Dumfries Mutual Insurance Company
Financial Statements
For the year ended December 31, 2019

Contents

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Independent Auditor's Report

To the Board of Directors of Dumfries Mutual Insurance Company

Opinion

We have audited the financial statements of Dumfries Mutual Insurance Company (the "Company"), which comprise the statement of financial position as at December 31, 2019 and the statements of comprehensive income and unappropriated members' surplus and cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2019, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Basis for Opinion

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

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

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

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the 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.

Auditor's Responsibility

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

Independent Auditor's Report

Auditor's Responsibility (continued)

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the 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 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 financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

BDO Canada LLP

Chartered Professional Accountants, Licensed Public Accountants

Mississauga, Ontario
February 12, 2020

Dumfries Mutual Insurance Company
Statement of Financial Position

December 31		2019		2018
Assets				
Cash	**$**	**1,923,237**	$	1,814,928
Due from policyholders		**5,417,140**		4,576,823
Investments (Note 5)		**48,223,778**		44,315,738
Prepaid expenses		**78,148**		50,549
Income taxes recoverable		**-**		857,840
Unpaid claims recoverable from reinsurer (Note 4)		**2,890,000**		3,926,000
Deferred policy acquisition expenditures (Note 4)		**1,006,176**		871,465
Property and equipment (Note 11)		**4,969,755**		4,978,313
	$	**64,508,234**	$	61,391,656
Liabilities				
Accounts payable and accrued liabilities	**$**	**588,608**	$	299,748
Provision for refund of premium		**312**		62,632
Income taxes payable		**78,238**		-
Due to reinsurer (Note 4)		**323,653**		145,080
Unpaid claims		**14,637,653**		14,529,373
Unearned premiums (Note 4)		**8,940,302**		7,634,526
Future income tax liability		**129,852**		95,749
		24,698,618		22,767,108
Members' surplus				
Unappropriated members' surplus		**39,809,616**		38,624,548
	$	**64,508,234**	$	61,391,656

On behalf of the Board:

Director

Director

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

For the year ended December 31	2019	2018
Revenue		
Gross premiums written	**$ 18,359,433**	$ 15,849,936
Less: reinsurance ceded	**(3,205,329)**	(3,007,202)
Net premiums written	**15,154,104**	12,842,734
Change in unearned	**(1,305,776)**	(534,688)
Net premiums earned	**13,848,328**	12,308,046
Service charges	**169,417**	124,197
	14,017,745	12,432,243
Direct losses incurred		
Gross claims and adjustment expenses	**13,680,814**	11,920,851
Reinsurance recoveries	**(2,678,748)**	(1,839,053)
	11,002,066	10,081,798
	3,015,679	2,350,445
Expenses		
Commissions expense	**2,029,323**	1,851,810
Other operating and administrative expenses (Note 8)	**2,581,378**	2,240,048
	4,610,701	4,091,858
Net underwriting loss	**(1,595,022)**	(1,741,413)
Other income		
Investment income (Note 6)	**3,142,606**	929,455
Gain on disposal of property	**-**	860,448
	3,142,606	1,789,903
Comprehensive income before income taxes	**1,547,584**	48,490

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

For the year ended December 31	2019	2018
Income taxes (Note 9)		
Current	**328,413**	(273,684)
Deferred	**34,103**	235,749
	362,516	(37,935)
Comprehensive income for the year	**1,185,068**	86,425
Unappropriated members' surplus, beginning of year	**38,624,548**	38,538,123
Unappropriated members' surplus, end of year	**$ 39,809,616**	$ 38,624,548

