



124th ANNUAL REPORT



**Ayr Farmers
Mutual**
Insurance Company

2017 FINANCIAL STATEMENTS

YOU'RE INVITED TO THE 124th Annual General Meeting

TAKE NOTICE that an Annual General Meeting of the Members of Ayr Farmers Mutual Insurance Company will be held at the head office of Ayr Farmers Mutual Insurance Company, 1400 Northumberland Street, Ayr, Ontario on the 2nd day of March, 2018 at the hour of 2:00 p.m. for the purposes of:

- 1** To receive, consider and approve the annual statements for the year ending December 31st, 2017;
- 2** To appoint auditors for 2018;
- 3** To approve the amendment to article 20(e) of Bylaw #5 passed by the Directors on April 11, 2017, which adds to section 20(e) that no person shall seek election to fill a vacancy on the Board if he or she seeks election to a three (3) year term, and that his or her notice of intention shall specify if he or she is seeking election to fill the vacancy or the three (3) year term;
- 4** To elect two directors for a three (3) year term. The members will be asked to elect two Directors for a period of three years, the retiring directors being Cathy Formica and Jason Vernooy. Both are eligible for re-election.

The annual statement will be made available on the website of Ayr Farmers Mutual no later than 21 days prior to the Annual General Meeting. A member may obtain a copy of the annual statement by sending a written request to the head office at least 14 days prior to the Annual General Meeting.

By order of the Board of Directors, dated at Ayr, Ontario, this 13th day of December 2017.



Dave Paterson, BBA
CORPORATE SECRETARY

To review the minutes from the 122nd Annual General Meeting held on Friday March 4th, 2016, please visit www.ayrmutual.com

Any person wishing to seek election or re-election as a Director must file their intention to stand for election, in writing, with the Corporate Secretary before 12:00 noon, at least forty five (45) days in advance of the Annual General Meeting. Forms are available from the Corporate Secretary at the Head Office during regular business hours. For more information on becoming a Director, please refer to the "Become a Director" document under the "People" tab on the company's website, www.ayrmutual.com.



MESSAGE FROM THE CHAIR

I am pleased to report the activities of your Board of Directors at Ayr Farmers Mutual Insurance Company for the year ended 2017.

Ayr Farmers Mutual achieved excellent financial results in 2017. We value each and every policyholder as you are essential to our success and we thank you for your continued support.

Your board of directors was active throughout the year attending various meetings, committee work and governance sessions to improve oversight responsibilities. To expand the overall performance of directors and the board as whole we have engaged the services of Sandi Verrechia at Satori Consulting. Sandi has assisted the board in its peer review process and has been added to the Nominating Committee to provide independent participation in fulfilling this mandate. Sandy also attended the Board Strategic Planning session, where an overview of board responsibilities and improved governance responsibilities were identified. We look forward to working with Sandi in the future.

Each year, the financial statement is presented by the auditors for the board to receive. At that time, the board may consider if a refund of premiums to qualifying policyholders is possible after considering the company's financial position, future strategic plans and expected premium growth. Consideration was given to future strategic plans and expected premium growth within our next 2 - 3 years. After thorough assessment, your Board has declared a 5% refund of premiums to all qualifying non-automobile policyholders, reinforcing that Ayr Farmers Mutual will remain a leader in the mutual insurance industry.

I would like to take this opportunity to thank the staff of Ayr Farmers Mutual for their dedication and commitment over the past year. Ayr Farmers Mutual has a great team and they play a significant role in defining our success.

Thank you to my fellow directors for fulfilling their duties and responsibilities as board members and for supporting me as your Chair this past year.

Ayr Farmers Mutual is very excited about our future as we move into our 125th year of business. We look forward to celebrating this milestone with each of you.

Sincerely,

A handwritten signature in black ink that reads "Brian Sayles". The signature is fluid and cursive, with the first name "Brian" and last name "Sayles" clearly legible.

Brian Sayles
BOARD CHAIR



MESSAGE FROM THE PRESIDENT & CEO

It is my pleasure to present the financial statements for the year ended 2017.

I would like to take this opportunity to thank our many Policyholders for their continued support of Ayr Farmers Mutual Insurance Company. We value the opportunity to serve you as Mutual members.

On December 13th, 2017, Ayr Farmers completed its 124th year of operation. We are now entering our 125th year in business and look forward to celebrating and sharing this accomplishment with the communities and people we serve. Ayr Farmers Mutual was started out of a necessity to help a community provide financial protection against loss. These core values and purpose remain in effect today and serve as guiding principles to our Mutual insurance belief. A community family fun day is scheduled for Saturday, June 16, 2018 at the North Dumfries Community Centre from 11 am to 3 pm. All are welcome to join us for this free event, and to enjoy food, games, activities and entertainment to suit all ages.

AFM has experienced a very strong year of financial performance. Our premiums have grown by 7.7% to nearly \$30 million, with policies of insurance in effect growing to nearly 20,000. We have obtained positive underwriting results with an overall claims loss ratio of 55% and a total combined ratio of 87.2%, when factoring in expenses.

Investment performance in 2017 provided a rate of return of 5% and an additional \$3.6 million to improve our overall comprehensive income to \$4.9 million. After considering the company's overall financial position, long term strategic initiatives and anticipated premium growth, your Board of Directors declared a refund of premiums at 5% of non-automobile premiums to qualifying policyholders.

Over the course of this past year, AFM continued to focus on our long term planning. We have initiated a new process for strategic planning and have welcomed new expertise to the organization. We are excited about our future and look forward to serving our Policyholders through improved operational excellence and customer service. We are committed to advancing our mission and vision.

Your company continues to support numerous community and non-profit organizations through financial contribution. We congratulate the many volunteers who provide countless hours of commitment to these organizations. Your efforts in these activities make up the fabric and foundations within our community. In addition, we provide scholarship opportunities for children of Policyholders. We encourage you to check our website for details on how your child may apply.

CONTINUED ON NEXT PAGE

I look forward to celebrating our 125th year of service with each of you. Our dedicated team of staff, agents and brokers enjoy the privilege of serving each of our Policyholders.

