Caradoc Townsend Mutual Insurance Company

Consolidated Financial Statements

December 31, 2019

Caradoc Townsend Mutual Insurance Company

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December 31, 2019

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CTM | Caradoc Townsend Mutual Insurance Company

Management's Responsibility for Financial Reporting

The consolidated financial statements of Caradoc Townsend Mutual Insurance Company have been prepared in accordance with International Financial Reporting Standards. When alternative accounting methods exist, management has chosen those it deems most appropriate in the circumstances. These statements include certain amounts based on management's estimates and judgments. Management has determined such amounts based on a reasonable basis in order to ensure that the consolidated financial statements are presented fairly in all material respects.

The integrity and reliability of Caradoc Townsend Mutual Insurance Company's reporting systems are achieved through the use of formal policies and procedures, the careful selection of employees and an appropriate division of responsibilities. These systems are designed to provide reasonable assurance that the financial information is reliable and accurate.

The Board of Directors is responsible for ensuring that management fulfills its responsibility for financial reporting and is ultimately responsible for reviewing and approving the consolidated financial statements. Following its review of the consolidated financial statements and discussions with the auditors, the Board approves the consolidated financial statements to be submitted to the members for their approval at the annual general meeting. The Board also considers the engagement or re-appointment of the external auditors for approval by the Members at the annual general meeting.

The consolidated financial statements have been audited on behalf of the members by Millard, Rouse & Rosebrugh LLP, in accordance with Canadian Generally Accepted Auditing Standards.

Neil Shay, CEO & General Manager

Mary Heastont, VP Corporate Services & Treasurer

February 24, 2020

INDEPENDENT AUDITOR'S REPORT

To the Members of Caradoc Townsend Mutual Insurance Company:

Opinion

We have audited the consolidated financial statements of Caradoc Townsend Mutual Insurance Company (the Company), which comprise the consolidated statement of financial position as at December 31, 2019, and the consolidated statements of surplus, income, and cash flow for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2019, its financial performance, and its cash flow 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 Consolidated Financial Statements* section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada, and we have fulfilled our other ethical responsibilities in accordance with those 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 Consolidated Financial Statements

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

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

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

(continues)

Independent Auditor's Report to the Members of Caradoc Townsend Mutual Insurance Company:

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated 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 consolidated financial statements. 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 consolidated 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 Company'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 Company'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 consolidated 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 Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure, and content of the consolidated financial statements, including the disclosures, and whether the consolidated 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.

Millard, Rouse + Rosebrugh LLP

Millard, Rouse & Rosebrugh LLP
Chartered Professional Accountants
Licensed Public Accountants

February 24, 2020
Simcoe, Ontario

Caradoc Townsend Mutual Insurance Company

Consolidated Statement of Financial Position

As at December 31, 2019

		2019		2018
ASSETS				
Cash	**$**	**2,670,708**	$	1,848,248
Investments *(Note 5)*		**20,007,525**		18,614,237
Accrued investment income		**110,122**		90,614
Due from policyholders		**3,991,425**		3,750,099
Due from reinsurer *(Note 6)*		**53,996**		59,291
Due from Facility Association		**88,735**		110,206
Miscellaneous accounts receivable		**35,789**		1,536
Reinsurers' share of unearned premiums *(Note 7)*		**149,313**		122,688
Prepaid expenses		**21,910**		19,903
Deferred policy acquisition costs *(Note 8)*		**1,200,531**		1,513,000
Deferred income taxes *(Note 9)*		**1,657,000**		761,000
Investment in associate *(Note 10)*		**636,707**		636,442
Property and equipment *(Note 11)*		**2,284,740**		2,246,436
Reinsurers' share of provision for unpaid claims *(Note 12)*		**2,989,272**		2,667,934
	$	**35,897,773**	$	32,441,634
LIABILITIES AND SURPLUS				
Accounts payable	**$**	**565,881**	$	535,308
Due to other insurance companies		**136,114**		171,703
Unearned premiums *(Note 13)*		**7,201,922**		6,335,261
Unearned commission revenue *(Note 14)*		**45,399**		31,874
Provision for unpaid claims and adjustment expenses *(Note 15)*		**13,603,834**		9,151,834
Lease liabilities *(Note 16)*		**110,862**		-
		21,664,012		16,225,980
Surplus		**14,233,761**		16,215,654
	$	**35,897,773**	$	32,441,634

ON BEHALF OF THE BOARD

John Van Ryssen ________________________ *Director*

________________________ *Director*

See accompanying notes

Caradoc Townsend Mutual Insurance Company
Consolidated Statement of Surplus
Year ended December 31, 2019

	2019	2018
Balance - beginning of year	**$ 16,215,654**	$ 17,304,660
Net loss for the year	**(1,981,893)**	(1,089,006)
BALANCE - END OF YEAR	**$ 14,233,761**	$ 16,215,654

