involves assessing the future behaviour of claims, taking into consideration the consistency of the Company's claim handling procedures, the amount of information available, the characteristics of the line of business from which the claim arises and claims reporting patterns. In general, the longer the term required for the settlement of a group of claims the more variable the estimates. Short settlement term claims are those which are expected to be substantially paid within a year of being reported.

The tables below show how the Company’s estimate of cumulative incurred claim cost for each accident year has changed at successive year ends and reconciles the cumulative claims to the amount appearing in the statement of financial position. An accident-year basis is considered to be the most appropriate for the business written by the Company.

4. Insurance Contracts (continued)

(c) Provision for unpaid claims (continued)

Gross claims (in 000's)

	Accident Year										
Reporting Date	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**Total**
At end of accident year	$ 8,533	$ 9,720	$ 13,962	$ 10,342	$ 13,470	$ 9,623	$ 9,095	$ 12,006	$14,456	$ 14,399	
1 year later	8,404	9,558	13,450	9,901	13,747	9,336	9,037	12,611	14,680		
2 years later	8,379	9,154	12,434	9,578	13,181	8,996	8,603	13,040			
3 years later	7,640	8,774	12,431	9,121	12,827	8,441	7,658				
4 years later	7,288	8,279	10,847	8,660	12,897	8,072					
5 years later	7,263	8,621	10,310	9,519	11,114						
6 years later	7,246	8,500	10,523	8,805							
7 years later	7,245	8,510	10,416								
8 years later	7,245	8,437									
9 years later	7,245										
Current estimate of ultimate cost	7,245	8,437	10,416	8,805	11,114	8,072	7,658	13,040	14,680	14,399	103,866
Cumulative payments	7,245	8,436	10,333	8,790	10,927	7,943	7,057	10,015	11,651	7,983	90,380
Outstanding claims	$ -	$ 1	$ 83	$ 15	$ 187	$ 129	$ 601	$ 3,025	$ 3,029	$ 6,416	$ 13,486
Liability for all prior accident years											34
Impact of discount and PFAD											1,150
Facility Association and risk sharing pool											370
Total gross outstanding claims											$ 15,040

4. Insurance Contracts (continued)

(c) Provision for unpaid claims (continued)

Net of reinsurance (in 000's)

	Accident Year										
Reporting Date	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**Total**
At end of accident year	$ 6,234	$ 6,641	$ 6,965	$ 6,244	$ 7,674	$ 7,672	$ 7,395	$ 9,936	$ 12,122	$ 11,910	
1 year later	6,351	6,159	6,745	6,727	8,115	7,625	7,602	10,185	12,025		
2 years later	5,822	6,218	6,852	6,395	7,821	7,402	7,251	10,086			
3 years later	5,474	6,120	6,615	6,074	7,546	7,314	7,050				
4 years later	5,318	5,852	6,351	5,983	7,534	7,136					
5 years later	5,308	5,916	6,219	5,882	7,624						
6 years later	5,294	5,809	6,190	5,733							
7 years later	5,294	5,819	6,226								
8 years later	5,294	5,746									
9 years later	5,294										
Current estimate of ultimate cost	5,294	5,746	6,226	5,733	7,624	7,136	7,050	10,086	12,025	11,910	78,830
Cumulative payments	5,294	5,745	6,142	5,718	7,456	7,115	6,629	8,983	10,041	7,233	70,356
Outstanding claims	$ -	$ 1	$ 84	$ 15	$ 168	$ 21	$ 421	$ 1,103	$ 1,984	$ 4,677	$ 8,474
Liability for all prior accident years											34
Impact of discount and PFAD											1,138
Facility Association and risk sharing pool											370
Total gross outstanding claims											$ 10,016

4. Insurance Contracts (continued)

(c) Provision for unpaid claims (continued)

The risks associated with insurance contracts are complex and subject to a number of variables which complicates quantitative sensitivity analysis. The Company uses various techniques based on past claims development experience to quantify these sensitivities. This includes indicators such as average claim cost, amount of claims frequency, expected loss ratios and claims development.