On behalf of everyone at Ayr Farmers Mutual, thank you for your business. We are your neighbours and your insurance company.

Sincerely,



Jeff Whiting CIP
PRESIDENT & CEO

BOARD OF DIRECTORS



L-R: Gerry Pullin, Past Chair; Cathy Formica, Vice Chair; Dave Thompson, Director; Jason Vernooy, Director; Elizabeth Baldwin, Director; Brian Sayles, Board Chair.



**Ayr Farmers
Mutual**
Insurance Company

FINANCIAL STATEMENTS

Year Ended December 31, 2017





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**Ayr Farmers
Mutual**
Insurance Company

**MANAGEMENT RESPONSIBILITY FOR FINANCIAL REPORTING
DECEMBER 31, 2017**

The accompanying financial statements and all other information contained in this annual report are the responsibility of the management of Ayr Farmers Mutual Insurance Company. The financial statements have been prepared by management in accordance with International Financial Reporting Standards (including the accounting requirements of the Financial Services Commission of Ontario) and have been approved by the Board of Directors.

Preparation of financial information is an integral part of management's broader responsibilities for the ongoing operations of Ayr Farmers Mutual Insurance Company, which includes adherence by all employees to the company's Code of Conduct. Management maintains a system of internal accounting controls to provide reasonable assurance that transactions are accurately recorded on a timely basis, are properly approved and result in reliable financial information. Such information also includes data based on management's best estimates and judgements.

The Audit Committee and the Board of Directors review and approve the annual financial statements. In addition, the Audit Committee meets periodically with financial officers of Ayr Farmers Mutual Insurance Company and the external auditors, and reports to the Board of Directors thereon. The Audit Committee and Board of Directors also review the annual report in its entirety.

The accompanying financial statements have been audited by Graham Mathew Professional Corporation, authorized to practise public accounting by the Chartered Professional Accountants of Ontario, who are engaged by the Board of Directors and whose appointment was ratified at the annual meeting of the policyholders. The auditors have access to the Audit Committee, without management present, to discuss the results of their work. Their report dated January 19, 2018 expresses their unqualified opinion on the Company's 2017 financial statements.

A handwritten signature in black ink, appearing to read 'Jeff Whiting'.

Jeff Whiting, CIP
President & CEO

A handwritten signature in black ink, appearing to read 'David Paterson'.

David Paterson, BBA
Chief Financial Officer

INDEPENDENT AUDITORS' REPORT

To the Policyholders of
Ayr Farmers Mutual Insurance Company

We have audited the accompanying financial statements of **Ayr Farmers Mutual Insurance Company**, which comprise the statement of financial position as at December 31, 2017, and the statements of comprehensive income, policyholders' equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility 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.

Auditors' Responsibility

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 comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the financial statements 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. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of **Ayr Farmers Mutual Insurance Company** as at December 31, 2017, and its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.



Cambridge, Ontario
January 19, 2018

Chartered Professional Accountants, authorized to practise public
accounting by the Chartered Professional Accountants of Ontario



**FINANCIAL POSITION
DECEMBER 31, 2017**

	2017 \$	2016 \$
ASSETS		
Cash and investments (note 4)	75,960,990	71,134,935
Due from reinsurer (note 6)	68,941	44,880
Premiums receivable	7,251,670	6,550,714
Receivable from Facility Association	32,505	25,010
Reinsurer's share of provision for unpaid claims (note 6)	6,725,543	6,281,392
Deferred policy acquisition expenses (note 6)	1,788,607	1,639,418
Property, plant and equipment (note 5)	2,550,525	2,721,015
Deferred income taxes	303,000	288,000
	94,681,781	88,685,364
LIABILITIES		
Provision for unpaid claims (note 6)	21,867,635	21,496,043
Unearned premiums (note 6)	14,479,689	13,443,012
Accounts payable and accrued liabilities	1,127,955	966,013
Income taxes payable	366,378	288,883
Provision for refund from premiums	821,000	1,415,000
	38,662,657	37,608,951
POLICYHOLDERS' EQUITY		
Policyholders' equity (page 5)	56,019,124	51,076,413
	94,681,781	88,685,364

APPROVED BY THE BOARD:

Director

Director



**STATEMENT OF COMPREHENSIVE INCOME
YEAR ENDED DECEMBER 31, 2017**

	2017 \$	2016 \$
Gross premiums written	29,851,720	27,723,283
Deduct		
Reinsurance premiums	2,209,619	2,004,052
Increase in reserve for unearned premiums	1,036,677	906,436
	3,246,296	2,910,488
Net premiums earned	26,605,424	24,812,795
Service charge revenue	204,159	340,772
Net underwriting revenue	26,809,583	25,153,567
Direct losses incurred		
Gross claims and adjusting expenses	16,180,131	15,099,228
Reinsurer's share of claims and adjusting expenses	(1,431,784)	(973,833)
	14,748,347	14,125,395
Expenses		
Fees, commissions and other acquisition expenses (note 9)	3,719,372	3,414,770
Other operating and administrative expenses (note 10)	4,916,494	4,889,689
	8,635,866	8,304,459
Underwriting profit	3,425,370	2,723,713
Other revenue (expense)		
Investment income (note 12)	3,567,325	3,374,807
Refund from premiums	(778,055)	(1,403,567)
	2,789,270	1,971,240
Income before income tax expense	6,214,640	4,694,953
Income tax expense (note 8)		
Current	(1,286,929)	(920,445)
Deferred	15,000	
	(1,271,929)	(920,445)
Net income, being total comprehensive income for year	4,942,711	3,774,508

The explanatory financial notes form an integral part of these financial statements.



