Unaudited Condensed Consolidated Interim Financial Statements of

EGI FINANCIAL HOLDINGS INC.

For the quarters ended March 31, 2014 and 2013

EGI Financial Holdings Inc.
Consolidated Balance Sheets
(Unaudited, in thousands of Canadian dollars)

	Note	March 31 2014	December 31 2013
Assets			
Cash and short–term deposits		40,929	18,156
Accounts receivable		41,654	35,926
Investments	6	447,397	454,317
Due from insurance companies		1,321	3,086
Deferred policy acquisition costs		35,896	32,608
Income taxes recoverable		2,337	3,770
Prepaid expenses and other assets		4,623	5,105
Reinsurers' share – unearned premiums		24,002	19,985
– provision for unpaid claims	7	33,595	32,762
Property and equipment		788	755
Intangible assets	9	8,199	5,360
Deferred income taxes		6,529	6,273
		647,270	618,103
Liabilities			
Income taxes payable		-	187
Accounts payable and accrued liabilities		22,902	17,079
Payable to insurance companies		4,431	4,731
Unearned premiums		135,970	127,247
Unearned commission		4,656	3,623
Provision for unpaid claims	7	302,769	296,857
		470,728	449,724
Equity			
Share capital		67,660	67,211
Contributed surplus		1,825	1,561
Retained earnings		95,589	94,593
Accumulated other comprehensive income	13	10,394	7,170
Equity attributed to shareholders of the Company		175,468	170,535
Non–controlling interest		1,074	(2,156)
Total equity		176,542	168,379
Total liabilities and equity		647,270	618,103

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

EGI FINANCIAL HOLDINGS INC.
Consolidated Statements of Income and Comprehensive Income
(Unaudited, in thousands of Canadian dollars)

	Note	3 months ended March 31, 2014	3 months ended March 31, 2013
Revenue			
Gross written and assumed premiums		79,768	53,240
Less: Premiums ceded to reinsurers		(14,603)	(8,034)
Net written and assumed premiums		65,165	45,206
(Increase) decrease in gross unearned premiums		(6,450)	(2,388)
Increase (decrease) in unearned premiums, reinsurers' share		3,383	1,748
Change in provision for unearned premiums		(3,067)	(640)
Net earned premiums		62,098	44,566
Investment income	6	6,134	5,088
Total revenue		68,232	49,654
Expenses			
Gross claims incurred		40,482	35,552
Less: claims recoveries from reinsurers		(4,746)	(3,528)
Net incurred claims		35,736	32,024
Gross acquisition costs		21,164	13,453
Less: acquisition cost recoveries from reinsurers		(3,065)	(2,604)
Net acquisition costs		18,099	10,849
Operating costs		7,731	5,208
Total expenses		61,566	48,081
Income before taxes and discount rate impact on claims		6,666	1,573
Impact of change in discount rate on claims	7		(1,759)
Income (loss) before income taxes		6,666	(186)
Income tax expense	11	(1,271)	(216)
Net income (loss) on continuing operations		5,395	30
Net loss on discontinued operations attributable to shareholders of the Company		-	(940)
Net income		5,395	(910)
Attributed to:			
Shareholders of the Company		5,295	(821)
Non–controlling interest		100	(89)
Net Income		5,395	(910)
Earnings per share attributable to shareholders of the Company	14		
Net income per share continuing operations – basic		$0.45	$0.01
Net income per share – basic		$0.45	($0.07)
Net income per share continuing operations – diluted		$0.44	$0.01
Net income per share – diluted		$0.44	($0.07)
Net income		5,395	(910)
Other comprehensive income (loss), net of taxes that may be classified subsequently to net income			
Available-for-sale investments:			
Change in net unrealized gains		5,568	3,314
Reclassification of net realized (gains) losses to net income		(1,869)	(1,234)
Cumulative translation gain (loss)		514	203
Tax impact		(989)	(282)
Other comprehensive income (loss)		3,224	2,001
Total comprehensive income		8,619	1,091
Attributed to:			
Shareholders of the Company		8,519	1,180
Non-controlling interest		100	(89)
Total comprehensive income		8,619	1,091

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

EGI FINANCIAL HOLDINGS INC.
Consolidated Statements of Changes in Equity
(Unaudited, in thousands of Canadian dollars)