Results of sensitivity testing based on expected loss ratios are as follows, showing gross and net of reinsurance and the impact on pre-tax income:

	Property claims		**Auto claims**		**Liability claims**	
	2018	2017	**2018**	2017	**2018**	2017
5% increase in loss ratios						
Gross	**$ 4,001,000**	$ 5,984,000	**$ 1,257,000**	$ 3,651,000	**$ 6,621,000**	$ 1,152,000
Net	**$ 3,218,000**	$ 5,216,000	**$ 914,000**	$ 2,923,000	**$ 5,818,000**	$ 841,000
5% decrease in loss ratios						
Gross	**$(4,001,000)**	$(5,984,000)	**$(1,257,000)**	$(3,651,000)	**$(6,621,000)**	$(1,152,000)
Net	**$(3,218,000)**	$(5,216,000)	**$ (914,000)**	$(2,923,000)	**$(5,818,000)**	$ (841,000)

There have been no significant changes from the previous year in the exposure to risk or policies, procedures and methods used to measure the risk.

(d) Liability adequacy test

At each reporting date, the Company performs a liability adequacy test on its insurance liabilities less deferred policy acquisition expenses to ensure the carrying value is adequate, using current estimates of future cash flows, taking into account the relevant discount rate. If that assessment shows that the carrying amount of the liabilities is inadequate, any deficiency is recognized as an expense in the statement of comprehensive income (loss) initially by writing down the deferred policy acquisition expense and subsequently by recognizing additional unearned premiums. No deficiency was recognized in the statement of comprehensive income (loss) in the current or prior period.

4. Insurance Contracts (continued)

(e) Reinsurer's share of provision for unpaid claims

The Company enters into reinsurance contracts in the normal course of business in order to limit potential losses arising from certain exposures. Retention limits for the excess-of-loss reinsurance are set by product line. Reinsurance premiums are accounted for in the same period as the related premiums for the direct insurance business being reinsured. Reinsurance liabilities, comprised of premiums payable for the purchase of reinsurance contracts, are included in accounts payable and accrued liabilities and are recognized as an expense on the same basis as revenue on the underlying policies being reinsured.

The Company follows a policy of underwriting and reinsuring contracts of insurance which, in the main, limit the liability of the Company to an amount on any one claim of $400,000 (2017 - $400,000) in the event of a property claim, an amount of $600,000 (2017 - $500,000) in the event of an automobile claim and $750,000 (2017 - $750,000) in the event of a liability claim. For amounts over the respective limits there is a 20% retention to a specified maximum. The Company also obtained reinsurance which limits the Company's liability to $1,200,000 (2017 - $1,200,000) plus 20% of the amount in excess of $1,200,000 (2017 - $1,200,000) in the event of a series of claims arising out of a single occurrence. In addition, the Company has obtained stop loss reinsurance which limits the liability of all claims in a specific year to 70% of gross net earned premiums for property and automobile.

Amounts recoverable from reinsurer are estimated in a manner consistent with the outstanding claims provision and are in accordance with the reinsurance contracts. Although the Company has reinsurance arrangements, it is not relieved of its direct obligations to its policyholders and thus a credit exposure exists with respect to ceded insurance, to the extent that the reinsurer is unable to meet its obligations assumed under such reinsurance agreements.

Expected reinsurance recoveries on unpaid claims and adjustment expenses are recognized as assets at the same time and using principles consistent with the Company's method for establishing the related liability. Changes in reinsurer's share of provision for unpaid claims in the statement of financial position for the years-ended December 31, 2018 and 2017 follow:

	2018	2017
Balance, beginning of the year	**$ 8,950,378**	$ 8,564,172
New claims reserve	**1,262,944**	1,461,883
Change in prior years' reserve	**(1,744,453)**	1,940,500
Submitted to reinsurer	**(3,444,654)**	(3,016,177)
Balance, end of the year	**$ 5,024,215**	$ 8,950,378

Reinsurance is placed with Farm Mutual Reinsurance Plan Inc. (FMRP), a Canadian reinsurer. Management monitors the creditworthiness of FMRP by reviewing their annual financial statements and through ongoing communications. Reinsurance treaties are reviewed annually by management prior to renewal of the reinsurance contract. At year end, the Company reviewed the amounts owing from its reinsurer and determined that no allowance is necessary.