**STATEMENT OF POLICYHOLDERS' EQUITY
YEAR ENDED DECEMBER 31, 2017**

	2017	2016
	\$	\$
Balance at beginning of year	51,076,413	47,301,905
Net income, being total comprehensive income for year	4,942,711	3,774,508
Balance at end of year	56,019,124	51,076,413



**STATEMENT OF CASH FLOWS
YEAR ENDED DECEMBER 31, 2017**

	2017 \$	2016 \$
Cash flows from operating activities:		
Net income, being total comprehensive income for year	4,942,711	3,774,508
Items not involving cash:		
Amortization and depreciation	349,901	330,281
Amortization, bonds	9,562	9,550
Deferred income tax	(15,000)	
Unrealized gains on investments	(598,626)	(900,746)
	4,688,548	3,213,593
Net change in non-cash working capital balances relating to operations:		
Unearned premiums	1,036,677	906,436
Reinsurer's share of provision for unpaid claims	(444,151)	(526,379)
Provision for unpaid claims	371,592	(774,804)
Other payables	239,441	454,820
Receivables, premiums and other	(732,512)	(451,994)
Deferred policy acquisition expenses	(149,189)	(131,919)
	5,010,406	2,689,753
Cash flows from investment activities:		
Proceeds from sale of investments	40,336,278	39,278,686
Purchase of investments	(41,930,949)	(46,672,536)
Net additions to property, plant and equipment and intangible assets	(179,412)	(259,110)
Investment income due and accrued	17,884	17,441
Recognized gains on investments	(865,491)	(335,388)
	(2,621,690)	(7,970,907)
Cash flows from financing activities:		
Provision for refund from premiums, net change	(594,000)	760,000
Increase (decrease) in cash during year	1,794,716	(4,521,154)
Cash, beginning of year	5,707,729	10,228,883
Cash, end of year (note 4)	7,502,445	5,707,729

The explanatory financial notes form an integral part of these financial statements.



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

1. Nature of Operations and Summary of Significant Accounting Policies

(a) Reporting entity

Ayr Farmers Mutual Insurance Company (the Company) is incorporated under the laws of Ontario and is subject to the Ontario Insurance Act. It is licensed to write property, liability, automobile, aircraft and farmers' accident insurance in Ontario. The Company's head office is located at 1400 Northumberland Street in Ayr, Ontario.

The Company is subject to rate regulation in 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. 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. 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 January 19, 2018.

(b) Basis of presentation

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

These financial statements were prepared on a historical cost basis except for those financial assets and financial liabilities that have been measured at fair value.

The Company's functional and presentation currency is the Canadian dollar. The financial statements are presented in Canadian dollars.

The preparation of financial statements in compliance with IFRS requires management to make certain critical accounting estimates. It also requires management to exercise judgement in applying the Company's accounting policies. The areas involving a higher degree of judgement of complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in note 2.

(c) 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 GAAP.

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

(i) 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 brokers and exclusive of taxes levied on premiums. The Company earns premium income evenly over the term of the insurance policy generally 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.



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

1. Nature of Operations and Summary of Significant Accounting Policies (Continued)

(c) Insurance contracts (continued)

(ii) Reinsurance

The company reflects reinsurance balances on the statement of financial position on a gross basis to indicate the extent of credit risk related to reinsurance and its obligations to policyholders and in the statement of comprehensive income to indicate the results of its retention of premiums written.

Reinsurance premiums ceded and reinsurance recoveries on losses incurred are recorded as reductions of the respective income and expense accounts. A contingent liability exists with respect to reinsurance ceded which could become a liability of the Company in the event that the reinsurer might be unable to meet its obligation under the reinsurance agreements. The Company ascertained that no provision is necessary at December 31 for doubtful collection of reinsurance recoveries.

(iii) Deferred policy acquisition expenses

Acquisition costs are comprised of agents' and brokers' commissions. 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.

(iv) Provisions for unpaid claims and adjustment expenses

Individual loss estimates are provided on each claim reported. In addition, provisions are made for adjustment expenses, 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 an undiscounted basis.

(v) 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 investment return. If that assessment shows that the carrying amount of the liabilities is inadequate, any deficiency is recognized as an expense to the statement of comprehensive income initially by writing off the deferred policy acquisition expense and subsequently by recognizing an additional claims liability for claims provisions.

(vi) Reinsurer's share of provisions for unpaid claims and adjustment expenses

The Company enters into reinsurance contracts in the normal course of business in order to limit potential losses arising from certain exposures. 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 when due.

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.



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

1. Nature of Operations and Summary of Significant Accounting Policies (Continued)

(c) Insurance contracts (continued)

(vii) Salvage and subrogation recoverable

In the normal course of business, the Company obtains the ownership of damaged property, which they resell to various salvage operations. Unsold property is valued at its estimated net realizable value.

Where the Company indemnifies policyholders against a liability claim, it acquires rights to subrogate its claim against other parties. These claims are reflected at amounts expected to be received from the subrogated parties net of related costs.

(viii) Refund from premium

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

(d) Structured settlements, Fire Mutuals Guarantee Fund and financial guarantee contracts

The Company enters into annuity agreements with various life insurance companies to provide for fixed and recurring payments to claimants. 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 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 insolvent. As a result, the Company may be required to contribute assets to their proportionate share in meeting this objective.

These exposures represent financial guarantee contracts. The Company accounts for financial guarantee contracts in accordance with IFRS 4, Insurance Contracts.

(e) Financial instruments

The Company classifies its financial instruments into one of the following categories based on the purpose for which the asset was acquired or liability incurred. All transactions related to financial instruments are recorded on a trade date basis. The Company's accounting policy for each category is as follows:

(i) Held-to-maturity financial assets

If the Company has the positive intent and ability to hold debt securities to maturity, then such financial assets are classified as held-to-maturity. Held-to-maturity financial assets are recognized initially at fair value plus any directly attributable transactions costs. Subsequent to initial recognition held-to-maturity financial assets are measured at amortized cost using the effective interest method, less any impairment losses. Any sale or reclassification of a more than insignificant amount of held-to-maturity investments not close to their maturity would result in the reclassification of all held-to-maturity investments as fair value through profit and loss, and prevent the Company from classifying investment securities as held-to-maturity for the current and the following two financial years.



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

1. Nature of Operations and Summary of Significant Accounting Policies (Continued)

(e) Financial instruments (continued)

(ii) Financial assets at fair value through profit or loss

A financial asset is classified at fair value through profit or loss if it is classified as held-for-trading or is designated as such upon initial recognition. Financial assets are designated as fair value through profit or loss if the Company manages such investments and makes purchase and sale decisions based on their fair value in accordance with the Company's documented risk management or investment strategy. Upon initial recognition, attributable transaction costs are recognized in profit or loss as incurred. Financial assets at fair value through profit or loss are measured at fair value, and changes therein are recognized in profit or loss.

