Dumfries Mutual Insurance Company
Financial Statements
For the year ended December 31, 2017

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Independent Auditor's Report

To the Policyholders of Dumfries Mutual Insurance Company

We have audited the accompanying financial statements of Dumfries Mutual Insurance Company, which comprise the statement of financial position as at December 31, 2017 and the statements of comprehensive income and unappropriated members' surplus 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.

Auditor's 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 the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers 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 Dumfries Mutual Insurance Company as at December 31, 2017 and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

BDO Canada LLP

Chartered Professional Accountants, Licensed Public Accountants
Mississauga, Ontario
February 20, 2018

Dumfries Mutual Insurance Company
Statement of Financial Position

December 31	2017	2016
Assets		
Cash	**$ 2,001,417**	$ 3,251,843
Due from policyholders	**4,007,451**	3,760,730
Investments (Note 4)	**48,438,626**	46,465,527
Prepaid expenses	**115,387**	54,756
Income taxes recoverable	**-**	353,769
Unpaid claims recoverable from reinsurer (Note 3e)	**6,030,276**	6,601,924
Deferred acquisition expenditures (Note 3b)	**818,141**	799,385
Property and equipment (Note 9)	**1,983,793**	422,505
Deferred tax assets	**140,000**	143,000
	$ 63,535,091	$ 61,853,439
Liabilities		
Accounts payable and accrued liabilities	**$ 1,036,247**	$ 979,072
Provision for refund of premium	**376,316**	306,691
Income taxes payable	**90,191**	-
Due to reinsurer (Note 3e)	**73,065**	35,990
Unpaid claims	**16,321,311**	16,940,457
Unearned premiums (Note 3a)	**7,099,838**	6,882,665
	24,996,968	25,144,875
Members' equity		
Unappropriated members' surplus	**38,538,123**	36,708,564
	$ 63,535,091	$ 61,853,439

On behalf of the Board:

Director

Director

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

Dumfries Mutual Insurance Company
Statement of Comprehensive Income and Unappropriated Members' Surplus

For the year ended December 31	2017	2016
Revenue		
Gross premiums written	**$ 14,827,520**	$ 14,267,955
Less: reinsurance ceded	**(2,604,831)**	(2,208,522)
Net premiums written	**12,222,689**	12,059,433
Change in unearned	**(217,173)**	(108,012)
Net premiums earned	**12,005,516**	11,951,421
Service charges	**70,162**	106,679
	12,075,678	12,058,100
Expenses		
Gross claims and adjustment expenses	**7,912,475**	8,344,030
Reinsurance recoveries	**(479,247)**	(562,916)
Commissions expense	**1,787,730**	1,708,575
Operating expenses (See Note 7)	**1,931,494**	2,207,638
	11,152,452	11,697,327
Net underwriting income	**923,226**	360,773
Other income		
Investment income (Note 5)	**1,870,690**	1,892,119
Comprehensive income before refund and income taxes	**2,793,916**	2,252,892
Refund of surplus to policyholders	**(376,839)**	(306,605)
Comprehensive income before income taxes	**2,417,077**	1,946,287
Income taxes (Note 8)		
Current	**584,518**	507,421
Deferred	**3,000**	(22,000)
	587,518	485,421
Comprehensive income for the year	**1,829,559**	1,460,866
Unappropriated members' surplus, beginning of year	**36,708,564**	35,247,698
Unappropriated members' surplus, end of year	**$ 38,538,123**	$ 36,708,564