4. Insurance Contracts (continued)

(f) Refund of premium

At the discretion of the Board of Directors, the Company may declare a refund to its policyholders based on the property premiums paid in the fiscal period. This refund is recognized as a reduction of revenue in the period for which it is declared.

5. Investments

(a) Recognition and initial measurement

The Company recognizes debt instruments on the date on which they are originated. Equity instruments including pooled funds, are recognized on the trade date, which is the date that the asset is received by the Company. The instruments are initially measured at fair value.

(b) Classification and subsequent measurement

The Company classifies its debt instruments, bankers' acceptances/GICs and bonds as FVTPL because the Company manages the debt instruments and evaluates their performance on a fair value basis in accordance with a documented investment strategy and the instruments are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

The Company's pooled funds are redeemable at the option of the holder and therefore considered debt instruments under IFRS 9 that do not give rise to cash flows that are solely payments of principal and interest and therefore are classified as FVTPL.

The Company classifies its equity instruments as FVTPL.

The debt and equity instruments are subsequently measured at fair value where the net gains and losses, including any interest or dividend income are recognized in profit or loss.

(c) Derecognition

The Company derecognizes investments when the contractual rights to the cash flows from the investment expires or the Company transfers the investment. On derecognition, the difference between the carrying amount at the date of derecognition and the consideration received is recognized in profit or loss.

(d) Risks

The following table provides fair value information of investments by type of security and issuer.

5. Investments (continued)

	2018	2017
	Fair value	Fair value
Cash	**$ 10,897**	$ 102,259
Bankers acceptance / GICs	**270,009**	270,009
	280,906	372,268
Bonds issued by		
Federal	**5,018,375**	5,048,534
Provincial	**7,118,017**	5,643,109
Municipal	**1,395,236**	1,392,874
Corporate		
A or better	**8,392,840**	10,465,207
BBB	**1,461,583**	1,256,892
	23,386,051	23,806,616
Equity investments		
Canadian	**3,092,605**	1,732,465
Canadian equity pooled fund	**4,728,043**	5,911,406
	7,820,648	7,643,871
Other investments		
Fire Mutuals guarantee fund	**49,375**	42,196
Commercial mortgage pooled fund	**3,393,141**	2,751,926
Money market liquidity pooled fund	**665,829**	1,010,407
Other - MCCG	**1**	1
	4,108,346	3,804,530
Total investments	**$ 35,595,951**	$ 35,627,285

5. **Investments** (continued)

The Company is exposed to credit risk relating to its bond holdings in its investment portfolio.

The Company’s investment policy puts limits on the bond portfolio including portfolio composition limits, issuer type limits, bond quality limits, aggregate issuer limits, corporate sector limits and general guidelines for geographic exposure. The bond portfolio includes 94% (2017 – 95%) of bonds rated A or better. The Company’s investment policy limits investment in bonds and debentures of the various ratings to limits ranging from 50% to 85% of the Company's portfolio. Funds should be invested in bonds and debentures of Federal, Provincial or Municipal Government and corporations rated BBB or better. All fixed income portfolios are measured for performance on a quarterly basis and monitored by management on a monthly basis.

The maximum exposure to investment credit risk is the carrying value of investments.

There have been no significant changes from the previous year in the exposure to risk or policies, procedures and methods used to measure the credit risk.

Liquidity risk is the risk that the Company will not be able to meet all cash outflow obligations as they come due. The Company mitigates this risk by monitoring cash activities and expected outflows. The Company's current liabilities arise as claims are made. The Company does not have material liabilities that can be called unexpectedly at the demand of a lender or client. The Company has no material commitments for capital expenditures, and there is no need for such expenditures in the normal course of business. Claim payments are funded by current operating cash flow including investment income.

The Company’s investment policy requires that 0% to 10% of the Company's portfolio be held in cash and short-term investments, which mitigates liquidity risk. Short-term investments are defined as loans of less than one year to maturity at the time of purchase.

