



LAMBTON MUTUAL

INSURANCE COMPANY

Financial Statements

For the year ended December 31, 2014

Lambton Mutual Insurance Company

Financial Statements

For the year ended December 31, 2014

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Independent Auditor's Report

To the Directors and Policyholders of Lambton Mutual Insurance Company

We have audited the accompanying financial statements of Lambton Mutual Insurance Company which comprise the statement of financial position as at December 31, 2014 and the statements of comprehensive income, policyholders' surplus and cash flows for the year 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 risk 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 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 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, these financial statements present fairly, in all material respects, the financial position of Lambton Mutual Insurance Company as at December 31, 2014 and the results of its operations and cash flows for the year then ended in accordance with International financial reporting standards.

BDO Canada LLP

Chartered Professional Accountants, Licensed Public Accountants

Sarnia, Ontario
January 28, 2015

Lambton Mutual Insurance Company
Statement of Financial Position
As at December 31, 2014

	2014	2013
Assets		
Cash	\$ 2,173,384	\$ 2,560,491
Investments (Note 4)	48,534,446	43,130,654
Investment income accrued	167,242	119,810
Income taxes recoverable	-	288,252
Due from reinsurers (Note 6)	-	489,535
Due from brokers and policyholders	3,647,579	3,671,121
Reinsurers' share of provision for unpaid claims (Note 6)	7,806,598	11,518,863
Deferred policy acquisition expenses (Note 6)	1,435,010	1,426,267
Property, plant & equipment (Note 5)	1,056,871	1,264,895
Intangible assets (Note 5)	241,565	373,156
Other assets	153,453	135,447
Deferred income taxes (Note 8)	49,000	13,000
	<u>\$65,265,148</u>	<u>\$ 64,991,491</u>
Liabilities		
Accounts payable and accrued liabilities	\$ 384,211	\$ 361,446
Income taxes payable	584,761	-
Unearned premiums (Note 6)	9,294,230	9,337,849
Provision for unpaid claims (Note 6)	23,128,442	26,409,530
	<u>33,391,644</u>	<u>36,108,825</u>
Policyholders' Surplus		
Unappropriated policyholders' surplus	<u>31,873,504</u>	<u>28,882,666</u>
	<u>\$65,265,148</u>	<u>\$ 64,991,491</u>

Signed on behalf of the Board by:

_____ Director

_____ Director

Lambton Mutual Insurance Company
Statement of Comprehensive Income
For the Year Ended December 31, 2014

	2014	2013
Underwriting income		
Gross premiums written	\$ 19,031,253	\$ 19,089,337
Less reinsurance ceded	<u>2,845,903</u>	<u>4,117,410</u>
	16,185,350	14,971,927
Net premiums written		
Less increase (decrease) in unearned premiums	<u>(43,619)</u>	<u>30,095</u>
	16,228,969	14,941,832
Net premiums earned	16,228,969	14,941,832
Service charges	<u>248,474</u>	<u>244,521</u>
	16,477,443	15,186,353
Direct losses incurred		
Gross claims and adjustment expenses (Note 9)	7,644,564	14,592,164
Less reinsurers' share of claims and adjustment expenses	<u>(2,635,169)</u>	<u>4,030,272</u>
	10,279,733	10,561,892
	<u>6,197,710</u>	<u>4,624,461</u>
Expenses		
Fees, commissions and other acquisition expenses (Note 10)	3,145,093	3,014,452
Other operating and administrative expenses (Note 11)	<u>2,856,069</u>	<u>2,861,576</u>
	6,001,162	5,876,028
Net underwriting income (loss)	196,548	(1,251,567)
Investment and other income (Note 13)	<u>3,345,673</u>	<u>1,266,392</u>
	3,542,221	14,825
Income before income taxes		
Provision for income taxes (Note 8)	<u>551,383</u>	<u>(35,859)</u>
Net income and total comprehensive income for the year	<u>\$ 2,990,838</u>	<u>\$ 50,684</u>

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

Lambton Mutual Insurance Company
Statement of Policyholders' Surplus
For the Year Ended December 31, 2014

	Total
Balance at January 1, 2013	\$28,831,982
Net income and total comprehensive income for the year	<u>50,684</u>
Balance on December 31, 2013	28,882,666
Net income and total comprehensive income for the year	<u>2,990,838</u>
Balance on December 31, 2014	<u>\$31,873,504</u>

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

Lambton Mutual Insurance Company
Statement of Cash Flows
For the Year Ended December 31, 2014