See accompanying notes

Caradoc Townsend Mutual Insurance Company

Consolidated Statement of Income

Year ended December 31, 2019

	2019	2018
UNDERWRITING OPERATIONS		
Gross premiums written	**$ 14,577,854**	$ 13,081,147
Deduct: reinsurance ceded	**(2,330,111)**	(2,347,297)
Net premiums written	**12,247,743**	10,733,850
Deduct: decrease (increase) in unearned premiums	**(840,036)**	68,586
Net premium earned	**11,407,707**	10,802,436
Service charges		
Service charges	**149,284**	157,008
Other	**38,243**	16,594
	187,527	173,602
Total underwriting revenue	**11,595,234**	10,976,038
Direct losses incurred		
Gross claims and adjustment expenses	**10,479,983**	10,516,834
Reinsurer's share of claims and adjustment expenses	**(326,494)**	(2,799,422)
	10,153,489	7,717,412
Expenses		
Fees, commissions, and other acquisition expenses *(Note 18)*	**2,605,529**	1,636,236
General expenses *(see schedule on page 7)*	**3,363,277**	3,249,571
Premium deficiency adjustments	**14,299**	(20,871)
	5,983,105	4,864,936
Underwriting loss	**(4,541,360)**	(1,606,310)
Investment income (loss) *(Note 19)*	**1,663,467**	(65,896)
Loss before income taxes	**(2,877,893)**	(1,672,206)
Income taxes		
Deferred *(Note 9)*	**(896,000)**	(583,200)
NET LOSS FOR THE YEAR	**$ (1,981,893)**	$ (1,089,006)

See accompanying notes

Caradoc Townsend Mutual Insurance Company

Consolidated Schedule of General Expenses

Year ended December 31, 2019

	2019	2018
Advertising	**$ 49,223**	$ 64,683
Association fees	**66,219**	59,523
Bad debts	**14,056**	19,776
Bank charges	**72,859**	67,884
Computer (a)	**656,322**	550,170
Contracted services	**20,434**	27,827
Directors fees	**79,494**	78,593
Donations	**36,462**	34,271
Employee benefits	**282,966**	230,124
Inspections and investigations	**50,904**	52,545
Insurance	**71,085**	74,637
Loss prevention rebates and supplies	**3,911**	5,164
Occupancy cost (a)	**184,385**	162,875
Operating lease (b)	**-**	188,202
Other	**27,537**	20,778
Pension deficit recovery *(Note 21)*	**-**	(95,476)
Postage	**38,012**	32,435
Premium tax	**41,816**	32,004
Printing and stationary	**51,253**	69,348
Professional fees	**159,624**	173,840
Salaries	**1,202,934**	1,138,772
Scholarships	**9,000**	10,000
Seminars, conventions, and meetings	**102,094**	122,375
Statistics and reports	**37,488**	36,290
Telephone	**29,321**	29,437
Vehicle and travel (a)	**75,878**	63,494
	$ 3,363,277	$ 3,249,571

(a) Amortization expense of $258,075 ($107,753 - 2018) is included in the above amount

(b) Prior period figures are not comparable due to the adoption of IFRS 16 (refer to Note 3). Lease payments were previously recorded as lease costs.

See accompanying notes

Caradoc Townsend Mutual Insurance Company

Consolidated Statement of Cash Flow

Year ended December 31, 2019

	2019	2018
OPERATING ACTIVITIES		
Net loss for the year	$ (1,981,893)	$ (1,089,006)
Adjustments for:		
Amortization of property and equipment and right-of-use assets	258,075	107,753
Loss on disposal of property and equipment	-	4,822
Deferred income taxes	(896,000)	(583,200)
Share of profit from investment in associate	(265)	(11,600)
Realized gain on sale of investments	(78,285)	(100,600)
Unrealized gain (loss) on investments	(1,054,962)	714,440
	(3,753,330)	(957,391)
Changes in non-cash working capital:		
Due to (from) policyholders	(241,326)	59,390
Due to (from) reinsurer	5,295	(49,291)
Due to (from) Facility Association	21,471	(37,349)
Miscellaneous accounts receivable	(34,253)	54,575
Reinsurers' share of unearned premiums	(26,625)	(23,611)
Prepaid expenses	(2,007)	(19,109)
Deferred policy acquisition costs	312,469	(313,693)
Reinsurers' share of provision for unpaid claims	(321,338)	(1,423,034)
Accounts payable	30,573	(189,604)
Due to other insurance companies	(35,589)	(73,274)
Unearned premiums	866,661	(44,975)
Unearned commission revenue	13,525	3,525
Provision for unpaid claims and adjustment expenses	4,452,000	2,269,057
	5,040,856	212,607
Cash flow from (used by) operating activities	1,287,526	(744,784)
INVESTING ACTIVITIES		
Purchase of property and equipment	(38,398)	(72,113)
Purchase of investments	(11,894,916)	(3,324,929)
Proceeds on disposition of investments	11,615,367	5,806,308
Investment in associate	-	(35,244)
Cash flow from (used by) investing activities	(317,947)	2,374,022
FINANCING ACTIVITIES		
Repayment of lease liabilities	(147,119)	-
Cash flow used by financing activities	(147,119)	-
INCREASE IN CASH	822,460	1,629,238
Cash - beginning of year	1,848,248	219,010
CASH - END OF YEAR	$ 2,670,708	$ 1,848,248

See accompanying notes

1. NATURE OF BUSINESS

Caradoc Townsend Mutual Insurance Company is a mutual insurance company and is owned by the member policyholders. The Company was incorporated under the laws of Ontario and is subject to the Insurance Act of Ontario. It is licensed to write property, liability, automobile, hail, boiler and machinery, and certain types of fidelity and accident and sickness insurance in Ontario. The company's head office is located in Waterford, Ontario and a satellite office is located in Mount Brydges, Ontario.