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

Dumfries Mutual Insurance Company
Statement of Cash Flows

For the year ended December 31	2017	2016
Cash provided by (used in)		
Operating activities		
Comprehensive income	$ 1,829,559	$ 1,460,866
Adjustments for:		
Depreciation	24,932	24,704
Current income taxes	584,518	507,421
Deferred income taxes	3,000	(22,000)
Realized loss (gain) on disposal of investments	(10,284)	129,164
Unrealized (gain) loss on investments	(1,657,164)	(1,661,376)
	774,561	438,779
Changes in working capital and insurance contract related balances		
Due from policyholders	(246,721)	21,556
Prepaid expenses	(60,631)	3,994
Unpaid claims recoverable from reinsurer	571,648	648,631
Deferred acquisition expenditures	(18,756)	(5,902)
Accounts payable and accrued liabilities	57,175	353,591
Provision for refund of premium	69,625	(48,944)
Due from reinsurer	37,075	5,838
Unpaid claims	(619,146)	573,682
Unearned premiums	217,173	108,013
	7,442	1,660,459
Cash flows related to income taxes	(494,327)	(848,196)
Total cash inflows from operating activities	287,676	1,251,042
Investing activities		
Disposals (purchases) of investments	46,793	(1,069,473)
Purchase of property and equipment	(1,584,895)	(102,173)
Total cash inflows from investing activities	(1,538,102)	(1,171,646)
Increase (decrease) in cash	(1,250,426)	79,396
Cash, beginning of year	3,251,843	3,172,447
Cash, end of year	$ 2,001,417	$ 3,251,843

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

December 31, 2017

1. Corporate Information

Dumfries Mutual Insurance Company (the "Company" or "Dumfries") was incorporated without share capital under the laws governed in Ontario on May 10, 1856. The Company is licensed to write property, auto and liability insurance in Ontario. The Company's products are marketed through independent agents and brokers located throughout Ontario. The Company's registered office is 12 Cambridge Street, Cambridge, Ontario.

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

These financial statements have been authorized for issue by the Board of Directors on February 13, 2018.

2. Basis of Preparation

(a) Statement of Compliance

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

(b) Basis of Measurement

These financial statements were prepared under the historical cost convention, as modified by revaluation of investments (Note 4).

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

(c) Judgment and Estimates

The preparation of financial statements in compliance with IFRS requires management to make certain critical accounting estimates. It also requires management to exercise judgment in applying the Company’s accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are within the next financial year are:

- The calculation of unpaid claims, including the determination of the initial claim liability, discount rates, the estimate of time until ultimate settlement and the performance of a liability adequacy test (Note 3); and
- The determination of the recoverability of deferred policy acquisition expenses (Note 3).

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

December 31, 2017

3. Insurance contracts

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

Balances arising from insurance contracts primarily include deferred acquisition expenditures, unpaid claims recoverable from reinsurer, unpaid claims and unearned premiums.

(a) Premiums and unearned premiums

Premiums written comprise the premiums on contracts incepting in the financial year. Premiums written are exclusive of taxes levied on premiums.

The Company earns premium income evenly over the term of the insurance policy using the pro rata method. The portion of the premium related to the unexpired portion of the policy at the end of the fiscal year is reflected in unearned premiums. Changes in unearned premiums recorded in the statement of financial position for the year ended December 31, 2017 and their impact on net premiums earned for the year is as follows:

	2017	2016
Balance, beginning of the year	**$ 6,882,665**	$ 6,774,652
Premiums written	**14,827,520**	14,267,955
Premiums earned during year	**(14,393,174)**	(14,051,930)
Change in unearned premiums	**(217,173)**	(108,012)
Balance, end of the year	**$ 7,099,838**	$ 6,882,665

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.

Amounts due from policyholders are at amortized cost less any impairment losses. These amounts are short-term in nature consisting of a large number of policyholders, and are not subject to material credit risk. Regular review of outstanding receivables is performed to ensure credit worthiness.