Dumfries Mutual Insurance Company
Statement of Cash Flows

For the year ended December 31	2019	2018
Cash provided by (used in)		
Operating activities		
Comprehensive income	**$ 1,185,068**	$ 86,425
Adjustments for:		
Gain on disposal of property and equipment	**-**	(860,448)
Depreciation	**183,475**	98,484
Current income taxes	**328,413**	(273,684)
Deferred income taxes	**34,103**	235,749
Realized gain on disposal of investments	**(396,534)**	(863,401)
Unrealized (gain) loss on investments	**(1,720,205)**	1,298,666
	(385,680)	(278,209)
Changes in working capital		
Due from policyholders	**(840,317)**	(569,372)
Accounts payable and accrued liabilities	**288,860**	(736,499)
	(551,457)	(1,305,871)
Changes in insurance contract related balances, provisions		
Provision for refund of premium	**(62,320)**	(313,684)
Due to reinsurer	**178,573**	72,015
Unpaid claims	**108,280**	(1,791,938)
Unearned premiums	**1,305,776**	534,688
Prepaid expenses	**(27,599)**	64,838
Unpaid claims recoverable from reinsurer	**1,036,000**	2,104,276
Deferred policy acquisition expenditures	**(134,711)**	(53,324)
	2,403,999	616,871
Cash flows related to income taxes	**607,665**	(584,156)
Total cash inflows (outflows) from operating activities	**2,074,527**	(1,551,365)
Investing activities		
Sale of investments	**21,515,184**	36,464,360
Purchase of investments	**(23,306,485)**	(30,964,147)
Purchase of property and equipment	**(174,917)**	(3,394,986)
Total cash (outflows) inflows from investing activities	**(1,966,218)**	2,105,227
Increase in cash	**108,309**	553,862
Cash, beginning of year	**1,814,928**	1,261,066
Cash, end of year	**$ 1,923,237**	$ 1,814,928

December 31, 2019

1. Corporate Information

Dumfries Mutual Insurance Company (the "Company" or "Dumfries") is incorporated under the laws of Ontario and is subject to the Ontario Insurance Act. It is licensed to write property, liability, automobile and farmers' accident insurance in Ontario. The Company's head office is located in Sheffield, Ontario.

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

These financial statements have been authorized for issue by the Board of Directors on REPORT DATE.

2. Basis of Preparation

(a) Statement of Compliance

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

(b) Basis of Measurement

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

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

(c) Judgment and Estimates

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

2. Basis of Preparation (continued)

- The calculation of unpaid claims, including the determination of the initial claim liability, discount rates, the estimate of time until ultimate settlement and the performance of a liability adequacy test (Note 4);
- The determination of the recoverability of deferred policy acquisition expenses (Note 4); and
- The classification of financial assets at FVTPL, which includes assessing the business model within which the assets are held and whether the contractual terms of the assets are solely payments of principal and interest on the principal amount outstanding (Note 5).

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

3. Adoption of new accounting standards

Accounting standards, interpretations and amendments effective for accounting years beginning on or after January 1, 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.

Impacts of adoption of IFRS 16

There was no impact of adopting IFRS 16 as the Company does not have any leases as at December 31, 2019.

IFRIC Interpretation 23 *Uncertainty over Income Tax Treatments* (IFRIC 23)

IFRIC 23 provides guidance on the accounting for current and deferred tax liabilities and assets in circumstances in which there is uncertainty over income tax treatments. The Interpretation requires:

- An entity to contemplate whether uncertain tax treatments should be considered separately, or together as a group, based on which approach provides better predictions of the resolution;
- An entity to determine if it is probable that the tax authorities will accept the uncertain tax treatment; and

3. Adoption of new accounting standards (continued)

IFRIC Interpretation 23 *Uncertainty over Income Tax Treatments* (IFRIC 23) (continued)

- If it is not probable that the uncertain tax treatment will be accepted, measure the tax uncertainty based on the most likely amount or expected value, depending on whichever method better predicts the resolution of the uncertainty.

The adoption of IFRIC 23 did not have a material impact on the Company's financial statements.

4. Insurance contracts

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

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

(a) Premiums and unearned premiums

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

The Company recognizes premium income evenly over the term of the insurance policy using the pro rata method. The portion of the premium related to the unexpired portion of the policy at the end of the fiscal year is reflected in unearned premiums (UEP). Changes in unearned premiums recorded in the statement of financial position for the years-ended December 31, 2019 and their impact on net premiums earned is as follows:

	2019	2018
Balance, beginning of the year	**$ 7,634,526**	$ 7,099,838
Premiums written	**18,359,433**	15,849,936
Premiums earned during year	**(15,747,881)**	(14,780,560)
Change in unearned premiums	**(1,305,776)**	(534,688)
Balance, end of the year	**$ 8,940,302**	$ 7,634,526

4. Insurance contracts (continued)

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 Regulatory Authority of Ontario and therefore may result in a delay in adjusting the pricing to exposed risk.

The Company is exposed to a pricing risk to the extent that unearned premiums are insufficient to meet the related future policy costs. Evaluation is performed regularly to estimate future claims costs, related expenses, and expected profit in relation to unearned premiums. There was no premium deficiency at December 31, 2019.

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

(b) Unpaid claims recoverable from reinsurer

The Unpaid claims recoverable from reinsurer are recognized as an asset using principles consistent with the Company's method for determining the unearned premium liability.