(iii) Loans and receivables

These assets are non-derivative financial assets resulting from the delivery of cash or other assets by a lender to a borrower in return for a promise to repay on a specified date or dates, or on demand. They are initially recognized at fair value plus transaction costs that are directly attributable to their acquisition or issue and subsequently carried at amortized cost, using the effective interest rate method, less any impairment losses.

Impairment provisions are recognized when there is objective evidence (such as significant financial difficulties on the part of the counterparty or default or significant delay in payment) that the Company will be unable to collect all of the amounts due under the terms receivable, the amount of such a provision being the difference between the net carrying amount and the present value of the future expected cash flows associated with the impaired receivable. For amounts due from policyholders and reinsurer, which are reported net, such provisions are recorded in a separate allowance account with the loss being recognized in net income. On confirmation that the amounts receivable will not be collectable, the gross carrying value of the asset is written off against the associated provision.

(iv) Other financial liabilities

Other financial liabilities include all financial liabilities and comprise accounts payable, and other short-term monetary liabilities. These liabilities are initially recognized at fair value net of any transaction costs directly attributable to the issuance of the instrument and subsequently carried at amortized cost using the effective interest rate method, which ensures that any interest expense over the period to repayment is at a constant rate on the balance of the liability carried in the statement of financial position. Interest expense in this context includes initial transaction costs and premiums payable on redemption, as well as any interest or coupon payable while the liability is outstanding.

(f) Facility Association

As a member of the Facility Association, the Company records its proportionate share of the Association's revenue, expenses, unearned premiums and provision for unpaid claims.

(g) Income taxes

Income tax expense includes current and deferred tax. Current tax and deferred tax are recognized in net income except to the extent that it relates to a business combination, or items recognized directly in policyholders' equity or in other comprehensive income.

Current income taxes are recognized for the estimated income taxes payable or receivable on taxable income or loss for the current year and any adjustment to income taxes payable in respect of previous years. Current income taxes are determined using tax rates and tax laws that have been enacted or substantively enacted by the year-end date.



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

1. Nature of Operations and Summary of Significant Accounting Policies (Continued)

(g) Income taxes (continued)

Deferred tax assets and liabilities are recognized where the carrying amount of an asset or liability differs from its tax base. The amount is determined using tax rates and tax laws that have been enacted or substantively enacted by the year-end date and are expected to apply when the liabilities / (assets) are settled / (recovered).

(h) Pension plan

The Company participates in a multi-employer defined benefit pension plan. However, sufficient information is not available to use defined benefit accounting. Therefore, the Company accounts for the plan as if it were a defined contribution plan, recognizing contributions as an expense in the year to which they relate.

(i) Standards, amendments and interpretations not yet effective

Certain new standards, amendments and interpretations have been published that are mandatory for the Company's accounting periods beginning on or after January 1, 2018 or later periods that the Company has decided not to early-adopt.

- IFRS 9 Financial Instruments amends the requirements for classification and measurement of financial assets, impairment, and hedge accounting. IFRS 9 introduces an expected loss model of impairment and retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortized cost, fair value through profit or loss, and fair value through other comprehensive income (loss). The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. The effective date for IFRS 9 is January 1, 2018; however, insurance entities have been provided the option of deferring the adoption of IFRS 9 until January 1, 2021, which is the effective date of IFRS 17, Insurance Contracts. The Company does not plan to defer the effective date of IFRS 9 and therefore expects to adopt IFRS 9 on January 1, 2018.

The Company expects that its investments will continue to be classified at fair value through profit or loss based on the business model assessment, therefore, the adoption of IFRS 9 is not expected to have a material impact on the Company's financial position or performance.

- IFRS 17 Insurance Contracts supersedes IFRS 4 Insurance Contracts. IFRS 17 fundamentally changes how entities account for insurance contracts, introducing a default "building block approach", which disaggregates the cash flows in an insurance contract and provides a different measurement basis for each component, and a simplified "premium allocation approach" for certain short-term contracts. Assumptions used in measuring insurance assets and liabilities such as cash flows, discount rates and risk adjustment will be updated at each reporting period. The discount rate will reflect the characteristics of the insurance liabilities and the estimated future cash flows to settle claims incurred will be discounted unless the period of time between claim occurrence and settlement is less than one year. Presentation changes include 'insurance revenue' replacing the current reporting of 'written premiums' and 'earned premiums' and insurance contract assets and liabilities will not be netted. Under this standard, premiums receivable, unearned premiums and claims payable may no longer be presented separately from other insurance assets and liabilities. The effective date for IFRS 17 is January 1, 2021 with mandatory restatement of comparative periods. The Company is currently assessing the impact of IFRS 17.

**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

2. Critical Accounting Estimates and Judgements

The preparation of these financial statements in conformity with IFRS requires management to make certain critical estimates. It also requires management to exercise judgement in applying the Company's accounting policies. The areas involving critical judgements 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 include primarily the calculation and determination of unpaid claims and the related reinsurer's share (note 6).

3. Financial Instrument Classification

The carrying amount of the Company's financial instruments by classification is as follows:

	Held to maturity \$	Fair value through profit or loss \$	Loans and receivables \$	Other financial liabilities \$	Total \$
December 31, 2017					
Cash		7,502,445			7,502,445
Investments (note 4)	5,610,777	60,587,866			66,198,643
Due from reinsurer and premiums receivable			7,320,611		7,320,611
Investment income accrued			117,285		117,285
Loan receivable			2,142,617		2,142,617
Accounts payable and accrued liabilities				(1,127,955)	(1,127,955)
	5,610,777	68,090,311	9,580,513	(1,127,955)	82,153,646
December 31, 2016					
Cash		5,707,729			5,707,729
Investments (note 4)	5,161,608	57,723,316			62,884,924
Due from reinsurer and premiums receivable			6,595,594		6,595,594
Investment income accrued			135,168		135,168
Loan receivable			2,407,114		2,407,114
Accounts payable and accrued liabilities				(966,013)	(966,013)
	5,161,608	63,431,045	9,137,876	(966,013)	76,764,516

The above fair value through profit and loss investments have been designated as such upon initial recognition.