	2014	2013
Operating activities		
Net income	\$ 2,990,838	\$ 50,684
Adjustments for:		
Depreciation (Note 9 and Note 11)	228,027	190,869
Unrealized (gain) loss on investments	(1,051,388)	389,542
Amortization of investments	134,313	154,490
Interest and dividend income	(1,784,475)	(1,135,814)
Provision for income taxes	551,383	(35,859)
Realized gain from disposal of investments	(615,973)	(294,122)
Loss on disposal of capital assets	4,402	770
	<u>(2,533,711)</u>	<u>(730,124)</u>
Changes in working capital		
Change in due from policyholders and reinsurers	4,225,342	(1,331,897)
Change in other assets	(18,006)	(17,095)
Change in accounts payable and accrued liabilities	22,765	(93,008)
	<u>4,230,101</u>	<u>(1,442,000)</u>
Changes in insurance contract related balances, provisions		
Change in deferred policy acquisition expenses	(8,743)	(18,454)
Change in unearned premiums	(43,619)	30,096
Change in provision for unpaid claims	(3,281,088)	2,709,750
	<u>(3,333,450)</u>	<u>2,721,392</u>
Cash flows related to interest, dividends and income taxes		
Interest and dividends received	1,737,043	1,156,093
Income taxes paid	285,630	(489,995)
	<u>2,022,673</u>	<u>666,098</u>
Total cash inflows from operating activities	<u>3,376,451</u>	<u>1,266,050</u>
Investing activities		
Sale of investments	6,052,521	24,192,081
Purchase of investments	(9,923,265)	(25,440,506)
Proceeds from sale of property plant & equipment	146,663	-
Purchase of property, plant & equipment and intangible assets	(39,477)	(176,051)
Total cash outflows from investing activities	<u>(3,763,558)</u>	<u>(1,424,476)</u>
Net decrease in cash and cash equivalents	<u>(387,107)</u>	<u>(158,426)</u>
Cash and cash equivalents, beginning of year	<u>2,560,491</u>	<u>2,718,917</u>
Cash and cash equivalents, end of year	<u>\$ 2,173,384</u>	<u>\$ 2,560,491</u>

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

Lambton Mutual Insurance Company

Notes to Financial Statements

December 31, 2014

1. Nature of operations and summary of significant accounting policies

Reporting entity

Lambton Mutual Insurance Company (the Company) is incorporated under the laws of Ontario, Canada 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 at 7873 Confederation Line, Watford, 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 mutual insurance companies by the Ontario Mutuals' Auto Rate Filing Committee. The rate filing must include actuarial justification for rate increases or decreases. All rate filings are approved or denied by the Financial Services Commission of Ontario. Rate regulation may affect the automobile revenues that are earned by the Company. The actual impact of rate regulation would depend on the competitive environment at the time.

These financial statements have been authorized for issue by the Board of Directors on January 28, 2015.

Basis of presentation

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

These financial statements were prepared under the historical cost convention, as modified by the revaluation of fair value through profit and loss of financial assets.

The Company's functional and presentation currency is the Canadian dollar.

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 disclosed in Note 2.

Lambton Mutual Insurance Company Notes to Financial Statements

December 31, 2014

1. Nature of operations and summary of significant accounting policies (continued)

Significant accounting policies

Insurance contracts

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

Balances arising from insurance contracts primarily include the following:

(a) Premiums and unearned premiums

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

The Company earns premium income evenly over the term of the insurance policy generally using the pro rata method. The portion of the premium related to the unexpired portion of the policy at the end of the fiscal year is reflected in unearned premiums.

(b) Deferred policy acquisition expenses

Acquisition costs are comprised of brokers' commissions. These costs are deferred and amortized over the terms of the related policies to the extent that they are considered to be recoverable from unearned premiums, after considering the related anticipated claims and expenses.

(c) Provisions for unpaid claims and adjustment expenses

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

Claim liabilities are carried on an undiscounted basis.

Lambton Mutual Insurance Company Notes to Financial Statements

December 31, 2014

1. Nature of operations and summary of significant accounting policies (continued)

(d) Liability adequacy test

At each reporting date the Company performs a liability adequacy test on its insurance liabilities less deferred policy acquisition expenses to ensure the carrying value is adequate, using current estimates of future cash flows, taking into account the relevant investment return. If that assessment shows that the carrying amount of the liabilities is inadequate, any deficiency is recognized as an expense to comprehensive income initially by writing off the deferred policy acquisition expense and subsequently by recognizing an additional claims liability for claims provisions.

(e) Reinsurers' share of provisions for unpaid claims and adjustment expenses

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

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.

(f) Salvage and subrogation recoverable

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

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

(g) Refund from premium

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

Lambton Mutual Insurance Company Notes to Financial Statements

December 31, 2014

1. Nature of operations and summary of significant accounting policies (continued)

Structured settlements, Fire Mutuals Guarantee Fund and financial guarantee contracts

The Company enters into annuity agreements with various life insurance companies to provide for fixed and recurring payments to claimants. Under such arrangements, the Company's liability to its claimants is substantially transferred, although the Company remains exposed to the credit risk if life insurers fail to fulfil their obligations.

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

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

Financial instruments

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

Loans and receivables

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

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

Lambton Mutual Insurance Company Notes to Financial Statements

December 31, 2014

1. Nature of operations and summary of significant accounting policies (continued)

Fair value through profit and loss

The Company does not have any instruments that are held-for-trading purposes; however, management has designated to voluntarily classify its investments as fair value through profit and loss. These instruments are carried at fair value with changes in fair value recognized in comprehensive income. Transaction costs on these instruments are expensed as incurred. Interest on debt securities classified as fair value through profit and loss is calculated using the effective interest rate method.

Other financial liabilities

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

Property, plant & equipment

Property, plant & 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 comprehensive income and is provided as follows:

Buildings	2.5% diminishing balance basis
Computer hardware	25% straight line basis
Equipment	10-20% diminishing balance basis
Vehicles	30% diminishing balance basis

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

Intangible assets

Intangible assets consist of computer software which are not integral to the computer hardware owned by the Company. Computer software is initially recorded at cost and subsequently measured at cost less accumulated depreciation. Computer software is depreciated on a straight-line basis over its estimated useful life of 4 years. Depreciation is taken in the year of acquisition using the half year rule. The depreciation expense is included in other operating and administrative expenses in the statement of comprehensive income.