(c) Deferred policy acquisition expenses

Acquisition costs are comprised of agents' commissions and premium taxes. These costs are deferred and amortized over the terms of the related policies to the extent that they are considered to be recoverable from unearned premiums, after considering the related anticipated claims and expenses. Changes in deferred policy acquisition expenses recorded in statement of financial position for the years-ended December 31, 2019 and their impact on fees, commissions and other acquisition expenses is as follows:

	2019	2018
Balance, beginning of the year	**$ 871,465**	$ 818,141
Acquisition expenses incurred	**2,175,666**	1,901,643
Expensed during the year	**(2,040,955)**	(1,848,319)
Balance, end of the year	**$ 1,006,176**	$ 871,465

4. Insurance Contracts (continued)

(d) Unpaid claims and adjustment expenses

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

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

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

	December 31, 2019			December 31, 2018		
	Gross	**Re-insurance**	**Net**	Gross	Re-insurance	Net
Outstanding claims provision						
Long-term	**$ 8,029,544**	**$ 1,393,595**	**$ 6,635,950**	$ 6,808,160	$ 2,474,420	$ 4,333,740
Short-term	**1,305,070**	**63,517**	**1,241,553**	2,669,100	-	2,669,100
Facility Association and other residual pools	**434,653**	**-**	**434,653**	424,374	-	424,374
	9,769,267	**1,457,112**	**8,312,156**	9,901,634	2,474,420	7,427,214
Provision for claims incurred but not reported	**4,868,386**	**1,432,888**	**3,435,498**	4,627,739	1,451,580	3,176,159
	$ 14,637,653	**$ 2,890,000**	**$ 11,747,654**	$ 14,529,373	$ 3,926,000	$ 10,603,373

4. Insurance Contracts (continued)

(d) Unpaid claims and adjustment expenses (continued)

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

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

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

	2019	2018
Unpaid claims liabilities - beginning of year – net of reinsurance	**$ 10,603,373**	$ 10,291,035
Decrease in estimated losses and expenses, for losses occurring in prior years	**1,717,280**	312,338
Provision for losses and expenses on claims occurring in the current year	**9,391,000**	9,770,000
Payment on claims:		
Current year	**(4,747,000)**	(6,328,000)
Prior years	**(5,217,000)**	(3,442,000)
Unpaid claims – end of year - net of reinsurance	**11,747,653**	10,603,373
Reinsurer’s share	**2,890,000**	3,926,000
	$ 14,637,653	$ 14,529,373

4. Insurance Contracts (continued)

Claim development

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

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

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

The estimation of claim development involves assessing the future behaviour of claims, taking into consideration the consistency of the Company's claim handling procedures, the amount of information available, the characteristics of the line of business from which the claim arises and 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 tables below 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.

4. Insurance Contracts (continued)

Gross claims (000's)

	Accident Year										
Reporting date	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Total
At end of claim year	$ 6,944	$ 10,641	$ 5,701	$ 6,938	$ 13,724	$ 6,972	$ 7,883	$ 7,906	$ 10,304	$ 12,153	
1 year later	6,884	9,851	6,031	7,184	12,598	7,100	7,249	7,699	10,215		
2 years later	6,994	9,962	5,491	6,631	13,362	6,887	6,836	7,064			
3 years later	6,276	8,814	5,209	6,015	13,166	6,711	6,700				
4 years later	4,807	8,672	5,237	6,032	13,451	6,402					
5 years later	4,780	7,715	5,104	6,617	13,931						
6 years later	4,760	7,249	4,974	6,629							
7 years later	4,766	7,298	4,951								
8 years later	4,192	7,454									
9 years later	4,192										
Current estimate of ultimate cost	4,192	7,454	4,951	6,629	13,931	6,402	6,700	7,064	10,215	12,153	$ 79,691
Cumulative payments	4,192	7,454	4,807	5,592	13,408	5,749	5,728	5,679	7,680	6,326	66,614
Outstanding claims	$ -	$ -	$ 143	$ 1,037	$ 524	$ 653	$ 972	$ 1,385	$ 2,535	$ 5,828	$ 13,077
Liability for all prior accident years											15
Impact of discount and PFAD											550
Facility Association and risk sharing pool											996
Total gross claims											$ 14,638

4. **Insurance Contracts** (continued)

Net of reinsurance (000's)