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

4. Investments

The following table provides cost and fair value information of investments by type of security and issuer. The maximum exposure to credit risk would be the fair value as shown below.

The book values and market values of cash and investments as at December 31 were as follows:

	2017		2016	
	<u>Book value</u>	<u>Market value</u>	<u>Book value</u>	<u>Market value</u>
	\$	\$	\$	\$
Cash	7,502,445	7,502,445	5,707,729	5,707,729
Debt securities	43,226,162	43,370,825	41,869,589	42,131,926
Preferred shares	7,255	7,255	7,254	7,254
Common shares	22,965,226	22,965,226	21,008,081	21,008,081
Loan receivable	2,142,617	2,142,617	2,407,114	2,407,114
Accrued interest	117,285	117,285	135,168	135,168
	75,960,990	76,105,653	71,134,935	71,397,272

The market value of the debt securities and preferred and common shares is based on quoted market values.

	2017	2016
	\$	\$
The debt securities mature as follows:		
Within 1 year	2,769,788	1,608,993
Over 1 to 5 years	24,741,986	23,393,755
Over 5 years	15,859,051	17,129,178
	43,370,825	42,131,926

Loan receivable matures as follows:

Over 5 years	2,142,617	2,407,114
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The effective investment yield for the year is 5.0% (5.0% for 2016).

The book value of the investments is shown in the following tables categorized by fair value through profit or loss, held-to-maturity and loans and receivables. Book values are equal to their fair values. The maximum exposure to credit risk would be the fair value indicated.



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

4. Investments (Continued)

a) Financial assets at fair value through profit or loss

	2017		2016	
	<u>Cost</u>	<u>Fair value (Book value)</u>	<u>Cost</u>	<u>Fair value (Book value)</u>
	\$	\$	\$	\$
Debt securities:				
Corporate				
A or better	13,715,251	13,671,147	13,954,062	13,947,169
Below A	2,495,115	2,496,060	2,091,930	2,052,248
Pooled funds	21,630,530	21,379,220	20,656,614	20,640,709
Fire Mutual Guarantee Fund	68,958	68,958	67,855	67,855
	37,909,854	37,615,385	36,770,461	36,707,981
Equity investments:				
Canadian common	9,283,475	10,478,601	10,601,078	11,609,137
Canadian preferred	5,000	7,255	5,000	7,254
U.S. equities	11,220,670	12,486,625	8,776,533	9,398,944
	20,509,145	22,972,481	19,382,611	21,015,335
	58,418,999	60,587,866	56,153,072	57,723,316

b) Held-to-Maturity

	2017		2016	
	<u>Cost</u>	<u>Fair value (Book value)</u>	<u>Cost</u>	<u>Fair value (Book value)</u>
	\$	\$	\$	\$
Debt securities:				
Provincial	3,791,513	3,791,513	3,435,180	3,435,180
Municipal	1,819,264	1,819,264	1,726,428	1,726,428
	5,610,777	5,610,777	5,161,608	5,161,608

c) Loans and receivables

Loan receivable	2,142,617	2,142,617	2,407,114	2,407,114
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The following table provides an analysis of the 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 that the entity can access at the measurement date;
- 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



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

4. Investments (Continued)

- 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).

On December 31, 2017 and December 31, 2016, the company held only Level 1 and 2 investments.

	Level 1 \$	Level 2 \$	Level 3 \$	Total \$
December 31, 2017				
Cash and cash equivalents	7,502,445			7,502,445
Bonds				
Corporate		16,167,207		16,167,207
Fire Mutual Guarantee Fund		68,958		68,958
Pooled funds				
Canadian fixed income		21,379,220		21,379,220
Canadian equity		8,467,625		8,467,625
U.S. equity		10,633,341		10,633,341
Equity investments				
Canadian	2,010,976	7,255		2,018,231
U.S.				NIL
Mutual funds		1,853,284		1,853,284
Total assets measured at fair value	9,513,421	58,576,890	NIL	68,090,311

	Level 1 \$	Level 2 \$	Level 3 \$	Total \$
December 31, 2016				
Cash and cash equivalents	5,707,729			5,707,729
Bonds				
Corporate		15,999,417		15,999,417
Fire Mutual Guarantee Fund		67,855		67,855
Pooled funds				
Canadian fixed income		20,640,709		20,640,709
Canadian equity		8,512,905		8,512,905
U.S. equity		4,482,332		4,482,332
Equity investments				
Canadian	3,096,232	7,254		3,103,486
U.S.	3,203,439			3,203,439
Mutual funds		1,713,173		1,713,173
Total assets measured at fair value	12,007,400	51,423,645	NIL	63,431,045

There were no transfers between Level 1 and Level 2 for the years ended December 31, 2017 and 2016.



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

5. Property, Plant and Equipment and Intangible Assets

Property, plant and equipment is initially recorded at cost and subsequently measured at cost less accumulated depreciation and accumulated impairment losses, with the exception of land which is not depreciated. Depreciation is recognized in net income and is provided over the estimated useful lives of the assets, using the straight-line method (years) or declining-balance method (percentage).

Intangible assets consist of computer software which are not integral to the computer hardware owned by the company. Software is initially recorded at cost and subsequently measured at cost less accumulated amortization and accumulated impairment losses. The amortization expense is included within other operating and administrative expenses in the statement of comprehensive income and is provided over the estimated useful life of the asset.

		2017		
	Depreciation rate	Cost	Accumulated Depreciation	Net Book Value
Land		154,073		154,073
Buildings	4%	3,437,663	1,393,690	2,043,973
Computer hardware	3 years	647,797	546,627	101,170
Furniture and fixtures	5 years	1,037,977	920,713	117,264
Vehicles	30%	192,838	65,549	127,289
Computer software	3 years	78,071	71,315	6,756
		5,548,419	2,997,894	2,550,525

		2016		
	Depreciation rate	Cost	Accumulated Depreciation	Net Book Value
Land		154,073		154,073
Buildings	4%	3,415,231	1,308,524	2,106,707
Computer hardware	3 years	620,883	460,861	160,022
Furniture and fixtures	5 years	1,026,070	800,801	225,269
Vehicles	30%	93,050	29,366	63,684
Computer software	3 years	78,071	66,811	11,260
		5,387,378	2,666,363	2,721,015

The unamortized cost of capital assets available to reduce net income for income tax purposes amounts to approximately \$2,451,000 (\$2,560,000 in 2016).