Impairment of non-financial assets

Non-financial assets are subject to impairment tests whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. Where the carrying value of an asset exceeds its recoverable amount, which is the higher of value in use and fair value less costs to sell, the asset is written down accordingly.

Lambton Mutual Insurance Company Notes to Financial Statements

December 31, 2014

1. Nature of operations and summary of significant accounting policies (continued)

For the purpose of assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Where it is not possible to estimate the recoverable amount of an individual asset, the impairment test is carried out on the asset's cash-generating unit, which is the lowest group of assets in which the asset belongs for which there are separately identifiable cash flows.

Income taxes

Income tax expense is comprised of current and deferred tax. Current tax 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.

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

Deferred tax assets and liabilities are recognized where the carrying amount of an asset or liability differs from its tax base, except for taxable temporary differences arising on the initial recognition of goodwill and temporary differences arising on the initial recognition of an asset or liability in a transaction which is not a business combination and at the time of the transaction affects neither accounting nor taxable profit or loss.

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

The amount of the deferred tax asset or liability is measured at the amount expected to be recovered from or paid to the taxation authorities. This amount is determined using tax rates and tax laws that have been enacted or substantively enacted by the year-end date and are expected to apply when the liabilities / (assets) are settled / (recovered).

Pension plan

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

Provisions

Provisions are recognized for liabilities of uncertain timing or amounts that have arisen as a result of past transactions, including legal, equitable or constructive obligations. The provision is measured at the best estimate of the expenditure required to settle the obligation at the reporting date.

Lambton Mutual Insurance Company Notes to Financial Statements

December 31, 2014

1. Nature of operations and summary of significant accounting policies (continued)

New standards, interpretations and amendments effective from January 1, 2014

There are no new standards, interpretations and amendments, effective for the first time from January 1, 2014 that have had a material effect on the financial statements.

Standards, amendments and interpretations not yet effective

A new standard, amendment and interpretation has been published that is mandatory for the Company's accounting periods beginning on or after January 1, 2015 that the Company has decided not to early adopt. The standard, amendment and interpretation that will be relevant to the Company is:

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

IFRS 9 amends the requirements for classification and measurement of financial assets, impairment, and hedge accounting. IFRS 9 introduces an expected loss model of impairment and retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets; amortized cost, fair value through profit or loss, and fair value through other comprehensive income. 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. The Company is in the process of evaluating the impact of the new standard.

IAS 1 Presentation of Financial Statements

The amendments to IAS 1 are a part of a major initiative to improve disclosure requirements in IFRS financial statements. The amendments clarify the application of materiality to note disclosure and the presentation of line items in the primary statements provide options on the ordering of financial statements and additional guidance on the presentation of other comprehensive income related to equity accounted investments. The effective date for these amendments is January 1, 2016. The Company is in the process of evaluating the impact of these amendments.

IFRS 15 Revenue from Contracts with Customers

IFRS 15 is based on the core principle to recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. IFRS 15 focuses on the transfer of control. IFRS 15 replaces all of the revenue guidance that previously existed in IFRSs. The effective date for IFRS 15 is January 1, 2017. The Company is in the process of evaluating the impact of the new standard.

Lambton Mutual Insurance Company Notes to Financial Statements

December 31, 2014

2. Critical accounting estimates and judgments

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

The effect of a change in an accounting estimate is recognized prospectively by including it in comprehensive income in the period of the change.

The estimates and assumptions that have a significant risk of causing material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

Provision for unpaid claims

The estimation of the provision for unpaid claims and the related reinsurers' 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 experience and industry experience. More details are included in Note 6.

Income taxes

The Company periodically assesses its liabilities and contingencies related to income taxes for all years open to audit based on the latest information available. For matters where it is probable that an adjustment will be made, the Company records its best estimate of the tax liability including the related interest and penalties in the current tax provision. Management believes they have adequately provided for the probable outcome of these matters, however, the final outcome may result in a materially different outcome than the amount included in the tax liabilities.

Lambton Mutual Insurance Company

Notes to Financial Statements

December 31, 2014

3. Financial instrument classification

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

	Fair value through profit and loss	Loans and receivables	Other financial liabilities	Total
December 31, 2014				
Cash	\$ -	\$ 2,173,384	\$ -	\$ 2,173,384
Investments	48,534,446	-	-	48,534,446
Investment income accrued	-	167,242	-	167,242
Due from brokers and policyholders	-	3,647,579	-	3,647,579
Accounts payable and accrued liabilities	-	-	(384,211)	(384,211)
	<u>\$ 48,534,446</u>	<u>\$ 5,988,205</u>	<u>\$ (384,211)</u>	<u>\$ 54,138,440</u>
December 31, 2013				
Cash	\$ -	\$ 2,560,491	\$ -	\$ 2,560,491
Investments	43,130,654	-	-	43,130,654
Investment income accrued	-	119,810	-	119,810
Due from brokers and policyholders	-	3,671,121	-	3,671,121
Accounts payable and accrued liabilities	-	-	(361,446)	(361,446)
	<u>\$ 43,130,654</u>	<u>\$ 6,351,422</u>	<u>\$ (361,446)</u>	<u>\$ 49,120,630</u>