The Company is subject to rate regulation in the automobile business it writes. Before automobile insurance rates can be changed, a rate filing is prepared as a combined filing for most Ontario Farm Mutual's by the Ontario Mutual's Auto Rate Filing Committee. 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 that time.

These consolidated financial statements have been authorized for issue by the Board of Directors on February 24, 2020.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS).

These consolidated financial statements were prepared on a historical cost basis, except for those financial assets that have been measured at fair value. The Company's functional and presentation currency is the Canadian dollar. The consolidated financial statements are presented in Canadian dollars.

The notes to the consolidated 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.

Consolidation

The consolidated financial statements of the company include its wholly-owned subsidiary, 2598695 Ontario Inc., which was incorporated on September 27, 2017. The accounting policies of the subsidiary have been aligned with the policies adopted by the Company. All intra-company transactions have been eliminated upon consolidation.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Insurance contracts

In accordance with IFRS 4, balances arising from insurance contracts primarily include unearned premiums, provisions for unpaid claims and adjustment expenses, the reinsurers' share of unpaid claims and adjustment expenses, deferred policy acquisition expenses, and salvage and subrogation recoverable.

Premiums and unearned premiums

The Company earns premium income over the term of the insurance policy on a pro rata basis. 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. Premiums receivable are recorded at amounts due less any required provision of doubtful amounts.

Reinsurers' share of unearned premiums

The reinsurers' share of unearned premiums are recognized as an asset using principles consistent with the Company's method for determining the unearned premium liability.

Deferred policy acquisition costs

Acquisition costs are comprised of agents' commissions, premium taxes, and other expenses which relate directly to the acquisition of premiums, including salaries for underwriting personnel and inspection fees. 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 and investment income.

Provision 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 a discounted basis.

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.

(continues)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Reinsurers' share of provision for unpaid claims for adjustment expenses

Incurred reinsurance recoveries are recorded as reductions of the claims incurred accounts. 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. 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 obligations under the reinsurance agreements.

Fire Mutuals Guarantee Fund

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 became bankrupt. As a result, the Company may be required to contribute assets to their proportionate share in meeting this objective.

Property and equipment

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

Buildings	35 years
Office equipment	10 years
Computer equipment	3-5 years
Signs	5 years
Paving & sidewalks	10 years
Motor vehicles	5 years

Amortization methods, useful lives, and residual values are reviewed annually and adjusted if necessary. Property and equipment acquired during the year are amortized at one-half of the normal rate.

Right-of-use assets

At inception of a contract, the Company assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. This policy is applied to contracts entered into, or changed, on or after January 1, 2019. All leases are accounted for by recognizing a right-to-use asset and a lease liability except for leases of low value and short-term leases with a lease term of twelve months or less.

The Company recognizes right-of-use assets and lease liabilities at the lease commencement date.

The right-of-use assets are initially measured at the amount of the lease liability, reduced for any lease incentives received, and increased for lease payments made at or before commencement of the lease or initial direct costs incurred.

(continues)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

Lease liabilities are initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Company's incremental borrowing rate.

Right-of-use assets are subsequently measured at cost less any accumulated depreciation and impairment losses, and adjusted for certain remeasurements of the lease liability.

Lease liabilities are subsequently increased by the interest cost on the lease liability and decreased by lease payments made. Lease liabilities are remeasured when there is a change in future lease payments arising from a change in an index or rate. The revised future lease payments are discounted at the same discount rate that applied on lease commencement.

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 a business combination, or items recognized directly in 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.

Deferred tax assets and liabilities are recognized where the carrying amount of an asset or liability differs from its tax base, except for taxable temporary differences arising on the initial recognition of goodwill and temporary differences arising on the initial recognition of an asset or liability in a transaction which is not a business combination and at the time of the transaction affects neither accounting or taxable profit or loss.

Recognition of deferred tax assets for unused tax losses, tax credits, and deductible temporary differences is restricted to those instances where it is probable that future taxable profit will be available against which the deferred tax asset can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

The amount of the deferred tax asset or liability is measured at the amount expected to be recovered from or paid to the taxation authorities. This 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 liabilities (assets) are settled (recovered).

Financial instruments

The Company classifies its consolidated financial instruments into one of the following categories based on the characteristics of the financial instruments and management's choices and intentions. All transactions related to financial instruments are recorded on a trade date basis. The Company's accounting policy for each category is as follows:

(continues)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

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 purchases 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.

Loans and receivables

These are comprised of amounts due from policyholders, reinsurers', Facility Association, and miscellaneous 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, less any impairment losses. Impairments are recognized when there is objective evidence that the Company will be unable to collect all of the amounts due under the terms receivable. On confirmation that the amounts receivable will not be collectable, the gross carrying value of the asset is written off and the loss is recognized in net income.

Other financial liabilities

Other financial liabilities include all financial liabilities and are comprised of accounts payable and amounts due to other insurance companies. 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.

Standards, amendments and interpretations not yet effective

There are no new standards, amendments, and interpretations effective for the first time from January 1, 2019, that have had a material effect on the consolidated financial statements.

Certain new standards, amendments and interpretations have been published that are mandatory for the Company's accounting periods beginning on or after January 1, 2019 or later periods that the Company has decided not to early adopt. The standards, amendments, and interpretations that may be relevant to the Company are:

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, 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, 2022, which is the effective date of IFRS 17, *Insurance Contracts*. The Company plans to defer the effective date of IFRS 9 and therefore expects to adopt IFRS 9 on January 1, 2022, concurrent with IFRS 17. The Company is currently assessing the impact of IFRS 9.