	Share Capital	Contributed Surplus	Accumulated Other Comprehensive Income	Retained Earnings	Shareholders' Equity	Non–controlling interest	Total Equity
Balance at January 1, 2014	67,211	1,561	7,170	94,593	170,535	(2,156)	168,379
Net income (loss)	–	–	–	5,295	5,295	100	5,395
Other comprehensive income (loss)	–	–	3,224	–	3,224	–	3,224
Total comprehensive income (loss)	–	–	3,224	5,295	8,519	100	8,619
Common shares repurchased	–	–	–	–	–	–	–
Dividends Paid	–	–	–	(1,169)	(1,169)	–	(1,169)
Investment in subsidiary	–	–	–	(3,130)	(3,130)	3,130	–
Common shares issued on stock options exercised	449	–	–	–	449	–	449
Stock options – expense	–	264	–	–	264	–	264
Balance at March 31, 2014	67,660	1,825	10,394	95,589	175,468	1,074	176,542

	Share Capital	Contributed Surplus	Accumulated Other Comprehensive Income	Retained Earnings	Shareholders' Equity	Non–controlling interest	Total Equity
Balance at January 1, 2013	68,244	1,068	6,054	91,237	166,603	(1,200)	165,403
Net income (loss)	–	–	–	(821)	(821)	(89)	(910)
Other comprehensive income (loss)	–	–	2,001	–	2,001	–	2,001
Total comprehensive income (loss)	–	–	2,001	(821)	1,180	(89)	1,091
Common shares repurchased	(158)	–	–	(132)	(290)	–	(290)
Common shares issued on stock options exercised	28	–	–	–	28	–	28
Stock options – expense	–	115	–	–	115	–	1,153
Balance at March 31, 2013	68,114	1,183	8,055	90,284	167,636	(1,289)	166,347

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

EGI FINANCIAL HOLDINGS INC.
Consolidated Statements of Cash Flows
(Unaudited, in thousands of Canadian dollars)

	3 months ended March 31, 2014	3 months ended March 31, 2013
Cash provided by (used in):		
Operating activities		
Net income from continuing operations	5,395	30
Net income from discontinued operations	-	(940)
adjusted for:		
Reinsurers' share of unearned premiums	(4,017)	(1,708)
Reinsurers' share of unpaid claims	(833)	(13)
Provision for unpaid claims	5,912	6,441
Unearned premiums	8,723	2,446
Deferred income taxes	(256)	(252)
Unearned commissions	1,033	141
Deferred policy acquisition costs	(3,288)	(707)
Amortization on property plant equipment and intangible assets	1,172	617
Amortization of premiums on bonds	669	652
Fair value change on FVTPL investments	(552)	(291)
Options expense	264	99
Currency translation	514	203
Prepaid expenses & other assets	482	109
Other	-	(65)
	9,823	7,672
Cash flow from changes in		
Accounts receivable	(5,728)	(3,276)
Net realized (gains) losses	(1,663)	(1,305)
Income taxes payable/recoverable	257	(3,523)
Due to insurance companies	1,465	(2,368)
Other liabilities	5,823	(290)
Cash provided by continuing operating activities	15,372	(4,000)
Financing activities		
Issue of common shares from stock options exercised	449	44
Common share dividends	(1,169)	-
Share repurchase	-	(290)
Cash provided by (used in) financing activities	(720)	(246)
Investing activities		
Purchases of property, equipment and intangible assets	(4,044)	(560)
Purchase of investments	(223,532)	(126,588)
Sale/maturity of investments	235,697	120,922
Cash (used in) investing activities	8,121	(6,226)
Increase in cash and short-term deposits	22,773	(10,472)
Cash and short-term deposits, beginning of year	18,156	19,578
Cash and short-term deposits, end of year	40,929	9,106
Supplementary information		
Operating activities		
Income taxes paid	529	2,834

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

1 Organization and basis of presentation

EGI Financial Holdings Inc. (the Company) was incorporated on August 18, 1997, under the Business Corporations Act (Ontario) and is incorporated and domiciled in Canada. The Company is principally engaged, through its subsidiaries, in property and casualty insurance in Canada and Europe. The Company's head office is located at 2680 Matheson Blvd. East, Suite 300, Mississauga, Ontario.