Lambton Mutual Insurance Company

Notes to Financial Statements

December 31, 2014

4. Investments

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

	December 31, 2014		December 31, 2013	
	Cost	Fair value	Cost	Fair value
Treasury bills	\$ 332,675	\$ 332,675	\$ 479,077	\$ 479,077
Bonds issued by				
Federal	-	-	2,256,166	2,275,251
Provincial	11,321,051	11,771,064	11,637,408	11,748,268
Corporate (A or better)	9,908,537	10,108,817	4,551,208	4,611,531
	<u>21,229,588</u>	<u>21,879,881</u>	<u>18,444,782</u>	<u>18,635,050</u>
Equity investments				
Canadian	<u>4,303,394</u>	<u>5,449,578</u>	<u>5,552,665</u>	<u>6,494,638</u>
Pooled funds				
ACM Mortgage one fund	502,601	506,689	-	-
Farm mutual Canadian fixed income	8,271,274	8,057,003	7,742,570	7,462,553
Lincluden Canadian equity	1,884,087	1,953,003	1,553,629	1,528,716
Lincluden fixed income	10,118,152	10,309,287	8,520,293	8,488,866
	<u>20,776,114</u>	<u>20,825,982</u>	<u>17,816,492</u>	<u>17,480,135</u>
Other investments				
Fire Mutuals guarantee fund	<u>45,956</u>	<u>46,330</u>	<u>42,308</u>	<u>41,754</u>
Total investments	<u>\$46,687,727</u>	<u>\$48,534,446</u>	<u>\$ 42,335,324</u>	<u>\$ 43,130,654</u>

Lambton Mutual Insurance Company

Notes to Financial Statements

December 31, 2014

4. Investments (continued)

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).

	Level 1	Level 2	Level 3	Total
December 31, 2014				
Treasury bills	\$ 332,675	\$ -	\$ -	\$ 332,675
Bonds	21,879,881	-	-	21,879,881
Equity investments	5,449,578	-	-	5,449,578
Pooled funds	-	20,825,982	-	20,825,982
Other investments	-	46,330	-	46,330
Total	\$27,662,134	\$20,872,312	\$ -	\$48,534,446
December 31, 2013				
Treasury bills	\$ 479,077	\$ -	\$ -	\$ 479,077
Bonds	18,635,050	-	-	18,635,050
Equity investments	6,494,638	-	-	6,494,638
Farm mutual pooled funds	-	17,480,135	-	17,480,135
Other investments	-	41,754	-	41,754
Total	\$ 25,608,765	\$ 17,521,889	\$ -	\$ 43,130,654

There were no transfers between Level 1 and Level 2 for the years ended December 31, 2013 and 2014.

Lambton Mutual Insurance Company
Notes to Financial Statements

December 31, 2014

4. Investments (continued)

Maturity profile of bonds held is as follows:

	Within 1 year	2 to 5 years	6 to 10 years	Over 10 years	Fair value
December 31, 2014	\$ -	\$10,021,787	\$11,858,094	\$ -	\$21,879,881
Percent of Total	- %	46 %	54 %	- %	
December 31, 2013	\$ 819,082	\$ 9,648,707	\$ 7,121,414	\$ 1,045,847	\$18,635,050
Percent of Total	4 %	52 %	38 %	6 %	

The effective interest rate of the bonds portfolio held is 4.07% and 4.27% at December 31, 2014 and 2013 respectively.

Lambton Mutual Insurance Company
Notes to Financial Statement

December 31, 2014

5. Property, plant & equipment and intangible assets

	Property, plant & equipment						Intangible assets
	Land	Buildings	Computer hardware	Equipment	Vehicles	Total	Computer software
Cost							
Balance - December 31, 2013	\$ 320,734	\$ 1,194,868	\$ 298,956	\$ 420,197	\$ 110,973	\$ 2,345,728	\$ 560,321
Additions	-	-	3,945	1,632	33,900	39,477	-
Disposals	(40,000)	(126,201)	(15,264)	(2,361)	(25,977)	(209,803)	(3,959)
Balance - December 31, 2014	\$ 280,734	\$ 1,068,667	\$ 287,637	\$ 419,468	\$ 118,896	\$ 2,175,402	\$ 556,362
Accumulated depreciation							
Balance - December 31, 2013	\$ -	\$ 479,920	\$ 175,517	\$ 352,344	\$ 73,052	\$ 1,080,833	\$ 187,165
Depreciation expense	-	16,767	53,449	10,435	15,785	96,436	131,591
Disposals	-	(20,730)	(15,264)	(1,273)	(21,471)	(58,738)	(3,959)
Balance - December 31, 2014	\$ -	\$ 475,957	\$ 213,702	\$ 361,506	\$ 67,366	\$ 1,118,531	\$ 314,797
Net book value							
December 31, 2013	\$ 320,734	\$ 714,948	\$ 123,439	\$ 67,853	\$ 37,921	\$ 1,264,895	\$ 373,156
December 31, 2014	\$ 280,734	\$ 592,710	\$ 73,935	\$ 57,962	\$ 51,530	\$ 1,056,871	\$ 241,565

Lambton Mutual Insurance Company
Notes to Financial Statements

December 31, 2014

6. Insurance contracts

Due from reinsurers	2014	2013
Balance, beginning of the year	\$ 489,535	\$ -
Submitted to reinsurer	1,077,096	3,182,123
Received from reinsurer	(1,566,631)	(2,692,588)
Balance, end of the year	\$ -	\$ 489,535
Expected settlement		
Within one year	\$ -	\$ 489,535