(continues)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

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 liabilitie. 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, 2022 with mandatory restatement of comparative periods. The Company is currently assessing the impact of IFRS 17.

3. ACCOUNTING ESTIMATES AND JUDGMENTS

The Company makes estimates and assumptions about the future that affect the reported amounts of assets and other liabilities. Estimates and judgments are continually evaluated and based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. In the future, actual experience may differ from these estimates and assumptions.

The effect of a change in an accounting estimate is recognized prospectively by including it in income in the period of the change, if the change affects that period only; or in the period of the change and future periods, if the change affects both.

See Note 15 and Note 17, "Provision for Unpaid Claims and Adjustment Expenses" and "Insurance Contracts" for estimates and assumptions that have a significant risk of causing material adjustment to the carrying amounts of assets and liabilities within the next financial year.

4. ADOPTION OF NEW ACCOUNTING STANDARDS

Accounting standards, interpretations, and amendments effective for accounting years beginning on or after January 1, 2019 did not materially affect the Company's financial statements other than those described below.

IFRS 16 Leases (IFRS 16)

On January 1, 2019, the Company adopted IFRS 16 Leases (IFRS 16). IFRS 16 provides a single lessee accounting model, requiring the recognition of assets and liabilities for all leases, unless the lease term is 12 months or less, or the underlying asset is of low value. IFRS 16 substantially carries forward the lessor accounting in IAS 17 - Leases ("IAS 17"), with the distinction between operating leases and finance leases being retained.

The Company adopted IFRS 16 using the modified retrospective approach without restatement of comparative figures. The Company elected to apply the practical expedient to not reassess whether a contract is, or contains a lease at the date of initial application. Contracts entered into before the transition date that were not identified as leases under IAS 17 and IFRIC 4 were not reassessed. The definition of a lease under IFRS 16 was applied only to contracts entered into or changed on or after January 1, 2019.

IFRS 16 provides for certain optional practical expedients, including those related to the initial adoption of the standard. The Company applied the following practical expedients when applying IFRS 16 to leases previously classified as operating leases under IAS 17:

Applied a single discount rate to a portfolio of leases with reasonably similar characteristics;

Reliance on previous assessments of whether leases are onerous as opposed to preparing an impairment review under IAS 36 as at the date of initial application; and

Applied the exemption not to recognize right-of-use assets and liabilities for leases with less than 12 months of lease term remaining as of the date of initial application.

Recognition and measurement

As a lessee, the Company previously classified leases as operating or finance leases based on its assessment of whether the lease transferred substantially all of the risks and rewards of ownership. Under IFRS 16, the Company recognizes right-of-use assets and lease liabilities for most leases. However, the Company has elected not to recognize right-of-use assets and lease liabilities for some leases of low value based on the value of the underlying asset when new or for short-term leases with a lease term of 12 months or less.

On adoption of IFRS 16, the Company recognized right-of-use assets and lease liabilities in relation to leases of computer equipment which had previously been classified as operating leases.

The lease liabilities and right-of-use assets were measured as follows:

The lease liabilities were measured at the present value of the remaining lease payments, discounted using the Company's incremental borrowing rate as at January 1, 2019. The Company's incremental borrowing rate is the rate at which a similar borrowing could be obtained from an independent creditor under comparable terms and conditions; and

Right-of-use assets are measured at an amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments.

(continues)

4. ADOPTION OF NEW ACCOUNTING STANDARDS *(continued)*

Impacts on the Company's financial statements

As a result of initially applying IFRS 16, in relation to the leases that were previously classified as operating leases, the Company recognized $257,980 of right-of-use assets and $257,980 of lease liabilities as at January 1, 2019.

When measuring lease liabilities for leases that were previously operating leases, the Company discounted lease payments using its incremental borrowing rate at January 1, 2019. The weighted average incremental borrowing rate applied to the lease liabilities was 3.95%. The minimum operating lease commitment disclosed as at December 31, 2018 was $271,340. The effect of discounting using the incremental borrowing rate as at the date of initial application was $13,360. The net difference totaling $257,980 was recognized at January 1, 2019.

Also, in relation to those leases under IFRS 16, the Company recognized depreciation and interest costs, instead of operating lease expense. During the year ended December 31, 2019, the Company recognized $140,507 of amortization expense and $6,961 of interest costs.

The balances as at December 31, 2019 are $257,980 for right-of-use assets and $110,861 for lease liabilities.

5. INVESTMENTS

The book and fair values of investments at December 31 are shown as follows:

	2019 $		2018 $	
	Book Value	**Fair Value**	Book Value	Fair Value
Held-for-trading				
Bonds issued by:				
Federal	**2,671,447**	**2,671,447**	2,439,270	2,439,270
Provincial	**3,872,584**	**3,872,584**	1,922,936	1,922,936
Corporate	**10,008,634**	**10,008,634**	7,952,327	7,952,327
	16,552,665	**16,552,665**	12,314,533	12,314,533
Equity Investments				
Common shares	**1,981,518**	**1,981,518**	4,831,178	4,831,178
Preferred shares	**563,076**	**563,076**	729,615	729,615
Equity interest in private company	**400,000**	**400,000**	-	-
Equity pooled funds	**510,266**	**510,266**	738,911	738,911
	3,454,860	**3,454,860**	6,299,704	6,299,704
Total investments	**20,007,525**	**20,007,525**	18,614,237	18,614,237

The maximum exposure to credit risk would be the fair value, as shown above.