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

	2017 \$	2016 \$
6. Insurance Contracts		
Due From Reinsurer		
Balance, beginning of year	44,880	24,202
Submitted to reinsurer	1,005,633	500,454
Received from reinsurer	(981,572)	(479,776)
Balance, end of year	68,941	44,880

All of the above amounts are expected to be settled within one year. At year-end, the company reviewed the amounts owing from its reinsurer and determined that no allowance is necessary.

Reinsurer's Share of Provision For Unpaid Claims

Balance, beginning of year	6,281,392	5,755,013
New claims reserve	1,600,114	92,099
Change in prior years reserve	(150,330)	934,734
Submitted to reinsurer	(1,005,633)	(500,454)
Balance, end of year	6,725,543	6,281,392

Expected settlement		
Within one year	664,266	57,099
More than one year	6,061,277	6,224,293
	6,725,543	6,281,392

Deferred Policy Acquisition Expenses

Balance, beginning of year	1,639,418	1,507,499
Acquisition costs incurred	3,791,328	3,466,449
Expense recognized as a result of liability adequacy tests	NIL	NIL
Expensed during the year	(3,642,139)	(3,334,530)
Balance, end of year	1,788,607	1,639,418

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

Unearned Premiums (UEP)

Balance, beginning of year	13,443,012	12,536,576
Premiums written	29,851,720	27,723,283
Premiums earned during year	(28,815,043)	(26,816,847)
Increase in reserve for unearned premiums	1,036,677	906,436
Balance, end of year	14,479,689	13,443,012



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

6. Insurance Contracts (Continued)

Insurance Contract Provisions and Related Reinsurance Assets

The following is a summary of the insurance contract provisions and related reinsurance assets.

	Gross \$	Re-insurance \$	Net \$
December 31, 2017			
Outstanding claims provision			
Long settlement term	13,600,540	4,143,277	9,457,263
Short settlement term	3,275,644	664,266	2,611,378
Facility Association and other residual pools	438,887		438,887
Provisions for claims incurred but not reported, net	4,552,564	1,918,000	2,634,564
Balance, end of year	21,867,635	6,725,543	15,142,092

	Gross \$	Re-insurance \$	Net \$
December 31, 2016			
Outstanding claims provision			
Long settlement term	13,535,814	4,324,293	9,211,521
Short settlement term	3,118,934	57,099	3,061,835
Facility Association and other residual pools	427,617		427,617
Provisions for claims incurred but not reported, net	4,413,678	1,900,000	2,513,678
Balance, end of year	21,496,043	6,281,392	15,214,651

Comments and Assumptions For Specific Claims Categories

The ultimate cost of long settlement general liability claims are difficult to predict for several reasons. Claims may not be reported until a number of years after a policy expires. Changes in the legal environment have created 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 liabilities provided by the actuaries of the pools.

Claims and Adjustment Expenses

Changes in claim liabilities recorded in the statement of financial position for the years ended December 31, 2017 and 2016 and their impact on claims and adjustment expenses:



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

6. Insurance Contracts (Continued)

	2017	2016
	\$	\$
Balance, beginning of year	21,496,043	22,270,847
New claims reserve	7,605,748	4,221,576
Change in prior years reserve	(23,060,692)	(20,923,412)
Paid claims		
Current year	9,777,468	9,226,409
Prior years	6,049,068	6,700,623
Balance, end of year	21,867,635	21,496,043
Expected settlement		
Within one year	2,903,774	2,758,825
More than one year	18,963,861	18,737,218
	21,867,635	21,496,043

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

Claim Development

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 historical delays in reporting claims. In general, the longer the term required for the settlement of a group of claims the more variable the estimates. Short-term settlement claims are those which are expected to be substantially paid within a year of being reported.

The tables that follow present the development of claims payments and the estimated ultimate cost of claims for the claim years 2008 to 2017. The upper half of the tables show the cumulative amounts paid or estimated to be paid during successive years related to each claim year. The original estimates will be increased or decreased, as more information becomes known about the original claims and overall claim frequency and severity.



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

6. Insurance Contracts (Continued)

Gross Claims	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Total
	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$
Gross estimate of cumulative claims cost											
At the end year of claim	13,120,618	12,359,764	12,816,679	13,658,668	12,601,391	14,651,019	19,407,545	15,516,349	16,266,985	20,066,216	
One year later	10,981,483	10,897,230	10,140,484	13,293,461	9,663,620	12,939,173	18,318,339	14,105,907	15,238,583		
Two years later	9,601,423	9,223,315	9,691,527	12,176,078	9,288,451	12,691,808	17,702,555	13,134,710			
Three years later	9,628,495	8,804,158	8,336,437	12,270,642	9,046,875	12,979,054	15,585,288				
Four years later	9,376,148	8,375,109	7,934,522	11,968,882	9,008,733	13,131,414					
Five years later	9,142,538	8,312,475	7,843,812	12,524,205	9,044,265						
Six years later	8,792,999	8,231,636	7,840,491	12,722,041							
Seven years later	8,646,139	8,167,704	7,780,446								
Eight years later	8,655,741	8,167,902									
Nine years later	8,660,277										
Current estimate of cumulative claims cost	8,660,277	8,167,902	7,780,446	12,722,041	9,044,265	13,131,414	15,585,288	13,134,710	15,238,583	20,066,216	123,531,142
Cumulative payments	8,586,266	8,167,902	7,722,771	12,378,515	8,864,109	11,164,611	12,069,788	10,741,400	12,433,510	9,777,468	101,906,340
Outstanding claims	74,011		57,675	343,526	180,156	1,966,803	3,515,500	2,393,310	2,805,073	10,288,748	21,624,802
Outstanding claims 2007 and prior											242,833
Total gross outstanding claims and handling expenses											21,867,635