Reinsurers' share of provision for unpaid claims	2014	2013
Balance, beginning of the year	\$11,518,863	\$ 10,670,714
New claims reserve	1,690,713	4,286,002
Change in prior years' reserve	(4,325,882)	(255,730)
Submitted to reinsurer	(1,077,096)	(3,182,123)
Balance, end of the year	\$ 7,806,598	\$ 11,518,863
Expected settlement		
Within one year	\$ 1,934,412	\$ 4,056,167
More than one year	\$ 5,872,186	\$ 7,462,696

Lambton Mutual Insurance Company
Notes to Financial Statements

December 31, 2014

6. Insurance contracts (continued)

Deferred policy acquisition expenses	2014	2013
Balance, beginning of the year	\$ 1,426,267	\$ 1,407,813
Acquisition costs incurred	3,153,836	3,032,906
Expensed during the year	(3,145,093)	(3,014,452)
Balance, end of the year	<u>\$ 1,435,010</u>	<u>\$ 1,426,267</u>

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

Unearned premiums	2014	2013
Balance, beginning of the year	\$ 9,337,849	\$ 9,307,753
Premiums written	19,031,253	19,089,337
Premiums earned during year	(19,074,872)	(19,059,241)
Balance, end of the year	<u>\$ 9,294,230</u>	<u>\$ 9,337,849</u>

Lambton Mutual Insurance Company
Notes to Financial Statement

December 31, 2014

6. Insurance contracts (continued)

The following is a summary of the insurance contract provisions and related reinsurance assets at December 31.

	December 31, 2014			December 31, 2013		
	Gross	Re- insurance	Net	Gross	Re- insurance	Net
Outstanding claims provision						
Long term	\$13,649,553	\$ 4,640,949	\$ 9,008,604	\$ 12,329,283	\$ 3,352,179	\$ 8,977,104
Short term	3,357,687	909,917	2,447,770	4,381,508	1,928,684	2,452,824
Facility Association and other residual pools	355,490	-	355,490	390,203	-	390,203
	17,362,730	5,550,866	11,811,864	17,100,994	5,280,863	11,820,131
Provision for claims incurred but not reported	5,765,712	2,255,732	3,509,980	9,308,536	6,238,000	3,070,536
	\$23,128,442	\$ 7,806,598	\$15,321,844	\$ 26,409,530	\$ 11,518,863	\$ 14,890,667

Lambton Mutual Insurance Company

Notes to Financial Statements

December 31, 2014

6. Insurance contracts (continued)

Comments and assumptions for specific claims categories

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

Claims and adjustment expenses

Changes in claim liabilities recorded in the balance sheet for the years ended December 31, 2014 and 2013 and their impact on claims and adjustment expenses for the two years is as follows:

	2014	2013
Unpaid claim liabilities - beginning of year - net of reinsurance	\$ 14,890,667	\$ 13,029,066
Decrease in estimated losses and expenses, for losses occurring in prior years	(4,865,066)	(3,040,529)
Provision for losses and expenses on claims occurring in the current year	15,144,798	13,602,424
Payment on claims:		
Current year	(6,490,348)	(6,123,543)
Prior years	(3,358,207)	(2,576,751)
Unpaid claims - end of year - net	15,321,844	14,890,667
Reinsurers' share and subrogation recoverable	7,806,598	11,518,863
Provision for unpaid claims, end of year	\$ 23,128,442	\$ 26,409,530

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

Lambton Mutual Insurance Company Notes to Financial Statements

December 31, 2014

6. Insurance contracts (continued)

Provision for unpaid claims and adjustment expenses

The determination of the provision for unpaid claims and adjustment expenses and the related reinsurers' share requires the estimation of two major variables which are the development of claims and reinsurance recoveries.

Claim development

The estimation of claim development involves assessing the future behaviour of claims, review of previous legal settlements, the amount of information available, the characteristics of the line of business from which the claim arises and historical delays in reporting claims. In general, the longer the term required for the settlement of a group of claims the more variable the estimates. Short settlement term claims are those which are expected to be substantially paid within a year of being reported.

The tables that follow present the development of claims payments and the estimated ultimate cost of claims for the claim year 2007 to 2014. The table on page 24 shows the cumulative amounts paid or estimated to be paid during successive years related to each claim year. The original estimates will be increased or decreased, as more information becomes known about the original claims and overall claim frequency and severity.

In 2011, the year of adoption of IFRS, only information from periods beginning on or after January 1, 2007 was required to be disclosed. This is being increased each additional year, until ten years of information is included.

Reinsurance recoveries

Reinsurance recoveries are measured using the amounts and assumptions associated with the underlying insurance contracts and in accordance with the terms of each reinsurance contract.

Lambton Mutual Insurance Company
Notes to Financial Statement

December 31, 2014

6. Insurance contracts (continued)

Gross claims	2007	2008	2009	2010	2011	2012	2013	2014	Total
Gross estimate of cumulative claims cost									
At the end year of claim \$	13,027,825	\$ 10,928,908	\$ 12,004,842	\$ 15,709,070	\$ 14,359,963	\$ 16,256,300	\$ 17,888,427	\$ 16,839,510	
One year later	13,072,908	11,466,349	10,288,967	13,363,489	12,557,183	14,148,115	13,437,360		
Two years later	13,826,870	11,847,720	10,139,036	12,329,693	12,957,338	12,596,327			
Three years later	14,100,101	12,071,914	9,488,599	12,229,445	12,513,395				
Four years later	14,110,265	11,866,950	9,484,060	11,518,159					
Five years later	14,198,456	11,192,311	8,914,484						
Six years later	13,920,018	10,349,673							
Seven years later	13,478,497								
Current estimate of cumulative claims cost	13,478,497	10,349,673	8,914,484	11,518,159	12,513,395	12,596,327	13,437,360	16,839,510	99,647,405
Cumulative payments	12,814,203	10,159,472	8,529,782	10,933,588	9,350,274	9,126,601	9,162,021	6,492,775	76,568,716
Outstanding claims	\$ 664,294	\$ 190,201	\$ 384,702	\$ 584,571	\$ 3,163,121	\$ 3,469,726	\$ 4,275,339	\$ 10,346,735	\$ 23,078,689
Outstanding claims 2006 and prior									49,753
Claims handling expense									(2,518,493)
Total gross outstanding claims net of claims handling expense									<u>\$ 20,609,949</u>