6. DUE FROM REINSURER

The continuity of amounts due from reinsurer are as follows:

	2019	2018
	$	$
Balance, beginning of year	**59,291**	10,000
Submitted to reinsurer	**212,415**	1,394,764
Received from reinsurer	**(217,710)**	(1,345,473)
Balance, end of year	**53,996**	59,291

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

7. REINSURERS' SHARE OF UNEARNED PREMIUMS

The continuity of reinsurers' share of unearned premiums are as follows:

	2019	2018
	$	$
Balance, beginning of year	**122,688**	99,077
Submitted to reinsurer	**2,330,111**	2,347,297
Premiums earned during the year	**(2,303,486)**	(2,323,686)
Balance, end of year	**149,313**	122,688

8. DEFERRED POLICY ACQUISITION COSTS

The continuity of deferred policy acquisition costs are as follows:

	2019	2018
	$	$
Balance, beginning of year	**1,513,000**	1,053,710
Assumed on amalgamation	**-**	145,597
Balance, beginning of year - restated	**1,513,000**	1,199,307
Acquisition costs incurred	**2,293,059**	1,949,930
Expensed during the year	**(2,605,528)**	(1,636,237)
Balance, end of year	**1,200,531**	1,513,000

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

9. DEFERRED INCOME TAXES

The income tax provision recorded differs from the income tax obtained by applying the statutory income tax rate of 26.5% (2018 - 26.5%) to the income for the year and is reconciled as follows:

	2019	2018
Loss before income taxes	**$ (2,877,893)**	$ (1,672,206)
Income tax recovery at the combined basic federal and provincial tax rate:	**$ (762,642)**	$ (443,135)
Decrease resulting from:		
Non-taxable investment income	**(34,852)**	(42,588)
Capital cost allowance claimed in excess of amortization	**24,821**	7,814
Non-deductible portion of claims liabilities	**(54,801)**	(76,524)
Reserves transferred upon amalgamation	**-**	25,090
Other	**38,445**	16,787
Non-capital loss carried forward due to amalgamation	**(106,971)**	(70,644)
Effective tax recovery	**$ (896,000)**	$ (583,200)

The significant components of deferred income tax balance are as follows:

	2019	2018
	$	$
Deferred tax assets		
Non-capital losses carried forward	**1,623,600**	757,000
Non-deductible portion of claims liabilities	**139,000**	85,000
	1,762,600	842,000
Deferred tax liabilities		
Capital cost allowance claimed in excess of amortization	**(105,600)**	(81,000)
Deferred income taxes	**1,657,000**	761,000

10. INVESTMENT IN ASSOCIATE

On December 15, 2017, Townsend Mutual Insurance Company acquired an equal share, 33.33% of a private insurance brokerage company with two unrelated parties. These shares are carried at cost in 2598695 Ontario Inc. which is 100% owned by Caradoc Townsend Mutual Insurance Company.

The investment is to be accounted for using the equity method of accounting whereby the investment will be adjusted to reflect the proportionate share of net income of the brokerage company less any dividends received. During 2019, the company recognized their share of income in the amount of $265 (2018 - $11,600).

11. PROPERTY AND EQUIPMENT

Cost	Land $	Building $	Office Equipment $	Computer Equipment $	Signs $	Paving & Sidewalks $	Motor Vehicles $	Total $
Balance on December 31, 2018	430,000	1,637,497	167,431	274,093	44,413	77,083	28,395	2,658,912
Additions	-	-	19,762	19,395	-	-	-	39,157
Additions - right-of-use				257,980				257,980
Disposals	-	(758)	-	-	-	-	-	(758)
Balance on December 31, 2019	**430,000**	**1,636,739**	**187,193**	**551,468**	**44,413**	**77,083**	**28,395**	**2,955,291**
Accumulated amortization								
Balance on December 31, 2018	-	150,117	42,909	165,616	18,505	26,811	8,518	412,476
Amortization expense	-	46,786	17,731	171,288	8,882	7,709	5,679	258,075
Disposals	-	-	-	-	-	-	-	-
Balance on December 31, 2019	**-**	**196,903**	**60,640**	**336,904**	**27,387**	**34,520**	**14,197**	**670,551**
Net book value								
December 31, 2018	430,000	1,487,380	124,522	108,477	25,908	50,272	19,877	2,246,436
December 31, 2019	**430,000**	**1,439,836**	**126,553**	**214,564**	**17,026**	**42,563**	**14,198**	**2,284,740**

Included in computer equipment above are the right-of-use assets. These assets were recognized on January 1, 2019 with a cost of $257,980. Amortization included in computer equipment for the right-of-use assets amounted to $140,507.