3. Insurance Contracts (continued)

(b) Deferred acquisition expenditures

Acquisition costs are comprised of commissions, premium taxes, association fees, and certain idenfitied business development costs considered to be directly related to the premiums written and therefore are allowed to be deferred. These costs are deferred and amortized over the terms of the related policies to the extent that they are considered to be recoverable from unearned premiums, after considering the related anticipated claims and expenses. Changes in deferred policy acquisition expenses recorded in statement of financial position for the year ended December 31, 2017 and their impact on fees, comissions and other acqusition expenses for the year is as follows:

	2017	2016
Balance, beginning of the year	**$ 799,385**	$ 793,483
Acquisition expenses incurred	**1,786,145**	1,726,428
Expensed during the year	**(1,767,389)**	(1,720,526)
Balance, end of the year	**$ 818,141**	$ 799,385

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

(c) Unpaid claims

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 comprehensive income.

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

The estimation of the unpaid claims and the related reinsurer’s share are the Company’s most critical accounting estimates. There are several sources of uncertainty that need to be considered by the Company in estimating the amount that will ultimately be paid on these claims. The uncertainty arises because all events affecting the ultimate settlement of claims have not taken place and may not take place for some time. Changes in the estimate of the provision 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 based on the Company's historical and industry experience.

Changes in unpaid claim liabilities recorded in the consolidated statement of financial position and its impact on claims and adjustment expenses is as follows:

3. Insurance Contracts (continued)

(c) Unpaid Claims (continued)

	2017	2016
Unpaid claim liabilities - beginning of year – net of reinsurance	**$ 10,338,533**	$ 9,116,220
Increase (decrease) in estimated losses and expenses, for losses occurring in prior years	**(161,000)**	320,000
Provision for losses and expenses on claims occurring in the current year	**7,594,000**	7,461,000
Payment on claims:		
Current year	**(4,792,000)**	(4,111,000)
Prior years	**(2,688,498)**	(2,447,687)
Unpaid claims - end of year net	**10,291,035**	10,338,533
Reinsurer’s share	**6,030,276**	6,601,924
	$ 16,321,311	$ 16,940,457

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

Claim development

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

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

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

The estimation of claim development involves assessing the future behaviour of claims, taking into consideration the consistency of the Company's claim handling procedures, the amount of information available, the characteristics of the line of business from which the claim arises and 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 claims are those which are expected to be substantially paid within a year of being reported.

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

3. Insurance Contracts (continued)

Gross claims (000's)

	Accident Year										
Reporting date	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Total
At end of claim year	$ 7,774	$ 8,825	$ 6,944	$ 10,641	$ 5,701	$ 6,938	$ 13,724	$ 6,972	$ 7,833	$ 7,906	
1 year later	6,976	9,357	6,884	9,851	6,031	7,184	12,598	7,100	7,249		
2 years later	6,214	9,367	6,994	9,962	5,491	6,631	13,362	6,887			
3 years later	4,912	9,427	6,276	8,814	5,209	6,015	13,166				
4 years later	4,103	8,706	4,807	8,672	5,237	6,052					
5 years later	4,090	7,424	4,780	7,715	5,104						
6 years later	4,250	6,929	4,760	7,249							
7 years later	4,247	6,669	4,766								
8 years later	4,124	6,669									
9 years later	4,117										
Current estimate of ultimate cost	4,117	6,669	4,766	7,249	5,104	6,052	13,166	6,887	7,249	7,906	$ 69,165
Cumulative payments	4,117	6,669	3,700	6,955	4,768	5,354	9,277	4,741	5,210	4,067	54,858
Outstanding claims	$ -	$ -	$ 1,066	$ 294	$ 336	$ 698	$ 3,889	$ 2,146	$ 2,039	$ 3,839	$ 14,307
Liability for all prior accident years											357
Impact of discount and PFAD											716
Facility Association and risk sharing pool											940
Total gross claims											$ 16,320

3. Insurance Contracts (continued)

Net of reinsurance (000's)