The maturity profile of bonds held is as follows:

	Within 1 year	1 to 5 years	6 to 10 years	Over 10 years	Fair value
December 31, 2018	**$ 1,680,340**	**$ 10,842,225**	**$ 9,411,324**	**$ 1,452,162**	**$ 23,386,051**
Percent of Total	**7 %**	**47 %**	**40 %**	**6 %**	
December 31, 2017	$ 110,363	$ 12,922,469	$ 10,715,279	$ 58,505	$ 23,806,616
Percent of Total	- %	55 %	45 %	- %	

There have been no significant changes from the previous year in the exposure to risk or policies, procedures and methods used to measure the liquidity risk.

5. Investments (continued)

Market Rate Risk

Market factors that will impact the fair value of investments include three types of risk: currency risk, interest rate risk and equity risk. The Company does not purchase investments in foreign currencies, therefore there is no currency risk.

The Company's investment policy operates within the guidelines of the Insurance Act. An investment policy is in place and its application is monitored by the Investment Committee and the Board of Directors. Diversification techniques are utilized to minimize risk.

Interest Rate Risk

Interest rate risk is the potential for financial loss caused by fluctuations in fair value or future cash flows of financial instruments because of changes in market interest rates.

The Company is exposed to interest rate risk through its interest bearing investments (bankers acceptances, GICs and bonds).

Historical data and current information is used to profile the ultimate claims settlement pattern by class of insurance, which is then used in a broad sense to develop an investment policy and strategy. However, because a significant portion of the Company's assets relate to its capital rather than liabilities, the value of its interest rate based assets exceeds its interest rate based liabilities. As a result, generally, the Company's investment income will move with interest rates over the medium to long-term with short-term interest rate fluctuations creating unrealized gains or losses in comprehensive income (loss). There are no occurrences where the interest would be charged on liabilities; therefore, little protection is needed to ensure fair market value of assets will be offset by a similar change in liabilities due to an interest rate change.

At December 31, 2018, a 1% move in interest rates, with all other variables held constant, could impact the market value of bonds by $1,164,228 (2017 - $1,146,712). This change would be recognized in comprehensive income (loss).

There have been no significant changes from the previous year in the exposure to risk or policies, procedures and methods used to measure the interest rate risk.

5. Investments (continued)

Equity Risk

Equity risk is the uncertainty associated with the valuation of assets arising from changes in equity markets. The Company is exposed to this risk through its equity and pooled fund holdings within its investment portfolio.

The Company's portfolio includes Canadian stocks and pooled funds with fair values that move with the Toronto Stock Exchange Composite Index. At December 31, 2018, a 10% movement in the stock markets with all other variables held constant would have an estimated effect on the fair values of the Company's Canadian equity instruments of $309,261 (2017 - $173,247). This change would be recognized in comprehensive (loss) income.

There have been no significant changes from the previous year in the exposure to risk or policies, procedures and methods used to measure equity risk.

Fair value measurement

The following table provides an analysis of investments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

	Level 1	Level 2	Level 3	Total
December 31, 2018				
Bonds	-	23,386,051	-	23,386,051
Equities and equity pooled funds	7,820,648	-	-	7,820,648
Other investments	665,829	-	3,442,517	4,108,346
Total	$ 8,486,477	$ 23,386,051	$ 3,442,517	$ 35,315,045

5. Investments (continued)

		Level 1		Level 2		Level 3		Total
December 31, 2017								
Bonds		-		23,806,616		-		23,806,616
Equities and equity pooled funds		7,643,871		-		-		7,643,871
Other investments		1,010,407		-		2,794,123		3,804,530
Total	$	8,654,278	$	23,806,616	$	2,794,123	$	35,255,017

Transfers between levels are considered to have occurred at the date of the event or change in circumstances that caused the transfer. There were no transfers between Level 1 and Level 2 for the year ended December 31, 2018. There were also no transfers in and out of Level 3.