12. REINSURERS' SHARE OF PROVISION FOR UNPAID CLAIMS

The continuity of reinsurers' share of provision for unpaid claims are as follows:

	2019	2018
	$	$
Balance, beginning of year	**2,667,934**	863,262
Assumed on amalgamation	**-**	381,638
Balance, beginning of year - restated	**2,667,934**	1,244,900
New claims reserve	**295,000**	1,296,753
Change in prior years' reserve	**(186,077)**	(1,268,483)
Submitted to reinsurer	**212,415**	1,394,764
Balance, end of year	**2,989,272**	2,667,934
Expected settlement		
Within one year	**658,313**	587,546
More than one year	**2,330,959**	2,080,388
	2,989,272	2,667,934

13. UNEARNED PREMIUMS

The continuity of unearned premiums are as follows:

	2019	2018
	$	$
Balance, beginning of year	**6,335,261**	5,189,901
Assumed on amalgamation	**-**	1,190,335
Balance, beginning of year - restated	**6,335,261**	6,380,236
Premiums written	**14,577,854**	13,081,147
Premiums earned during year	**(13,711,193)**	(13,126,122)
Increase (decrease) in reserve for unearned premiums	**866,661**	(44,975)
Balance, end of year	**7,201,922**	6,335,261

14. UNEARNED COMMISSION REVENUE

The continuity of unearned commission revenue is as follows:

	2019	2018
	$	$
Balance, beginning of year	**31,874**	28,349
Received from reinsurer and pools	**81,744**	60,288
Commissions earned during year	**(68,219)**	(56,763)
Increase in reserve for unearned commission revenue	**13,525**	3,525
Balance, end of year	**45,399**	31,874

15. PROVISION FOR UNPAID CLAIMS AND ADJUSTMENT EXPENSES

Changes in claim liabilities recorded in the statement of financial position for the years ended December 31, 2019 and 2018 and their impact on claims and adjustment expenses are as follows:

	2019	2018
	$	$
Balance, beginning of year	**9,151,834**	5,739,247
Assumed on amalgamation	**-**	1,143,530
Balance, beginning of year - restated	**9,151,834**	6,882,777
New claims reserve	**7,661,344**	9,345,983
Change in prior years' reserve	**3,002,160**	543,949
Paid claims		
Current year	**(3,797,521)**	(5,448,516)
Prior year	**(2,413,983)**	(2,172,359)
Balance, end of year, gross	**13,603,834**	9,151,834
Reinsurers' share of provision for unpaid claims	**(2,989,272)**	(2,667,934)
Balance, end of year	**10,614,562**	6,483,900
Expected settlement		
Within one year	**4,204,198**	2,828,329
More than one year	**9,399,636**	6,323,505
	13,603,834	9,151,834

The determination of the provision for unpaid claims and adjustment expenses and the related reinsurers' share requires the estimation of reinsurance recoveries and future development of claims. The provision for unpaid claims and adjustment expenses and related reinsurers' share are estimates subject to variability, and the variability could be material in the near term. The variability arises because all events affecting the ultimate settlement of claims have not taken place and may not take place for some time. Variability can be caused by receipt of additional claim information, changes in judicial interpretation of contracts, or significant changes in severity or frequency of claims from historical trends. The estimates are principally based on the Company's historical experience. Methods of estimation have been used which the Company believes produce reasonable results given current information. 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 shares of the liabilities provided by the actuaries of the pools.

An actuary is retained by the Company's Board of Directors to review the policy liabilities of the Company. The actuary's responsibility is to carry out a valuation of the Company's policy liabilities in accordance with accepted actuarial practices and report thereon to the Company. In performing the valuation, the actuary makes assumptions as to the future loss ratios, trends, future rates of claims frequency and severity, inflation, and both internal and external adjustment expenses, taking into consideration the circumstances of the Company. The actuary also makes use of the work of the external auditor in verifying the underlying data used in the valuation. The actuary's report outlines the scope of work performed and recommendation.

(continues)

15. PROVISION FOR UNPAID CLAIMS AND ADJUSTMENT EXPENSES *(continued)*

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

December 31, 2019	**Gross $**	**Re-Insurance $**	**Net $**
Outstanding claims provision			
Property	620,815	85	**620,730**
Automobile	5,701,643	249,000	**5,452,643**
Liability	3,861,178	1,820,210	**2,040,968**
Facility Association and other residual pools	444,198	-	**444,198**
Provisions for claims incurred but not reported	2,976,000	919,977	**2,056,023**
Balance, end of year	13,603,834	2,989,272	**10,614,562**

December 31, 2018	Gross $	Re-Insurance $	Net $
Outstanding claims provision			
Property	736,821	16,393	720,428
Automobile	2,210,338	230,564	1,979,774
Liability	3,728,375	1,832,977	1,895,398
Facility Association and other residual pools	484,300	-	484,300
Provisions for claims incurred but not reported	1,992,000	588,000	1,404,000
Balance, end of year	9,151,834	2,667,934	6,483,900

16. LEASE LIABILITIES

	2019	2018
HP Equipment and software lease, repayable in monthly payments of $1,499, due April 7, 2020	**$ 66,266**	$ -
HP Equipment lease, repayable in monthly payments of $11,341, due December 31, 2023	**44,596**	-
	$ 110,862	$ -

Interest expense on lease liabilities amounted to $6,961 during 2019.

Future minimum capital lease payments are approximately:

2020	$ 63,353
2021	17,990
2022	17,990
2023	17,990
Total minimum lease payments	117,323
Less: amount representing interest at various rates	6,461
	$ 110,862

17. INSURANCE CONTRACTS

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 settlement term 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. The tables reflect the combination of Townsend Mutual Insurance Company and Caradoc Delaware Mutual Insurance Company. The upper half of the tables shows 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.