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

6. Insurance Contracts (Continued)

Net Claims	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Total
	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$
Net estimate of cumulative claims cost											
At the end year of claim	11,413,358	11,567,725	11,807,507	13,241,436	11,073,407	13,105,450	15,242,298	14,631,176	15,309,443	17,354,221	
One year later	9,401,792	9,247,353	8,976,188	12,054,247	8,580,020	11,903,065	14,334,092	13,440,454	14,516,147		
Two years later	8,220,579	8,431,072	8,222,256	11,442,615	8,514,588	11,995,006	13,497,553	12,925,710			
Three years later	8,164,644	8,077,217	7,910,710	11,389,487	8,452,916	12,493,087	12,042,304				
Four years later	7,951,297	7,778,141	7,546,795	11,388,328	8,457,721	12,545,963					
Five years later	7,779,854	7,738,731	7,468,085	11,876,122	8,514,253						
Six years later	7,715,626	7,657,892	7,464,764	11,973,384							
Seven years later	7,580,372	7,606,223	7,405,719								
Eight years later	7,589,974	7,606,421									
Nine years later	7,594,541										
Current estimate of cumulative claims cost	7,594,510	7,606,421	7,405,719	11,973,384	8,514,253	12,545,963	12,042,304	12,925,710	14,516,147	17,354,221	112,478,632
Cumulative payments	7,520,499	7,606,421	7,348,044	11,777,364	8,337,097	10,936,672	11,310,858	10,741,400	12,304,079	9,549,587	97,432,021
Outstanding claims	74,011		57,675	196,020	177,156	1,609,291	731,446	2,184,310	2,212,068	7,804,634	15,046,611
Outstanding claims 2007 and prior											95,481
Total net outstanding claims and claims handling expenses											15,142,092



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

7. 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. 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 defined benefit plan has been closed to future eligible employees effective January 1, 2017. As of that date future eligible employees will be enrolled in the defined contribution plan.

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. 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.

During 2017, the amount contributed to the plan for current service was \$383,230 (\$359,102 in 2016) and the amount contributed for the solvency funded status deficit was \$368,354 (\$606,105 in 2016). These amounts have been recognized in comprehensive income. The Company had a 5.1% share of the total contributions to the Plan in 2017. The expected contribution to the Plan for 2018 is \$401,000.

An actuarial valuation of the Pension Plan as of December 31, 2016 showed a going-concern surplus position. The next actuarial valuation to be filed under the Pension Benefit Act will be as of December 31, 2019.

8. Income Taxes

The Company is subject to income taxes on that portion of its income derived from insuring other than farm related risks.

Reasons for the difference between tax expense for the year and the expected income taxes based on the statutory tax rate of 26.5% (26.5% in 2016) are as follows:

	2017 \$	2016 \$
Income before income taxes	6,214,640	4,694,953
Expected taxes based on the statutory rate of 26.5% (26.5% in 2016)	1,646,879	1,244,162
Income from insuring farm related risks	(152,106)	(109,727)
Claims reserves timing differences	(689)	(17,278)
Other non deductible expenses	594	15,858
Depreciation in excess of capital cost allowance	15,002	7,951
Other non taxable income	(222,751)	(220,521)
Current year income tax expense	1,286,929	920,445

9. Fees, Commissions and Other Acquisition Expenses

Commissions	3,642,137	3,334,530
Other	77,235	80,240
	3,719,372	3,414,770



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

	2017	2016
	\$	\$
10. Other Operating and Administrative Expenses		
Computer costs	446,379	327,516
Licenses, fees and dues	29,214	29,109
Depreciation	310,900	325,205
Repairs and maintenance	88,641	88,038
Utilities	46,024	53,618
Property taxes	69,721	69,501
Postage, office supplies and telephone	158,948	171,085
Professional fees	85,325	49,835
Salaries, benefits and directors fees	3,012,398	3,116,317
Employee development, travel and conventions	222,881	193,458
Advertising and promotion	211,578	193,265
Statistical service	109,437	121,666
Memberships	66,983	64,745
Other	58,065	86,331
	4,916,494	4,889,689

11. Salaries, Benefits and Directors Fees

Underwriter salaries and benefits	783,575	769,953
Sales salaries and commissions	3,642,137	3,334,530
Other salaries, benefits and directors fees	2,228,823	2,346,364
	6,654,535	6,450,847

Included in claims expenses were salary and benefit costs of \$825,182 (\$784,804 in 2016).

12. Investment Income

	Held to maturity \$	Fair value through profit or loss \$	Loans and receivables \$	2017 Total \$
Interest income	180,421	1,178,049		1,358,470
Dividend income		840,573		840,573
Realized gains on disposal of investments	622	864,869		865,491
Unrealized gains on investments		598,626		598,626
Investment expenses		(296,358)		(296,358)
Other			200,523	200,523
	181,043	3,185,759	200,523	3,567,325



EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017

12. Investment Income (Continued)

	Held to maturity \$	Fair value through profit or loss \$	Loans and receivables \$	2016 Total \$
Interest income	178,834	1,192,234		1,371,068
Dividend income		824,541		824,541
Realized gains on disposal of investments		335,388		335,388
Unrealized gains on investments		900,746		900,746
Investment expenses		(180,651)		(180,651)
Other			123,715	123,715
	178,834	3,072,258	123,715	3,374,807

13. 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:

	2017 \$	2016 \$
Compensation		
Salaries, benefits and director's fees	1,011,165	996,793
Pension and other post-employment benefits	91,489	99,549
	1,102,654	1,096,342
Premiums	97,427	101,030
Claims paid	23,153	25,666

Amounts owing to and from key management personnel at December 31, 2017 are \$23,496 (\$530 in 2016) and \$272 (\$Nil in 2016) respectively. The amounts are included in accounts payable and accrued liabilities and premiums receivable on the statement of financial position.



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

14. Capital Management

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 generally expect 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. The regulator indicates that the Company should produce a minimum MCT of 150%. During the year, the Company has consistently exceeded this minimum. 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 if deemed necessary.

The MCT for the company at December 31, 2017 was 548% (522% at December 31, 2016).