The fair value of the commercial mortgage pooled fund included in other investments, is based on the net asset value of the pooled fund as provided by the investment manager of the fund. The commercial mortgages included in the commercial mortgage pooled fund are valued at the present value of discounted future cash flows. The discount rate is based on the equivalent Government of Canada rate (time to maturity) and an additional spread to compensate for a loan's particular risk. The Government of Canada rates are obtained from an independent external source at the bond market prevailing rate. The bond rates are interpolated where necessary based on the yield. The Canada Treasury Bill rates are used for terms less or equal to one year. Due to the use of unobservable data and their limited liquidity, the commercial mortgage pooled fund is classified as Level 3.

6. Investment and Other Income (Loss)

		2018		2017
Interest income	**$**	**769,635**	$	745,805
Dividend income		**298,349**		329,263
Realized gains (losses) on disposal of investments		**(289,627)**		10,883
Investment expenses		**(123,175)**		(130,181)
Market value adjustment		**(740,991)**		91,198
Realized gain on disposal of property and equipment		**25,314**		386,182
	$	**(60,495)**	$	1,433,150

7. Capital Management

For the purpose of capital management, the Company has defined capital as members' surplus. The Company's objectives with respect to capital management are to maintain a capital base that is structured to exceed regulatory requirements and to best utilize capital allocations.

The regulators measure the financial strength of property and casualty insurers using a minimum capital test (MCT). The regulators require property and casualty companies to comply with capital adequacy requirements. This test compares a company's capital against the risk profile of the organization. The risk-based capital adequacy framework assesses the risk of assets, policy liabilities and other exposures by applying various factors that are dependent on the risks associated with the company's assets. Additionally, an interest rate risk margin is included in the MCT by assessing the sensitivity of the Company's interest-sensitive assets and liabilities to changes in interest rates. The regulator indicates that the Company should produce a minimum MCT of 150%. During the year, the Company has consistently exceeded this minimum on a quarterly basis. The regulator has the authority to request more extensive reporting and can place restrictions on the Company's operations if the company falls below this requirement and deemed necessary.

8. Fees, Commissions and Other Acquisition Expenses

	2018	2017
Broker profit sharing	**$ 395,687**	$ 486,078
Commissions	**3,893,496**	3,831,753
	$ 4,289,183	$ 4,317,831

9. Other Operating and Administrative Expenses

	2018	2017
Computer costs	**$ 291,745**	$ 316,816
Licenses, fees and dues	**118,344**	112,143
Amortization and depreciation	**254,489**	232,710
Utilities	**48,372**	43,584
Postage and office supplies	**222,392**	211,634
Professional fees	**109,294**	115,971
Regulatory assessments	**50,408**	45,051
Salaries, benefits and directors' fees (Note 14)	**1,689,162**	1,631,309
Other	**430,927**	453,312
	$ 3,215,133	$ 3,162,530

10. Income Taxes

Income tax expense is comprised of current and deferred tax. Current and deferred tax are recognized in net income except to the extent that it relates to items recognized directly in equity or in other comprehensive income (loss).

The significant components of the tax effect included in comprehensive income (loss) are composed of:

	2018	2017
Current tax recovery		
Based on current year taxable income	**$ -**	$ -
Provision for losses carried back to prior years	**(40,625)**	(379,023)
Adjustments for over / under provision in prior periods	**(5,371)**	(52,830)
	(45,996)	(431,853)
Deferred tax expense (recovery)		
Origination and reversal of temporary differences	**(14,299)**	35,000
Total income tax recovery	**$ (60,295)**	$ (396,853)

Reasons for the difference between income tax recovery for the year and the expected income taxes based on the statutory tax rate of 26.5% (2017- 26.5%) are as follows:

	2018	2017
Income (loss) for the year	**$ 252,775**	$ (869,089)
Expected taxes (recovery) based on the statutory rate of 26.5% (2017 – 26.5%)	**66,985**	(230,309)
Canadian dividend income not subject to tax	**(79,062)**	(87,255)
Other	**(48,218)**	(79,289)
Total income tax recovery	**$ (60,295)**	$ (396,853)