17. INSURANCE CONTRACTS *(continued)*

Gross claims

	Earlier	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Total
	$	$	$	$	$	$	$	$	$	$	$	$
Gross estimate of cumulative claims cost												
End of year claim	8,258,026	5,423,761	5,770,984	5,396,337	4,853,645	7,398,670	10,408,214	7,669,230	7,249,213	9,155,848	7,503,990	
One year later	7,495,721	4,006,235	5,674,238	4,482,318	4,243,297	6,566,776	9,455,485	7,143,687	7,840,311	9,922,379	-	
Two years later	5,999,924	3,452,100	5,329,160	4,690,005	4,773,096	6,110,623	9,374,029	8,034,844	8,952,338	-		
Three years later	5,435,387	3,138,622	4,983,880	4,242,979	4,637,721	5,491,495	9,104,924	9,184,307	-			
Four years later	4,711,810	3,090,954	4,741,551	4,269,309	4,196,619	5,442,863	9,348,475	-				
Five years later	4,745,075	3,188,328	4,724,863	4,333,580	4,111,190	5,532,975	-					
Six years later	4,622,806	3,057,734	4,581,783	4,334,808	4,129,137	-						
Seven years later	4,578,610	3,033,749	4,556,046	4,209,046	-							
Eight years later	4,570,610	2,988,967	4,551,046	-								
Nine years later	4,570,610	2,988,967	-									
Ten years later	4,570,610	-										
Current estimate of cumulative claims cost	4,570,610	2,988,967	4,551,046	4,209,046	4,129,137	5,532,975	9,348,475	9,184,307	8,952,338	9,922,379	7,503,990	
Cumulative payments	4,570,610	2,988,967	4,551,046	4,207,046	3,823,958	5,427,239	7,942,465	6,651,008	6,884,966	6,362,980	3,879,151	
Outstanding claims	-	-	-	2,000	305,179	105,736	1,406,010	2,533,299	2,067,372	3,559,399	3,624,839	13,603,834

17. INSURANCE CONTRACTS (*continued*)

Net claims after reinsurance

	Earlier	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Total
	$	$	$	$	$	$	$	$	$	$	$	$
Net estimate of cumulative claims cost												
End of year claim	3,532,620	2,155,144	3,369,350	2,651,601	4,335,870	5,484,324	6,391,716	5,476,156	6,319,571	7,505,545	7,212,990	
One year later	3,192,924	1,912,743	3,568,927	2,675,314	3,856,009	5,045,054	5,964,796	5,438,744	6,142,380	8,352,076	-	
Two years later	2,973,116	1,760,623	3,219,278	2,879,656	4,166,781	4,777,897	5,840,715	5,870,672	7,259,138	-		
Three years later	2,852,630	1,747,580	3,143,121	2,692,843	4,060,501	4,481,302	5,607,611	6,744,675	-			
Four years later	2,782,615	1,708,464	3,095,103	2,738,188	3,809,774	4,444,670	5,848,161	-				
Five years later	2,831,880	1,785,500	3,164,815	2,872,244	3,703,743	4,420,027	-					
Six years later	2,768,611	1,687,484	3,079,903	2,882,471	3,710,802	-						
Seven years later	2,795,197	1,707,194	3,061,167	2,762,710	-							
Eight years later	2,753,415	1,698,038	3,061,167	-								
Nine years later	2,753,415	1,698,038	-									
Ten years later	2,753,415	-										
Current estimate of cumulative claims cost	2,753,415	1,698,038	3,061,167	2,762,710	3,710,802	4,420,027	5,848,161	6,744,675	7,259,138	8,352,076	7,212,990	
Cumulative payments	2,753,415	1,698,038	3,061,167	2,762,710	3,583,408	4,319,292	4,708,047	4,990,881	5,301,851	6,150,677	3,879,151	
Outstanding claims	-	-	-	-	127,394	100,735	1,140,114	1,753,794	1,957,287	2,201,399	3,333,839	10,614,562

18. FEES, COMMISSIONS, AND OTHER ACQUISITION EXPENSES

	2019	2018
Agent commissions and benefits	**$ 1,011,651**	$ 1,048,460
Brokers commissions	**859,454**	580,564
Sales salaries	**443,952**	344,989
Other	**(21,997)**	(24,083)
Change in deferred policy acquisition costs *(Note 8)*	**312,469**	(313,694)
	$ 2,605,529	$ 1,636,236

19. INVESTMENT INCOME

Investment income was derived from the following:

	2019	2018
Interest income	**$ 425,431**	$ 446,084
Dividend and distribution income	**224,959**	203,140
Gain on sale of investments	**78,285**	100,600
Market value adjustments	**1,054,962**	(714,440)
Investment fees	**(120,435)**	(112,880)
Share of profit from investment in associate *(Note 10)*	**265**	11,600
	$ 1,663,467	$ (65,896)

20. 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:

	2019	2018
Compensation		
Salaries, benefits, and directors fees	**$ 754,531**	$ 699,003
Pension and other post-employment benefits	**78,698**	77,785
	$ 833,229	$ 776,788

Premiums for key management personnel during 2019 amounted to approximately $86,224 (2018 - $87,393). There were claims paid to key management personnel during 2019 $27,742 (2018 - $22,756).

21. 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 Company funds the excess defined benefit plan 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 defined benefit plan for 2019 was $96,033 (2018 - $ 98,537). The contributions were made for current service and have been recorded as expenses for 2019. The Company had a 1.80% share of the total contributions to the Plan in 2019.