	Accident Year										
Reporting date	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Total
At end of claim year	$ 5,869	$ 6,465	$ 4,563	$ 9,002	$ 5,600	$ 6,801	$ 8,576	$ 5,952	$ 7,067	$ 7,314	
1 year later	5,455	7,718	5,495	9,040	5,900	6,328	8,129	6,271	6,461		
2 years later	5,512	7,108	5,732	8,591	5,044	6,017	8,175	6,369			
3 years later	4,211	7,103	4,963	7,014	5,017	5,637	8,081				
4 years later	3,717	6,423	4,094	6,898	5,109	5,734					
5 years later	3,704	6,077	4,067	6,796	4,975						
6 years later	3,814	5,947	4,063	6,509							
7 years later	3,811	5,882	4,069								
8 years later	3,742	5,882									
9 years later	3,735										
Current estimate of ultimate cost	3,735	5,882	4,069	6,509	4,975	5,734	8,081	6,369	6,461	7,314	$ 59,129
Cumulative payments	3,735	5,882	3,700	6,418	4,641	5,073	7,353	4,512	4,942	4,067	50,323
Outstanding claims	$ -	$ -	$ 369	$ 91	$ 334	$ 661	$ 728	$ 1,857	$ 1,519	$ 3,247	$ 8,806
Liability for all prior accident years											134
Impact of discount and PFAD											411
Facility Association and risk sharing pool											940
Total net claims											$ 10,291

3. Insurance Contracts (continued)

Claim development (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.

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

	Property claims		Auto claims		Liability claims	
(000's)	**2017**	2016	**2017**	2016	**2017**	2016
5% increase in loss ratios						
Gross	**$ 289**	$ 285	**$ 390**	$ 367	**$ 61**	$ 61
Net	**250**	251	**320**	308	**41**	44
5% decrease in loss ratios						
Gross	**$ (289)**	$ (285)	**$ (390)**	$ (367)	**$ (62)**	$ (61)
Net	**(250)**	(251)	**(320)**	(308)	**(41)**	(44)

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

(d) Liability adequacy test

At each reporting date the Company performs a liability adequacy test on its insurance liabilities less deferred acquisition expenditures 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 and unappropriated members' surplus initially by writing off the deferred acquisition expenditures and subsequently by recognizing an additional liability for the provision for unearned premiums.

3. Insurance Contracts (continued)

(e) Unpaid claims recoverable from reinsurer

The Company enters into reinsurance contracts in the normal course of business in order to limit potential losses arising from certain exposures. Reinsurance premiums are accounted for in the same period as the related premiums for the direct insurance business being reinsured. Reinsurance liabilities, comprised of premiums payable for the purchase of reinsurance contracts, are included in accounts payable and accrued liabilities and are recognized as an expense when due.

The Company follows a policy of underwriting and reinsuring contracts of insurance which, in the main, limit the liability of the Company to $335,000 on any property claim and $410,000 on any automobile claim with no quota share ceded (2016 - $335,000 for property claim and $410,000 for automobile claim). It further limits the liability of the Company to the first $285,000 on any liability claim with no quota share ceded (2016 - $285,000).

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

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

	2017	2016
Balance, beginning of the year	**$ (35,990)**	$ 5,838
Submitted to reinsurer	**(2,567,723)**	(2,207,492)
Received from reinsurer	**2,530,648**	2,165,664
Balance, end of the year	**$ (73,065)**	$ (35,990)

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

December 31, 2017

3. Insurance Contracts (continued)

(e) Unpaid claims recoverable from reinsurer (continued)

Changes in reinsurer's share of unpaid claims recorded in the statement of financial position for the years-ended December 31, 2017 and their impact on net premiums earned for the year is as follows:

	2017	2016
Balance, beginning of the year	$ 6,601,924	$ 7,250,555
New claims reserve	592,000	1,380,038
Change in prior years' reserve	(457,386)	(1,465,245)
Submitted to reinsurer	(706,262)	(563,424)
Balance, end of the year	$ 6,030,276	$ 6,601,924

(f) Provision for refund of premium

Under the discretion of the Board of Directors, the Company may declare a refund to its policyholders based on premiums.