	Accident Year										
Reporting date	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	Total
At end of claim year	$ 4,563	$ 9,002	$ 5,600	$ 6,801	$ 8,576	$ 5,952	$ 7,067	$ 7,314	$ 9,721	$ 10,416	
1 year later	5,495	9,040	5,900	6,328	8,129	6,271	6,461	7,230	9,591		
2 years later	5,732	8,691	5,044	6,017	8,173	6,369	6,302	6,825			
3 years later	4,963	7,014	5,017	5,637	8,081	6,110	6,328				
4 years later	4,094	6,898	5,109	5,734	8,639	6,149					
5 years later	4,067	6,796	4,975	5,854	8,606						
6 years later	4,063	6,509	4,847	5,848							
7 years later	4,069	6,485	4,824								
8 years later	3,959	6,501									
9 years later	3,959										
Current estimate of ultimate cost	3,959	6,501	4,824	5,848	8,606	6,149	6,328	6,825	9,591	10,416	$ 69,047
Cumulative payments	3,959	6,501	4,680	5,311	8,319	5,521	5,436	5,679	7,615	5,710	58,731
Outstanding claims	$ -	$ -	$ 144	$ 537	$ 287	$ 628	$ 892	$ 1,146	$ 1,976	$ 4,706	$ 10,316
Liability for all prior accident years											(129)
Impact of discount and PFAD											565
Facility Association and risk sharing pool											996
Total net claims											$ 11,748

4. 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)	**2019**	2018	**2019**	2018	**2019**	2018
5% increase in loss ratios						
Gross	**$ 337**	$ 309	**$ 513**	$ 420	**$ 68**	$ 63
Net	**283**	264	**421**	332	**54**	47
5% decrease in loss ratios						
Gross	**$ (337)**	$ (309)	**$ (513)**	$ (420)	**$ (68)**	$ (63)
Net	**(283)**	(264)	**(421)**	(332)	**(54)**	(47)

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.

(e) 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 discount rate. If that assessment shows that the carrying amount of the liabilities is inadequate, any deficiency is recognized as an expense in profit and loss initially by writing down the deferred policy acquisition expense and subsequently by recognizing additional unearned premiums.

4. Insurance Contracts (continued)

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

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

The Company follows a policy of underwriting and reinsuring contracts of insurance which, in the main, limit the liability of the Company to an amount on any one claim of $335,000 (2018 - $335,000) in the event of a property claim, an amount of $410,000 (2018 - $410,000) in the event of an automobile claim and $285,000 (2018 - $285,000) in the event of a liability claim. For amounts over the respective limits there is a 50% retention to a specified maximum. In addition, the Company has obtained stop loss reinsurance which limits the liability of all claims in a specific year to 80% (2018 – 80%) of gross net earned premiums for property and automobile.

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

Expected reinsurance recoveries on unpaid claims and adjustment expenses are recognized as assets at the same time and using principles consistent with the Company's method for establishing the related liability. Changes in due from reinsurer recorded in the statement of financial position for the year ended December 31, 2019 is as follows:

	2019	2018
Balance, beginning of the year	**$ 3,926,000**	$ 6,030,276
New claims reserve	**619,242**	720,969
Change in prior years' reserve	**1,078,206**	59,044
Submitted to reinsurer	**(2,733,448)**	(2,884,289)
Balance, end of the year	**$ 2,890,000**	$ 3,926,000

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. At year end, the Company reviewed the amounts owing from its reinsurer and determined that no allowance is necessary.

4. Insurance Contracts (continued)

(g) Refund of premium

At the discretion of the board of directors, the Company may declare a refund to its policyholders based on the premiums paid.

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5. Investments

(a) Recognition and initial measurement

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

(b) Classification and subsequent measurement

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

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

The Company classifies its equity instruments as FVTPL.

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

(c) Derecognition

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

5. Investments (continued)

(d) Risks

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

	2019	2018
Bonds issued by		
Provincial	**399,923**	3,509,369
Municipal	**-**	206,062
US Treasury	**1,890,649**	1,007,866
Corporate	**1,825,885**	1,806,482
	4,116,456	6,529,778
Equity investments		
Canadian listed companies	**4,834,823**	4,668,181
Canadian private company	**1,400,000**	-
US listed companies	**4,709,892**	4,730,926
	10,944,715	9,399,107
Other investments		
Guaranteed investment certificates, money market funds and term deposits	**33,129,932**	28,354,173
Fire mutual guarantee fund	**32,675**	32,680
	32,375,838	27,367,759
Total investments	**$48,223,778**	$44,315,738

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

The Company's investment policy puts limits on the bond portfolio including portfolio composition limits, issuer type limits, bond quality limits, aggregate issuer limits, corporate sector limits and general guidelines for geographic exposure. The bond portfolio includes 71% (2018 – 88%) 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 20% to 90% of the Company's portfolio. The Company's policy requires that funds be invested in bonds and debentures of Federal, Provincial or Municipal Government and corporations rated A or better. All fixed income portfolios are measured for performance on a quarterly basis and monitored by management on a monthly basis.