The Company's wholly-owned subsidiaries are EGI Insurance Managers Inc., Echelon General Insurance Company (Echelon), CIM Reinsurance Company Ltd. (CIM Re) and CUISA Managing General Agency Corporation ("CUISA MGA"). The Company also owns all of the preferred shares plus 71.1% of common shares of QIC Holdings ApS (QIC), which owns 100% of Qudos Insurance A/S (Qudos).

2 Basis of preparation

These condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) applicable to the preparation of interim financial statements, including IAS 34, Interim Financial Reporting. The condensed consolidated interim financial statements should be read in conjunction with the annual financial statements for the year ended December 31, 2013, which have been prepared in accordance with IFRS.

These consolidated financial statements have been authorized for issue by the Board of Directors, on May 8, 2014.

Prior period figures have been reclassified to conform to the current period presentation.

3 Summary of significant accounting policies

The accounting policies adopted are consistent with those of the previous financial year end and the Company has consistently applied the same accounting policies through all periods presented except as described below.

Income taxes

Taxes on income in the interim periods are accrued using the estimated annual tax rate that would be applicable to expected total annual income.

IFRIC 21 - Levies

IFRIC 21 provides guidance on when a Company should recognise a liability for a levy imposed by a government, other than those levies within the scope of other standards such as income taxes and fines or penalties imposed for breaches of legislation. A liability to pay levies is recognised when an obligating event takes place, such as the generation of revenue in the current period. There is no obligating event where a levy is triggered in a future period and an entity is economically compelled to continue to operate in the future period or the financial statements are prepared on a going concern basis suggesting that the entity will continue to operate in the future period. If the obligating event occurs over a period of time, the liability is recognised progressively; if the obligating event is reaching a minimum threshold, the liability is recognised when the minimum threshold is met.

(Unaudited, in thousands of Canadian dollars, except per share amounts)

Retrospective adoption of the interpretation on January 1, 2014 did not have a significant impact on the consolidated financial statements.

4 Critical accounting estimates and assumptions

The preparation of the Company's condensed consolidated interim financial statements requires management to use estimates and judgements that affect the amounts reported in the financial statements. These estimates and judgements principally relate to the establishment of reserves for claims and expenses, impairments of investment securities, amounts recoverable from reinsurers and income taxes. As more information becomes known, these estimates and judgements could change and impact future results.

In preparing these condensed consolidated interim financial statements, the significant judgements made by management in applying accounting policies and the key sources of estimation uncertainty were the same as those applied to the annual 2013 consolidated financial statements.

5 Seasonality

The P&C insurance business is seasonal in nature. While net earned premiums are generally stable from quarter to quarter, net underwriting income is driven mainly by weather conditions which may vary significantly by quarter.

6 Investments

The investment policies adopted are consistent with those of the previous financial year end and the Company has consistently applied the same investment policies through all periods presented.

	Carrying and fair values	
Available-for-sale	**As at March 31, 2014**	**As at December 31, 2013**
Fixed income		
Canadian		
Federal	60,738	54,374
Provincial	39,133	42,718
Municipal	4,721	5,714
Corporate	169,252	162,316
	273,844	265,122
Fixed income lent through securities lending program		
Federal	11,463	49,165
Provincial	18,798	7,656
Municipal	-	411
Corporate	3,640	3,980
	33,901	61,212
Foreign fixed income		
Government	15,263	12,799
Corporate	57,745	45,608
	73,008	58,407
Total fixed income	380,753	384,741

(Unaudited, in thousands of Canadian dollars, except per share amounts)

	Carrying and fair values	
Available-for-sale	**As at March 31, 2014**	**As at December 31, 2013**
Commercial Mortgages pooled fund	2,075	2,052
Common shares		
Canadian	9,885	13,491
Foreign	20,955	24,693
	30,840	38,184
Total available-for-sale	413,668	424,977
Fair value through profit or loss		
Preferred shares	33,297	29,340
Preferred shares lent through securities lending program	432	-
Total Preferred Shares	33,729	29,340
Total investments	447,397	454,317

In accordance with the securities lending agreement, the amount of the collateral must be at least 105% of the fair value of the securities loaned. As at March 31, 2014 the company had collateral of $38,386 (2013 - $nil) for the loaned securities, which is in excess of 105% of the fair value of the loaned securities.