Lambton Mutual Insurance Company
Notes to Financial Statement

December 31, 2014

6. Insurance contracts (continued)

Net of Reinsurance	2007	2008	2009	2010	2011	2012	2013	2014	Total
Net estimate of cumulative claims cost									
At the end year of claim \$	9,105,768 \$	9,792,297 \$	10,449,117 \$	11,892,869 \$	12,463,116 \$	12,212,971 \$	13,602,427 \$	15,148,797	
One year later	8,730,734	9,208,699	8,339,267	10,258,937	10,237,307	9,977,459	10,809,137		
Two years later	8,752,074	8,955,635	8,183,921	9,825,672	9,961,824	8,999,933			
Three years later	8,462,727	8,703,022	7,809,538	9,767,038	9,561,403				
Four years later	8,366,344	8,661,496	7,741,922	9,564,301					
Five years later	8,283,151	8,387,574	7,567,551						
Six years later	8,214,752	8,186,022							
Seven years later	8,132,821								
Current estimate of cumulative claims cost									
	8,132,821	8,186,022	7,567,551	9,564,301	9,561,403	8,999,933	10,809,137	15,148,797	77,969,965
Cumulative payments	8,006,666	8,088,107	7,427,672	9,356,273	8,169,702	7,093,312	8,064,295	6,490,347	62,696,374
Outstanding claims	\$ 126,155	\$ 97,915	\$ 139,879	\$ 208,028	\$ 1,391,701	\$ 1,906,621	\$ 2,744,842	\$ 8,658,450	\$ 15,273,591
Outstanding claims 2006 and prior									48,253
Claims handling expense									(1,998,482)
Total net outstanding claims and claims handling									<u>\$13,323,362</u>

Lambton Mutual Insurance Company Notes to Financial Statements

December 31, 2014

7. Pension Plan

The Company makes contributions on behalf of its employees to "The Retirement Annuity Plan for Employees of the Ontario Mutual Insurance Association and Member Companies". This pension plan is being accounted for as a multi-employer pension plan as defined by IAS 19 Employee Benefits. Each member company has signed an Ontario Mutual Insurance Association Pension Plan Agreement. Eligible employees participate in the defined benefit plan. The defined benefit plan specifies the amount of the retirement benefit to be received by the employee based on the number of years the employee has contributed and his/her final average earnings. The plan is accounted for as a defined contribution plan as insufficient information is available to account for the plan as a defined benefit plan. The Company is one of a number of employers that participates in the plans and the financial information provided to the Company on the basis of the contractual agreements is insufficient to reliably measure the Company's proportionate share in the plan assets and liabilities on defined benefit accounting requirements.

The Company matches the employee contributions and funds the excess defined benefit based on the Company's percentage of pensionable earnings as calculated by the Pension Plan actuaries. The Pension Plan agreement states that the Company is responsible for its share of any deficit as a result of any actuarial valuation or cost certificate. The minimum funding requirement is the solvency valuation amount determined by the Pension Plan actuary on the valuation dates prescribed by the Pension Benefit Act. In the event of a wind-up, voluntary withdrawal or bankruptcy, either by the Company or the group as a whole, the Company is responsible for its portion of all expenses and deficit related to such. According to the most recent actuarial valuation dated December 31, 2013, the going concern valuation for the defined benefit plan shows a surplus. The next pension valuation is scheduled for December 31, 2016.

The defined benefit plan has been closed to future eligible employees effective September 1, 2013. The Company and all current employees who are accruing benefits under the defined benefit plan continue to contribute to the defined benefit plan according to the existing terms of the agreement. Future eligible employees will be enrolled in the defined contribution plan. The Company's obligation with respect to this plan is to make specified monthly contributions based on a percentage of the employee's eligible earnings.

The amount contributed to the plans for 2014 was \$180,875 (2013 - \$131,755). The contributions were made for current service and these have been recognized in comprehensive income. Additional lump sum payments for 2014 were \$Nil (2013 - \$267,898).

The Company had a 3.22% (2013 - 3.28%) share of the total contributions to the defined benefit plan in 2014.

The expected contributions to the plans by the Company for 2015 are \$199,065.