4. Investments

The Company classifies the majority of its investments as fair value through profit and loss. All transactions related to investments are recorded on a trade date basis. Investments that are classified at fair value through profit or loss are measured at fair value and changes therein are recognized in comprehensive income.

4. Investments (continued)

The following table provides 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:

	2017 Fair Value	2016 Fair Value
Available-for-sale:		
Fire Mutual Guarantee Fund	**$ 35,556**	$ 34,937
Fair value through profit or loss:		
Guaranteed investment certificates	**8,438,233**	8,560,544
Bonds and debentures	**3,778,601**	4,102,248
Canadian common shares	**6,170,754**	5,175,101
Foreign common shares	**5,885,060**	5,159,963
Canadian preferred shares	**58,061**	27,437
Greystone Fixed Income Pooled Fund	**24,072,361**	23,405,297
	$ 48,438,626	$ 46,465,527

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, including its investment in the Greystone Fixed Income Pooled Fund.

The Company's investment policy puts limits on the bond portfolio including portfolio composition limits, issuer type limits, bond quality limits, aggregate issuer limits, corporate sector limits and general guidelines for geographic exposure. The bond portfolio includes 55% (2016 – 52%) of bonds rated A or better. The Company's investment policy limits investment in bonds and debentures of the various ratings to limits ranging from 50% to 90% of the Company's portfolio. Funds should be invested in bonds and debentures of Federal, Provincial or Municipal Government and corporations rated BBB or better. All fixed income portfolios are measured for performance on a quarterly basis and monitored by management on a monthly basis.

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

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

4. Investments (continued)

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. Claim payments are funded by current operating cash flow including investment income.

Maturity profile of bonds held is as follows:

	Within 1 year	2 to 5 years	Total Fair Value
December 31, 2017	**$ 2,621,965**	**$ 1,192,192**	**$ 3,814,157**
Percent of Total	**68.74%**	**31.26%**	**100%**
December 31, 2016	$ 1,601,552	$ 2,536,041	$ 4,137,593
Percent of Total	38.71%	61.29%	100%

The effective interest rate of the bonds portfolio held at December 31, 2017 is 2.1% (2016 - 2.5%).

The interest rate ranges for the guaranteed investment certificates held at December 31, 2017 are 1.7% to 2.75% (2016 - 0.95% to 2.75%) with maturities ranging from 2018 to 2022 (2016 - 2017 to 2021)

There have been no significant changes from the previous year in the exposure to liquidity risk or policies, procedures and methods used to measure the 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 Board of Directors. Diversification techniques are utilized to minimize risk. The Policy limits the investment in equities to 25% of the portfolio, international equities cannot exceed 50% of the total equity balance.

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 is exposed to currency risk on its investments in the United States. Included in the statement of financial position are U.S. dollar denominated investments of $6,173,754 CDN (2016 - $5,187,399 CDN). If the U.S. dollar weakened/strengthened by 5% against the Canadian dollar, all other variables held constant, the net effect on the unappropriated members' surplus for the year would be $308,688 lower/higher (2016 - $259,370).

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

4. Investments (continued)

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, including it's investment in the Greystone Fixed Income Pooled Fund.

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 for its investments held in support of its claims liabilities. This allows the Company to effectively manage a portion of its interest rate risk. 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 the Company is exposed to significant interest rate risk. Generally, the Company’s investment income related to its fair value through profit or loss financial investment portfolio will move with interest rates over the medium to long-term with short-term interest rate fluctuations creating unrealized gains or losses in comprehensive income.

At December 31, 2017 a 1% move in interest rates, with all other variables held constant, could impact the market value of guaranteed investment certificates, bonds and debentures and the Greystone Fixed Income Pooled Fund by $1,530,700 (2016 - $1,451,128).

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

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. At December 31, 2017, 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 equities of $1,209,137 (2016 - $1,028,994).