The next actuarial valuation to be filed under the Pension Benefit Act is due no later than January 1, 2021, which is not expected to be completed until midyear 2021. The actuary has completed a valuation of the funded position of the pension plan as of January 1, 2018. Based on the report, the company has reversed the additional payments which were accrued in 2017 to fund the estimated deficit. The Company's share of the deficit in 2017 amounted to $102,309, of which $68,206 was reversed during the year. As a result of the amalgamation, the company reversed an additional $27,270 from the opening balances of Caradoc Delaware Mutual Insurance Company. These reversals have been recorded as a reduction to expenses in 2018.

The defined benefit plan has been closed to future eligible employees. The Company and all current employees who are accruing benefits under the defined benefit plan continue to contribute to the defined benefit plan according to the existing terms of the agreement. Future eligible employees are enrolled in a new defined contribution plan. The Company’s obligation with respect to this plan is to make specified monthly contributions based on a percentage of employee’s eligible earnings.

The amount contributed to the defined contribution plan for 2019 was $79,888 (2018 - $64,333). The contributions were made for current service and have been recorded as expenses for 2019.

The expected contributions to the defined benefit plan and defined contribution plan for 2020 are $179,440 combined.

22. SUBSEQUENT EVENTS

Subsequent to year-end, the company has entered into a Quota share reinsurance agreement with Farm Mutual Re to cede out 50% of their automobile premiums effective January 1, 2020.

23. FINANCIAL INSTRUMENTS 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 risk 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 reinsurers 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. Reinsurance is placed with Farm Mutual Reinsurance Plan Inc. (Farm Mutual Re), a Canadian registered reinsurer.

The Company followed 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 $430,000 in the event of a property claim, an amount of $430,000 in the event of an automobile claim, an amount of $430,000 in the event of a liability claim, an amount of $20,000 in the event of a farmers' accident claim, and $1,290,000 in the event of a catastrophe.

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.

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23. FINANCIAL INSTRUMENTS AND INSURANCE RISK MANAGEMENT *(continued)*

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 17*.

The table found at the end of *Note 15*, Provision for Unpaid Claims and Adjustment Expenses, sets out the concentration of unpaid claims and adjustment expenses by class of insurance.

A sensitivity analysis is based on the claims loss ratio, which is calculated by taking net claims incurred, including adjustment, expenses over net premiums earned. A 5% movement in the current year claims loss ratio would impact the statement of comprehensive income by approximately $566,000 (2018 - $539,000), before tax.

Fair value

The Company has categorized its assets that are carried at fair value on a recurring basis, based on priority of the inputs to valuation techniques used to measure fair value, into a three-level fair value hierarchy. Financial assets measured at fair value are categorized as follows:

Level 1: Fair value is based on unadjusted quoted prices for identical assets or liabilities in an active market.

Level 2: Fair value is based on quoted prices for similar assets or liabilities in active markets, valuation that is based on significant observable inputs or inputs that are derived principally for, or corroborated with, observable market data through correlation or other means.

Level 3: Fair value is based on valuation techniques that require one or more significant unobservable inputs or the use of broker quotes. These unobservable inputs reflect the Company's assumptions about the assumptions market participants would use in pricing the assets or liabilities. The Company does not have any amounts classified as Level 3.

December 31, 2019	Level 1 $	Level 2 $	Level 3 $	Total $
Cash	2,670,708	-	-	**2,670,708**
Bonds	-	16,552,665	-	**16,552,665**
Equities	-	3,054,860	400,000	**3,454,860**
Total assets measured at fair value	2,670,708	19,607,525	400,000	**22,678,233**

There were no transfers between any levels of the fair value hierarchy for the years ended December 31, 2019 and 2018.

(continues)

23. FINANCIAL INSTRUMENTS 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 reinsurers 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, corporate sector limits, and general guidelines for geographic exposure. All fixed income portfolios are measured for performance on a quarterly basis and monitored by management on a monthly basis.

The maximum exposure to credit risk and concentration of this risk would be the fair values as outlined in *Note 5*.

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

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

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.

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 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.

Currency risk

Currency risk is the risk that fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange values. The Company is not significantly exposed to foreign exchange rate risk.

(continues)

23. FINANCIAL INSTRUMENTS AND INSURANCE RISK MANAGEMENT *(continued)*

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 that include term deposits 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 other comprehensive 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 and policies and procedures for managing interest rate risk is to diversify the bond portfolio in such a way that the bond portfolio is laddered over a number of years. A portion of the bond portfolio would come due each year and be reinvested. This protects the Company from fluctuations in the interest rates.

At December 31, 2019 a 1% move in interest rates, with all other variables held constant, could impact the market value of interest bearing investments by approximately $620,000.

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 equity and fixed investments with fair values that fluctuate with the stock markets. As at December 31, 2019, a 10% movement in the stock markets would have an estimated affect on the fair values of approximately $258,000. For stocks that the Company did not sell during the period, the change would be recognized in the asset value and in net income. For stocks that the Company did sell during the period, the change during the period and changes prior to the period would be recognized as net realized gains in income during the period.

The Company limits its equity holdings to less than 25% of the total portfolio value.

(continues)

23. FINANCIAL INSTRUMENTS AND INSURANCE RISK MANAGEMENT *(continued)*

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 current liabilities arise as claims are made. There are no material liabilities that can be called unexpectedly at the demand of a lender or client. There are 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. There have been no significant changes from the previous period in the exposure to risk or policies.

24. 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 deemed necessary.

For the purpose of capital management, the Company has defined capital as surplus.