For the purpose of capital management, the Company has defined capital as policyholders' equity.

15. Financial Instrument and Insurance Risk Management

Insurance risk management

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 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 Company purchases reinsurance as part of its risk mitigation program. Retention limits for the excess-of-loss reinsurance vary by product line.

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 any reinsurer is unable to meet its obligations assumed under such reinsurance agreements.

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 Company manages this risk via its underwriting and reinsurance strategy within an overall risk management framework. Exposures are limited by having documented underwriting limits and criteria. 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. Reinsurance is purchased to mitigate the effect of the potential loss to the Company.



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

15. Financial Instrument and Insurance Risk Management (Continued)

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 \$750,000 in the event of a property claim, an amount of \$750,000 in the event of an automobile claim and \$750,000 in the event of a liability claim. The Company also obtained reinsurance which limits the Company's liability to \$2,250,000 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 net earned premiums.

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, 2017 and 2016.

The risks associated with insurance contracts are complex and subject to a number of variables which complicate 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 occurrence, expected loss ratios and claims development as described in note 6.

The table below sets out the concentration of unpaid claims and adjustment expenses by class of insurance:

	December 31, 2017			December 31, 2016		
	Gross Claims \$	Reinsurance Of Claims \$	Net Claims \$	Gross Claims \$	Reinsurance Of Claims \$	Net Claims \$
Property	2,600,444	548,266	2,052,178	2,390,848	(120,902)	2,511,750
Automobile	17,484,446	5,710,926	11,773,520	15,955,025	5,067,633	10,887,392
Liability	1,782,745	466,351	1,316,394	3,150,170	1,334,661	1,815,509
	21,867,635	6,725,543	15,142,092	21,496,043	6,281,392	15,214,651

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

	Property claims		Auto claims		Liability claims	
	2017 \$	2016 \$	2017 \$	2016 \$	2017 \$	2016 \$
5% increase in loss ratios						
Gross	(722,114)	(659,638)	(643,959)	(611,486)	(126,513)	(115,039)
Net	(679,173)	(622,259)	(597,321)	(567,151)	(105,610)	(96,551)
5% decrease in loss ratios						
Gross	722,114	659,638	643,959	611,486	126,513	115,039
Net	679,173	622,259	597,321	567,151	105,610	96,551

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.



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

15. Financial Instrument and Insurance Risk Management (Continued)

Credit risk

Credit risk is the risk of financial loss to the Company if a debtor fails to make payments of interest and principal when due. The Company is exposed to this risk relating to its debt holdings in its investment portfolio and the reliance on the reinsurer to make payment when certain loss conditions are met.

The Company's investment policy puts limits on the bond portfolio including portfolio composition limits, issuer type limits, bond quality limits, aggregate issuer limits and corporate sector limits. The bond portfolio remains very high quality with 82% of the bonds rated A or better. All fixed income portfolios are measured for performance on a quarterly basis and monitored by management on a monthly basis.

Reinsurance is placed with Farm Mutual Re, a Canadian registered reinsurer. Management monitors the credit-worthiness of Farm Mutual Re by reviewing their annual financial statements and through ongoing communications. Reinsurance treaties are reviewed annually by management and the Board prior to renewal of the reinsurance contract.

Amounts receivable are short-term in nature and are not subject to material credit risk.

The maximum exposure to credit risk and concentration of this risk is outlined in note 4.

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

The loan receivable is fully secured by a first security interest and collateral mortgage on all of the certain assets and real property owned by the borrower. Annual financial reviews are undertaken to determine if the borrower will be able to make the required payments when due. As such, the Company's credit exposure on this loan is limited to the carrying value as disclosed in note 4. On December 31, 2017, the loan is neither past due nor impaired and, therefore no provision is required.

Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate as a result of market factors. Market factors include three types of risk: currency risk, interest rate risk and equity risk.

The Company's investment policy operates within the guidelines of the Ontario 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. The policy limits the investment in any one corporate issuer to a maximum of 10% of the company's total assets.

a) Currency risk

Currency risk relates to the company operating in different currencies and converting non Canadian earnings at different points in time at different foreign exchange levels when adverse changes in foreign currency exchange rates occur.

The Company's foreign exchange risk is related to its stock holdings. The Company limits its holdings in foreign equity to 10% of investments in accordance with its investment policy. Foreign currency changes are monitored by the investment committee and holdings are adjusted when out of balance with its investment policy. A 1% change in the value of the United States dollar would affect the fair value of stocks and cash by approximately \$124,866, which would be reflected in the statement of comprehensive income.

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



**EXPLANATORY FINANCIAL NOTES
YEAR ENDED DECEMBER 31, 2017**

15. Financial Instrument and Insurance Risk Management (Continued)

Market risk (continued)

b) 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 this risk through its interest bearing investments, which include treasury bills, guaranteed investment certificates 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 its 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 net income. There are no occurrences where interest would be charged on liabilities; therefore, little protection is needed to ensure the fair market value of assets will be offset by a similar change in liabilities due to an interest rate change.

The objective, policies and procedures for managing interest rate risk are to diversify the bond portfolio in such a way that the bond portfolio is laddered over a period of years. This protects the Company from fluctuations in the interest rates. At December 31 2017, a 1% move in interest rates, with all other variables held constant, could impact the market value of bonds by approximately \$1,924,317.

There have been no significant changes from the previous period in the exposure to risk, nor any significant changes to policies, procedures and methods used to measure the risk.

c) 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 holdings within its investment portfolio.

The company's portfolio includes Canadian stocks with fair values that move with the Toronto Stock Exchange Composite Index, United States stocks with fair values that move with the S&P 500 Index, and international stocks that move with financial markets in Europe, Australia and Far East. 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 common stocks and United States common stocks of approximately \$2,296,523. A 10% move in the fair value of the Company's Canadian preferred stocks would have an impact of approximately \$725. These changes would be recognized in the statement of comprehensive income.

The Investment Committee of the Board of Directors follows investment policies, procedures and processes for managing equity risk.

Liquidity 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, nor does it have 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.

There have been no significant changes from the previous period in the exposure to risk, nor significant changes in policies, procedures and methods used to measure the risk.