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

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

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities using the last bid price;

- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and

- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

4. Investments (continued)

Financial assets recorded at fair value by the level of the fair value hierarchy:

	Level 1	Level 2	Level 3	Total
December 31, 2017				
Available-for-sale:				
Fire Mutual Guarantee Fund	**$ -**	**$ 35,556**	**$ -**	**$ 35,556**
Fair value through profit or loss:				
Guaranteed investment certificates	**8,438,233**	**-**	**-**	**8,438,233**
Bonds and debentures - Canadian Federal	**-**	**3,547,968**	**-**	**3,547,968**
Canadian common shares	**6,170,754**	**-**	**-**	**6,170,754**
Foreign common shares	**6,115,692**	**-**	**-**	**6,115,692**
Canadian preferred shares	**58,062**	**-**	**-**	**58,062**
Greystone Fixed Income Pooled Fund	**-**	**24,072,361**	**-**	**24,072,361**
Total	**$ 20,782,741**	**$ 27,655,885**	**$ -**	**$ 48,438,626**

	Level 1	Level 2	Level 3	Total
December 31, 2016				
Available-for-sale:				
Fire Mutual Guarantee Fund	$ -	$ 34,937	$ -	$ 34,937
Fair value through profit or loss:				
Guaranteed investment certificates	8,560,544	-	-	8,560,544
Bonds and debentures - Canadian Federal	-	4,102,248	-	4,102,248
Canadian common shares	5,175,101	-	-	5,175,101
Foreign common shares	5,159,963	-	-	5,159,963
Canadian preferred shares	27,437	-	-	27,437
Greystone Fixed Income Pooled Fund	-	23,405,297	-	23,405,297
Total	$ 18,923,045	$ 27,542,482	$ -	$ 46,465,527

Transfers between levels are considered to have occurred at the date of the event or change in circumstances that caused the transfer. There were no transfers between Level 1 and Level 2 for the year ended December 31, 2017. There were also no transfers in or out of Level 3.

5. Investment Income

		2017		2016
Interest income	**$**	**276,823**	$	283,326
Dividend income		**264,548**		190,213
Realized (loss) gain on disposal of investments		**10,284**		(129,164)
Investment expenses		**(338,129)**		(113,632)
Unrealized gain on investments		**1,657,164**		1,661,376
	$	**1,870,690**	$	1,892,119

6. 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. Reinsurance is utilized to protect capital from catastrophic losses as the frequency and severity of these losses are inherently unpredictable. To limit their potential impact, the Company purchases reinsurance, the details of which are outlined in Note 3. For the purpose of capital management, the Company has defined capital as members' equity.

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

7. Other Operating and Administrative Expenses

	2017	2016
Advertising	**$ 113,379**	$ 209,112
Association fees, training and other	**75,950**	55,952
Bad debts	**4,398**	13,485
Computer services	**252,580**	199,761
Employee benefits	**241,376**	524,108
Facility office costs	**4,339**	3,598
Inspection of risks and fire prevention	**58,732**	41,898
Insurance	**47,980**	50,868
Occupancy costs	**45,088**	37,894
Office and general	**156,720**	181,718
Postage and telephone	**41,379**	32,306
Conventions	**64,510**	54,276
Provincial premium tax	**21,310**	22,653
Salaries and directors' fees	**756,444**	721,856
Scholarships	**5,100**	4,300
Statistics and assessments	**42,209**	53,853
	$ 1,931,494	$ 2,207,638

8. Income taxes

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

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

	2017	2016
Comprehensive income for the year	**$ 2,417,077**	$ 1,946,287
Expected taxes based on the statutory rate	**$ 640,525**	$ 515,766
Non deductible expenses	**516**	2,164
Canadian dividend income not subject to tax	**(45,218)**	(50,406)
Effect of foreign non-business tax credit	**(13,888)**	(10,659)
Other	**5,583**	28,556
Total income tax expense	**$ 587,518**	$ 485,421

9. Property and equipment

Property and equipment is initially recorded at cost and subsequently measured at cost less accumulated depreciation and accumulated impairment losses. Depreciation is recognized in comprehensive income and is provided on a straight-line basis over the estimated useful life of the assets as follows:

Buildings	2.5%
Computer equipment	20.0%
Equipment and fixtures	10.0%

Depreciation methods, useful lives and residual values are reviewed annually and adjusted if necessary.