11. Property, Equipment and Intangible Assets

Property, equipment and intangible assets are initially recorded at cost and subsequently measured at cost less accumulated depreciation, amortization or accumulated impairment losses, with the exception of land which is not depreciated. Amortization and depreciation is recognized in net income and is provided on a straight-line basis over the estimated useful life of the assets as follows:

	Useful Life	2018 Cost	2018 Accumulated Depreciation and Amortization	2018 Net Book Value
Property and Equipment				
Land	N/A	$ 1,029,754	$ -	$ 1,029,754
Building	40 years	6,967,199	275,785	6,691,414
Computer hardware	5 years	114,902	58,060	56,842
Furniture and fixtures	10 years	334,828	54,960	279,868
Vehicles	3 years	90,413	24,909	65,504
Total		**$ 8,537,096**	**$ 413,714**	**$ 8,123,382**
Intangible assets				
Computer software	2 years	**$ 162,836**	**$ 162,836**	**$ -**

	Useful Life	2017 Cost	2017 Accumulated Amortization and Depreciation	2017 Net Book Value
Property and Equipment				
Land	N/A	$ 1,029,754	$ -	$ 1,029,754
Building	40 years	6,967,199	101,605	6,865,594
Computer hardware	5 years	108,953	35,819	73,134
Furniture and fixtures	10 years	310,035	23,133	286,902
Vehicles	3 years	76,584	76,584	-
Total		**$ 8,492,525**	**$ 237,141**	**$ 8,255,384**
Intangible assets				
Computer software	2 years	**$ 162,836**	**$ 161,506**	**$ 1,330**

12. Structured Settlements, Fire Mutuals Guarantee Fund and Financial Guarantee Contracts

The Company enters into Type 1 annuity agreements with various life insurance companies to provide for fixed and recurring payments to claimants. Type 1 structured settlements are where the Company transfers the insurance contracts to the life insurer for an annuity that pays directly to the claimant, and the annuity is non-commutable, non-assignable, and non-transferable. Under such arrangements, the Company's liability to its claimants is substantially transferred, although the Company remains exposed to the credit risk that life insurers fail to fulfill their obligations.

The Office of the Superintendent of Financial Institutions ("OSFI") Guideline D5 Accounting for Structured Settlements requires that claims and annuities of Type 1 structures are derecognized from the property and casualty ("P&C") insurer's statement of financial position. The claimant's recourse to the P&C insurer represents a guarantee of the annuity underwriter's obligation to make payments to the claimant pursuant to the terms and conditions of the structured settlement. The financial guarantee on initial recognition is generally recognized at nil value. Subsequently, the guarantee is measured in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*.

The maximum exposure for the Company is the discounted value of the payments outstanding on such annuities that are still in force. The Company does not have an estimate of the undiscounted outstanding payments. The Company's potential exposure to any defaults by life insurers, taken together with coverage provided by the life insurance industry's consumer protection plan, is assessed as minimal as at December 31, 2018 (2017 - minimal).

The Company is a member of the Fire Mutuals Guarantee Fund ("the Fund"). The Fund was established to provide payment of outstanding policyholders' claims if a member company becomes bankrupt. As a result, the Company may be required to contribute assets in their proportionate share to meet this objective.

This exposure represents a financial guarantee contract. The Company accounts for financial guarantee contracts in accordance with IFRS 4, *Insurance Contracts*.

13. Pension Plan

The Company makes contributions on behalf of its employees to "The Retirement Annuity Plan for Employees of the Ontario Mutual Insurance Association and Member Companies", which is a multi-employer plan. Each member company has signed an Ontario Mutual Insurance Association Pension Plan Agreement. Eligible employees participate in the defined benefit plan and sales agents participate in the defined contribution plan. The defined benefit plan specifies the amount of the retirement benefit to be received by the employee based on the number of years the employee has contributed and his/her final average earnings. The plan is accounted for as a defined contribution plan as insufficient information is available to account for the plan as a defined benefit plan. The Company is one of a number of employers that participates in the plan and the financial information provided to the Company on the basis of the contractual agreements is insufficient to reliably measure the Company's proportionate share in the plan assets and liabilities on defined benefit accounting requirements.