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

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

5. 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. The Company has no material commitments for capital expenditures, and there is no need for such expenditures in the normal course of business. Claim payments are funded by current operating cash flow including investment income.

The Company's investment policy requires that 5% to 75% of the Company's portfolio be held in cash and short-term investments. Short-term investments include money market funds, in addition to GICs and term deposits with an original maturity of less than one year.

Maturity profile of bonds held is as follows:

	Within 1 year	2 to 5 years	Total Fair Value
December 31, 2019	**$ 1,695,456**	**$ 2,401,957**	**$ 4,097,413**
Percent of Total	**41.38%**	**58.62%**	**100%**
December 31, 2018	$ 2,061,083	$ 4,083,727	$ 6,144,810
Percent of Total	33.54%	66.46%	100%

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

Market factors that will impact the fair value of investments include three types of risk: currency risk, interest rate risk and equity risk.

The Company'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.

Company's currency risk is related to stock holdings which are limited to US listed equities in sectors which are not readily available in Canada. The Company limits its holdings in foreign equity to 50% of total equity investments in accordance with its investment policy. Foreign currency changes are monitored by the Investment Committee and holdings are adjusted when offside of the investment policy

The Company is exposed to currency risk on its investments in the US Included in the statement of financial position are US denominated investments of $7,270,543 CDN (2018 - $6,432,344 CDN). If the US 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 $363,527 lower/higher (2018 - $321,617).

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

5. Investments (continued)

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 gains or losses in profit or loss.

At December 31, 2019, a 1% move in interest rates, with all other variables held constant, could impact the market value of bonds by $ 65,340 (2018 - $91,119).

The Company is exposed to equity risk through its portfolio of stocks in listed Canadian and US companies. At December 31, 2019, 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 equity investments of $954,472 (2018 - $939,911). This change would be recognized in comprehensive income.

The Company's investment policy limits investment in preferred and common shares to a maximum of 25% of the market value of the portfolio. The total investment in preferred and common shares cannot exceed 25% of total assets.

Equities are monitored by the Investment Committee and the board of directors and holdings are adjusted following each quarter to ensure the investments portfolio remains in compliance with the investment policy.

The fair value of the investment in the Canadian private company fluctuates based on the value of underlying net assets held by the private company. At December 31, 2019, the change in measurement inputs would not result in a material adjustment to the Company's investment.

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

(e) Fair value measurement

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

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

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

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

5. 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, 2019				
Guaranteed investment certificates, money market funds and term deposits	**33,129,932**	**-**	**-**	**33,129,932**
Bonds	**-**	**3,530,580**	**-**	**3,530,580**
Canadian equities	**4,834,823**	**-**	**-**	**4,834,823**
Canadian private company	**-**	**-**	**1,400,000**	**1,400,000**
US equities	**4,709,892**	**-**	**-**	**4,709,892**
Canadian preferred shares	**585,876**	**-**	**-**	**585,876**
Fire Mutual Guarantee Fund	**-**	**32,675**	**-**	**32,675**
Total	**$ 43,260,523**	**$ 3,563,255**	**$ 1,400,000**	**$ 48,223,778**

	Level 1	Level 2	Level 3	Total
December 31, 2018				
Guaranteed investment certificates, money market funds and term deposits	28,354,173	-	-	28,354,173
Bonds	-	6,074,993	-	6,074,993
Canadian equities	4,668,181	-	-	4,668,181
US equities	4,730,926	-	-	4,730,926
Canadian preferred shares	454,785	-	-	454,785
Fire mutual guarantee fund	-	32,680	-	32,680
Total	$ 38,208,065	$ 6,107,673	$ -	$ 44,315,738

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

The investment in a Canadian private company is recorded at fair value and is not traded on an open market. The fair value of this investment is based on valuation techniques that include inputs that are not based on observable market data (unobservable inputs). Therefore, it is classified as Level 3.