Lambton Mutual Insurance Company

Notes to Financial Statements

December 31, 2014

8. Income taxes

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

The significant components of tax expense included in net income are composed of:

	2014	2013
Current tax provision		
Based on current year taxable income (loss)	\$ 633,899	\$ (23,859)
Adjustments for over / under provision in prior periods	(46,516)	-
	<u>587,383</u>	<u>(23,859)</u>
Deferred tax expense		
Origination and reversal of temporary differences	(36,000)	(12,000)
	<u>(36,000)</u>	<u>(12,000)</u>
Total income tax expense	<u>\$ 551,383</u>	<u>\$ (35,859)</u>

Reasons for the difference between current income tax expense for the year and the expected income taxes based on the statutory tax rate of 26.5% (2013 - 21%) are as follows:

	2014	2013
Income before income taxes	\$ 3,542,221	\$ 14,825
Expected taxes based on the statutory rate of 26.5% (2013 - 21%)	\$ 938,689	\$ 3,113
Income from insuring farm-related risks	(295,511)	-
Non-deductible portion of claims liabilities	5,713	19,547
Other non-deductible expenses	2,551	937
Adjustments related to investments	(49,660)	(31,395)
Difference between amortization and CCA	28,620	(16,870)
Recovery of prior year taxes due to difference in rates	-	809
Recapture on sale of capital assets	3,497	-
	<u>633,899</u>	<u>(23,859)</u>
Total current income tax expense	<u>\$ 633,899</u>	<u>\$ (23,859)</u>

Lambton Mutual Insurance Company
Notes to Financial Statement

December 31, 2014

8. Income taxes (continued)

The movement in 2014 deferred tax liabilities and assets are:

	Opening balance at Jan 1, 2014	Recognized in comprehensive income	Closing Balance at Dec 31, 2014
<hr/>			
2014			
Deferred tax assets			
Claims liabilities	\$ 156,000	\$ 5,000	\$ 161,000
<hr/>			
Deferred tax liabilities			
Property, plant & equipment	\$ 136,000	\$ (25,000)	\$ 111,000
Adjustments related to investments	7,000	(6,000)	1,000
<hr/>			
Deferred tax liability	\$ 143,000	\$ (31,000)	\$ 112,000
<hr/>			
2014 Net deferred tax asset movement	\$ 13,000	\$ 36,000	\$ 49,000
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Lambton Mutual Insurance Company
Notes to Financial Statement

December 31, 2014

8. Income taxes (continued)

The movement in 2013 deferred tax liabilities and assets are:

	Opening balance at Jan 1, 2013	Recognized in comprehensive income	Closing Balance at Dec 31, 2013
<hr/>			
2013			
Deferred tax assets			
Claims liabilities	\$ 137,000	\$ 19,000	\$ 156,000
<hr/>			
Deferred tax liabilities			
Property, plant & equipment	\$ 120,000	\$ 16,000	\$ 136,000
Adjustments related to investments	16,000	(9,000)	7,000
<hr/>			
Deferred tax liability	\$ 136,000	\$ 7,000	\$ 143,000
<hr/>			
2013 Net deferred tax asset movement	\$ 1,000	\$ 12,000	\$ 13,000
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Lambton Mutual Insurance Company

Notes to Financial Statements

December 31, 2014

9. Gross claims and adjustment expenses

Included in claims expenses were wage costs of \$835,222 (2013 - \$766,631) and depreciation of \$15,785 (2013 - \$16,248).

10. Fees, commissions and other acquisition expenses

	2014	2013
Commissions	\$ 3,145,093	\$ 3,014,452

11. Other operating and administrative expenses

	2014	2013
Computer costs	\$ 431,659	\$ 372,008
Licenses, fees and dues	189,692	184,765
Depreciation	212,242	174,621
Education, travel and meals	131,218	111,452
Office premises	130,756	127,280
Postage and office supplies	138,906	155,708
Professional fees	63,070	72,371
Salaries, benefits and directors fees	1,300,414	1,379,950
Other	258,112	283,421
	<u>\$ 2,856,069</u>	<u>\$ 2,861,576</u>

12. Salaries, benefits, commissions and directors fees

	2014	2013
Claims salaries and benefits (Note 9)	\$ 835,222	\$ 766,631
Commissions (Note 10)	3,145,093	3,014,452
Other salaries, benefits and directors fees (Note 11)	1,300,414	1,379,950
	<u>\$ 5,280,729</u>	<u>\$ 5,161,033</u>

Lambton Mutual Insurance Company

Notes to Financial Statements

December 31, 2014

13. Investment and other income

	2014	2013
Interest income	\$ 1,472,119	\$ 892,448
Dividend income	312,356	243,366
Realized gains on disposal of investments	615,973	294,122
Investment expenses	(102,008)	(85,748)
Unrealized gains (losses) on investments	1,051,388	(389,542)
Miscellaneous	(4,155)	11,424
FMRP premium refund	-	300,322
	<u>\$ 3,345,673</u>	<u>\$ 1,266,392</u>

14. Related party transactions

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

	2014	2013
Compensation		
Salaries, short term employee benefits and director's fees	\$ 537,872	\$ 512,661
Pension	61,337	38,151
	<u>\$ 599,209</u>	<u>\$ 550,812</u>
Premiums	<u>\$ 74,925</u>	<u>\$ 80,339</u>
Claims paid	<u>\$ 29,102</u>	<u>\$ 14,399</u>

Amounts owing to key management personnel at December 31, 2014 are \$nil (2013 - \$nil).

Lambton Mutual Insurance Company Notes to Financial Statements

December 31, 2014

15. Capital management

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

The regulators measure the financial strength of property and casualty insurers using a minimum capital test (MCT). The regulators generally expect property and casualty companies to comply with capital adequacy requirements. This test compares a company's capital against the risk profile of the organization. The risk-based capital adequacy framework assesses the risk of assets, policy liabilities and other exposures by applying various factors. The regulator indicates that the Company should produce a minimum MCT of 150%. During the year, the Company has consistently exceeded this minimum. The regulator has the authority to request more extensive reporting and can place restrictions on the Company's operations if the Company falls below this requirement as deemed necessary.