	2017		
	Cost	**Accumulated Depreciation**	**Net Book Value**
Land	**$ 450,137**	**$ -**	**$ 450,137**
Buildings	**1,945,360**	**453,057**	**1,492,303**
Computer equipment	**240,301**	**227,795**	**12,506**
Equipment and fixtures	**267,735**	**238,888**	**28,847**
Total	**$ 2,903,533**	**$ 919,740**	**$ 1,983,793**

	2016		
	Cost	**Accumulated Depreciation**	**Net Book Value**
Land	$ 101,500	$ -	$ 101,500
Buildings	725,976	437,114	288,862
Computer equipment	234,530	222,424	12,106
Equipment and fixtures	255,304	235,267	20,037
Total	$ 1,317,310	$ 894,805	$ 422,505

Included in capital assets is land and building under development totaling $1,656,265 (2016 - $88,243), comprised of $348,637 (2016 - $nil) included in land and $1,307,628 (2016- $88,243) included in buildings. These assets have not been amortized as they are not in use.

10. Committments

The Company has a Letter of Credit in the the amount of $181,386 (2016 - $nil) payable to the City of Hamilton as part of the purchase of the land for construction in progress which is secured by the Current Account balance held by the Company at Meridian Credit Union.

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

12. 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				
Short term employee benefits and directors' fees	**$**	**554,655**	$	599,356
Total pension and other post-employment benefits		**26,535**		26,073
Premiums		**74,977**		66,477
Claims paid		**800**		8,744
	$	**656,967**	$	700,650

13. Standards, amendments and interpretations not yet effective

At the date of authorization of these financial statements, certain new standards, amendments and interpretations to existing standards have been published by the IASB but are not yet effective, and have not been early adopted by the Company.

Information on new standards, amendments and interpretations that are expected to be relevant to the Company’s financial statements is provided below. Certain other new standards, amendments, and interpretations have been issued but are not expected to have a material impact on the Company’s financial statements.

i) IFRS 9 Financial Instruments replaces IAS 39 Financial Instruments: Recognition and Measurement

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 (loss) income. 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, the Company has been provided the option of deferring the adoption of IFRS 9 given the nature of its insurance operations 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 has not yet evaluated what impact this adoption will have on its financial results.

13. Standards, amendments and interpretations not yet effective (continued)

iii) IFRS 16 Leases

IFRS 16 supersedes IAS 17 Leases, IFRIC 4 Determining whether an Arrangement contains a Lease, SIC-15 Operating Leases – Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. It eliminates the distinction between operating and finance leases from the perspective of the lessee. All contracts that meet the definition of a lease will be recorded in the statement of financial position with a “right of use” asset and a corresponding liability. The asset is subsequently accounted for as property, plant and equipment or investment property and the liability is unwound using the interest rate inherent in the lease. The accounting requirements from the perspective of the lessor remains largely in line with previous IAS 17 requirements. The effective date for IFRS 16 is January 1, 2019.

iii) IFRS 17 Insurance Contracts

IFRS 17 Insurance Contracts, was issued in May 2017 and lays out a fundamentally new way of measuring and presenting insurance contracts and related financial statement items for entities that issue insurance contracts. Some of the key aspects of IFRS 17 include new models for insurance liabilities, changes to discounting and the rate being used to discount claims liabilities, and changes to deferred premium acquisition costs. The technical aspects of IFRS 17 are complex and will require specific consultation on the situation to determine the exact impact. The effective date for IFRS 17 is January 1, 2021, with the requirement to restate comparative figures. The Company is in the process of evaluating the impact of the new standard.