13. Pension Plan (continued)

The Company matches the employee contributions and funds the excess defined benefit based on the Company's percentage of pensionable earnings as calculated by the Pension Plan actuaries. The Pension Plan agreement states that the Company is responsible for its share of any deficit as a result of any actuarial valuation or cost certificate. The minimum funding requirement is the solvency valuation amount determined by the Pension Plan actuary on the valuation dates prescribed by the Pensions Benefit Act. In the event of a wind-up, voluntary withdrawal or bankruptcy, either by the Company or the group as a whole, the Company is responsible for its portion of all expenses and deficit related to such.

The amount contributed to the plan for 2018 was $170,655 (2017 - $145,873). The contributions were made for current service and these have been recognized in comprehensive (loss) income. The current service amount is determined by the Pension Plan actuary using the projected accrued benefit actuarial cost method. These contributions amount to 2.16% (2017 - 1.9%) of the total contributions made to the Ontario Mutual Insurance Association Pension Plan by all participating entities during the current fiscal year.

Expected contributions to the plan for the next annual reporting period amount to $178,000.

14. Related Party Transactions

The Company entered into the following transactions with key management personnel, which are defined by IAS 24 Related Party Disclosures, as those persons having authority and responsibility for planning, directing and controlling the activities of the Company, including directors and management:

	2018	2017
Compensation		
Short term employee benefits and directors' fees	**$ 705,686**	$ 808,722
Total pension and other post-employment benefits	**59,161**	77,357
	$ 764,847	$ 886,079
Premiums	**$ 51,270**	$ 59,212
Claims paid	**$ 14,231**	$ 8,733

15. Credit Facility

The Company has an available line of credit in the amount of $50,000, which bears interest at prime plus 3% . As of December 31, 2018 this facility has not been drawn on (2017 - $Nil).

16. Standards, Amendments and Interpretations Not Yet Effective

Certain pronouncements were issued by the IASB or the IFRS Interpretations Committee that are mandatory for accounting years beginning after January 1, 2019 or later.

The Company has not yet determined the extent of the impact of the following new standards, interpretations and amendments, which have not been applied in these financial statements:

IFRS 16 Leases

IFRS 16 Leases supersedes IAS 17 Leases, IFRIC 4 Determining whether an Arrangement contains a Lease, SIC-15 Operating Leases – Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. It eliminates the distinction between operating and finance leases from the perspective of the lessee. All contracts that meet the definition of a lease will be recorded in the statement of financial position with a “right of use” asset and a corresponding liability. The asset is subsequently accounted for as property, plant and equipment or investment property and the liability is unwound using the interest rate inherent in the lease. The accounting requirements from the perspective of the lessor remains largely in line with previous IAS 17 requirements. The effective date for IFRS 16 is January 1, 2019. The Company is in the process of evaluating the impact of IFRS 16 but it does not expect IFRS 16 to significantly impact the financial statements.

IFRS 17 Insurance Contracts

IFRS 17 Insurance Contracts, supersedes IFRS 4 Insurance Contracts. IFRS 17 establishes the principles for the recognition, measurement, presentation and disclosure of insurance contracts. IFRS 17 requires entities to measure insurance contract liabilities using updated estimates and assumptions that reflect the timing of cash flows and any uncertainty relating to insurance contracts. Additionally, IFRS 17 requires entities to recognize profits as it delivers insurance services. The effective date for IFRS 17 is January 1, 2021. However, the International Accounting Standards Board has proposed delaying the effective date to January 1, 2022. The Company has not yet determined the impact of adoption, however it is expected to significantly impact the overall financial statements.

IFRS 23 Uncertainty over Income Tax Treatments

IFRIC 23 Uncertainty over Income Tax Treatments provides guidance on recognition and measurement of uncertain income tax treatments. The effective date for IFRIC 23 is January 1, 2019. The Company is in the process of evaluating the impact of this interpretation.

17. Comparative Figures

Certain comparative figures have been reclassified to conform with the method of presentation adopted for the current year.