6. Investment income

		2019		2018
Interest income	**$**	**962,744**	$	634,715
Dividend income		**213,687**		277,755
Realized gain on disposal of investments		**396,534**		863,401
Investment (expenses) income		**(150,564)**		452,250
Unrealized gain (loss) on investments		**1,720,205**		(1,298,666)
	$	**3,142,606**	$	929,455

7. Capital Management

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

The Company's objectives with respect to capital management are to maintain a capital base that is structured to exceed regulatory requirements and to best utilize capital allocations.

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

8. Other Operating and Administrative Expenses

	2019	2018
Advertising and donations	**$ 121,571**	$ 108,182
Association fees, training and other	**110,118**	96,283
Bad debts	**6,425**	36,263
Computer services	**439,326**	581,423
Depreciation	**183,475**	98,484
Employee benefits	**406,519**	269,940
Inspection of risks and fire prevention	**82,598**	36,623
Insurance	**54,124**	52,198
Occupancy costs	**178,966**	135,913
Office and professional fees	**198,454**	201,229
Postage and telephone	**61,783**	79,786
Premium Tax	**33,289**	29,550
Salaries and directors' fees	**1,382,725**	1,168,133
Scholarships	**4,900**	5,100
Statistics and assessments	**55,719**	54,143
Travel and conventions	**91,942**	91,353
Internal adjusting - allocation to claims	**(830,556)**	(804,555)
	$ 2,581,378	$ 2,240,048

9. Income taxes

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

The significant components of the tax effect of the amounts recognized in other comprehensive income are composed of:

Reasons for the difference between tax expense for the year and the expected income taxes based on the statutory tax rate of 26.5% (2018 – 26.5%) are as follows:

	2019	2018
Comprehensive income for the year	**$ 1,547,584**	$ 48,490
Expected taxes based on the statutory rate	**$ 410,110**	$ 12,850
Non deductible expenses	**124**	543
Canadian dividend income not subject to tax	**(40,359)**	(48,468)
Effect of foreign non-business tax credit	**(10,013)**	-
Other	**2,654**	(2,860)
Total income tax expense	**$ 362,516**	$ (37,935)

10. 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 to their proportionate share in meeting this objective.

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

11. Property and equipment

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

Building	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.

11. Property and equipment (continued)

	Land and building	Computer equipment	Equipment and fixtures	Total
Cost				
Balance at January 1, 2018	$ 2,395,497	$ 252,731	$ 255,307	$ 2,903,535
Additions	2,837,901	14,564	542,520	3,394,985
Disposals	739,232	12,430	255,304	1,006,966
Balance at December 31, 2018	4,494,166	254,865 $	542,522 $	5,291,553
Additions	72,810	13,106	89,001	174,917
Disposals	-	-	-	-
Balance at December 31, 2019	**$ 4,566,976**	**$ 267,971**	**$ 631,523**	**$ 5,466,470**
Accumulated Depreciation				
Balance at January 1, 2018	$ 453,057	$ 227,796	$ 238,888	$ 919,741
Depreciation	61,896	7,051	29,537	98,484
Disposals	463,686	-	241,299	-
Balance at December 31, 2018	51,267	234,847 $	27,126 $	313,240
Depreciation	103,443	21,330	58,702	183,475
Disposals	-	-	-	-
Balance at December 31, 2019	**$ 154,710**	**$ 256,177**	**$ 85,828**	**$ 496,715**
Net book value:				
December 31, 2018	$ 4,442,899	$ 20,018	$ 515,396	$ 4,978,313
December 31, 2019	**$ 4,412,266**	**$ 11,794**	**$ 545,695**	**$ 4,969,755**

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:

	2019	2018
Compensation		
Short term employee benefits and directors' fees	**$ 686,800**	$ 691,041
Total pension and other post-employment benefits	**32,631**	31,604
Premiums	**79,208**	79,471
Claims paid	**7,826**	18,665
Reversal of claims reserved	**(23,452)**	-
	$ 783,013	$ 820,781

13. Standards, amendments and interpretations not yet effective

Certain new standards, amendments to standards, and interpretations were issued by the IASB or the IFRS Interpretations Committee that are mandatory for accounting years beginning after January 1, 2020 or later that the Company has decided not to adopt early.

Of those new standards, interpretations and amendments that are not yet effective, IFRS 17 *Insurance Contracts* is expected to have a material impact on the Company’s financial statements in the period of initial application.

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