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

16. Financial instrument and Insurance risk management

Insurance risk management

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

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

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

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

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

Lambton Mutual Insurance Company

Notes to Financial Statements

December 31, 2014

16. Financial instrument and Insurance risk management (continued)

The Company manages this risk via its underwriting and reinsurance strategy within an overall risk management framework. Exposures are limited by having documented underwriting limits and criteria. Pricing of property and liability policies are based on assumptions in regard to trends and past experience, in an attempt to correctly match policy revenue with exposed risk. Automobile premiums are subject to approval by the Financial Services Commission of Ontario and therefore may result in a delay in adjusting the pricing to exposed risk. Reinsurance is purchased to mitigate the effect of the potential loss to the Company. Reinsurance is placed with Farm Mutual Reinsurance Plan Inc. (FMRP), a Canadian registered reinsurer.

The company follows the policy of underwriting and reinsuring contracts of insurance which, for 2014 claims, limited the liability of the company to a maximum amount on any one property claim to \$250,000. The maximum liability to the company for each auto claim is limited to the amount of \$500,000, and for each liability claim to the amount of \$400,000.

Additionally the company carries reinsurance with an upper limit of \$750,000 to protect itself against certain catastrophic losses. In addition, the company has obtained stop loss reinsurance which limits the liability of all claims in a specific year to 80% of gross net earned premiums for all lines of business combined.

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, 2014 and 2013.

The risks associated with insurance contracts are complex and subject to a number of variables which complicate quantitative sensitivity analysis. The Company's various techniques are based on past claims development experience to quantify these sensitivities. This includes indicators such as average claim cost, amount of claims occurrence, expected loss ratios and claims development as described in Note 6.

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

	Property claims		Auto claims		Liability claims	
	2014	2013	2014	2013	2014	2013
5% increase in loss ratios						
Gross	\$ 406,636	\$ 389,348	\$ 472,325	\$ 490,121	\$ 74,783	\$ 73,493
Net	\$ 345,480	\$ 325,289	\$ 408,388	\$ 377,554	\$ 57,581	\$ 44,249
5% decrease in loss ratios						
Gross	\$ (406,636)	\$ (389,348)	\$ (472,325)	\$ (490,121)	\$ (74,783)	\$ (73,493)
Net	\$ (345,480)	\$ (325,289)	\$ (408,388)	\$ (377,554)	\$ (57,581)	\$ (44,249)

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.

Lambton Mutual Insurance Company

Notes to Financial Statements

December 31, 2014

16. Financial instrument and Insurance risk management (continued)

Credit risk

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

The Company's bond 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 100% (December 31, 2013 - 100%) of bonds rated A or better. The Company's bond investment policy limits investment in bonds and debentures of the various ratings to limits ranging from 65% to 90% of the Company's portfolio. Funds should 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.

Reinsurance is placed with Farm Mutual Reinsurance Plan Inc. (FMRP), 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.

Accounts receivable 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.

The maximum exposure to investment credit risk is outlined in Note 4.

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.

Market risk

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

The Company's bond and equity investment policy operates within the guidelines of the Insurance Act. A bond and equity 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.

Lambton Mutual Insurance Company Notes to Financial Statements

December 31, 2014

16. Financial instrument and Insurance risk management (continued)

Currency risk

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

The Company's foreign exchange risk is related to stock holdings which are limited to United States equities in sectors which are not readily available in Canada. The Company limits its holdings in foreign equity to 2% of the total investment portfolio in accordance with its bond and equity investment policy. Foreign currency changes are monitored by the Investment Committee and holdings are adjusted when offside of the investment policy. At year end, there were no foreign currency investments held in the portfolio.

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.

Interest rate risk

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

The Company is exposed to this risk through its interest bearing investments (bankers acceptance, treasury bills, guaranteed investment certificates, and bonds).

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

At December 31, 2014, a 1% move in interest rates, with all other variables held constant, could impact the market value of bonds by \$1,060,518 (2013 - \$856,840). Also, a 1% move in interest rates, with all other variables held constant, could impact the market value of the fixed income pooled fund by \$961,805 (2013 - \$864,135). These changes would be recognized in net income.

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.

Lambton Mutual Insurance Company Notes to Financial Statements

December 31, 2014

16. Financial instrument and Insurance risk management (continued)

Equity risk

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

The Company's portfolio includes Canadian stocks with fair values that move with the Toronto Stock Exchange Composite Index. At December 31, 2014, a 10% movement in the stock markets with all other variables held constant would have an estimated effect on the fair values of the Company's Canadian common equities of \$544,958 (2013 - \$649,464) and the equity pooled fund of \$195,300 (2013 - \$152,872). This change would be recognized in comprehensive income.

The Company's equity investment policy limits investment in preferred and common shares to a maximum of 25% of the market value of the portfolio.

Equities are monitored by the Board of Directors and holdings are adjusted following each quarter when the investments are offside of the investment policy.

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet all cash outflow obligations as they come due. The Company mitigates this risk by monitoring cash activities and expected outflows. The Company's current liabilities arise as claims are made. The Company does not have material liabilities that can be called unexpectedly at the demand of a lender or client. 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 bond and equity investment policy limits holdings in cash and short-term investments to a maximum of 20%. Short-term investments include treasury bills, commercial paper and term deposits with an original maturity of less than one year.

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.