Fair value

The Company is responsible for determining the fair value of its investment portfolio by utilizing market-driven fair value measurements from active markets, where available, by considering other observable and unobservable inputs and by employing valuation techniques which make use of current market data. The Company uses a fair-value hierarchy to categorize the inputs used in valuation techniques to measure fair value. A description of the inputs used in the valuation of financial instruments is as follows:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities. The fair value of the Company's common and preferred shares is determined based on quoted prices in active markets obtained from external pricing sources.

Level 2 – Inputs, other than quoted prices, that are observable for the investment either directly or indirectly. These inputs include quoted prices for similar instruments exchanged in active markets; quoted prices for identical or similar instruments exchanged in inactive markets; inputs other than quoted prices that are observable for the instruments, such as interest rates and yield curves, volatilities, prepayment speeds, loss severities, credit risks and default rates where available; and inputs that are derived principally from or corroborated by observable market data and correlation or other means.

The Company's investments in government securities (including federal, provincial and municipal bonds), corporate securities, private placements and infrequently traded securities are priced using publicly traded, over-the-counter prices or broker-dealer quotes which are based on market observable inputs. Observable inputs such as benchmark yields, reported trades, broker dealer quotes, issuer spreads and bids are available for these investments.

Level 3 – Inputs that are not based on observable market data. Management is required to use assumptions regarding unobservable inputs as there is little, if any, market activity in these investments or related observable inputs that can be corroborated at the measurement date. Unobservable inputs require management to make certain projections and assumptions about the information that would be used by market participants in pricing assets. To verify pricing, the Company assesses the reasonability of the fair values by comparing to industry-accepted valuation models, to movements in credit spreads and to recent transaction prices for similar assets where available.

(Unaudited, in thousands of Canadian dollars, except per share amounts)

The economic circumstances that affect the fair value of the Company's financial assets have changed in the period with the increasing interest rates.

The following table provides the classification of the Company's investments within the fair value hierarchy, as outlined above, as at March 31, 2014, and December 31, 2013:

March 31, 2014	**Investments at fair value**			
	Level 1	**Level 2**	**Level 3**	**Total**
Fixed Income	–	380,753	–	380,753
Commercial Mortgages pooled fund	–	–	2,075	2,075
Equities	64,569	–	–	64,569
	64,569	380,753	2,075	447,397

December 31, 2013	**Investments at fair value**			
	Level 1	**Level 2**	**Level 3**	**Total**
Fixed Income	–	384,741	–	384,741
Commercial Mortgages pooled fund	–	–	2,052	2,052
Equities	67,524	–	–	67,524
	67,524	384,741	2,052	454,317

The fair value of the Company's investments, determined with the use of unobservable market information as inputs, is approximately 0.5% (December 31, 2013 – 0.5%) of the total investment portfolio required to be measured at fair value, and consists of commercial mortgages pooled fund with a fair value of $2,075 (December 31, 2013 – $2,052).

A reconciliation of Level 3 investment with the use of significant unobservable inputs are as follows:

	3 months ended March 31	
	2014	**2013**
Balance at beginning of year	2,052	484
Net unrealized gains (losses) included in other comprehensive income	23	–
Balance at end of year	2,075	484

Investment in commercial mortgages pooled fund is valued using the company's share of the net asset value of the commercial mortgage pooled fund as of March 31, 2014.

The Company's policy is to recognize transfers into and transfers out of fair value hierarchy levels as of the date of the event or change in circumstances that caused the transfer. During the three months ended March 31, 2014 and March 31, 2013 there were no transfers between levels.

(Unaudited, in thousands of Canadian dollars, except per share amounts)

Impaired assets and provisions for losses

Management has reviewed currently available information regarding those financial assets where estimated fair values are less than amortized cost. For those investments that are considered impaired, the Company has recorded the difference between the amortized cost of the financial assets and its fair value as an impairment, which reduces investment income recorded in the period.

A provision for impairments on investments of $nil was recognized in 2014 (March 31, 2013 – $5). A remaining gross unrealized loss of $648 on AFS investments held as at March 31, 2014 (March 31, 2013 – $362) is recorded, net of tax, in the amount of $519 (March 31, 2013 – $266) as Accumulated Other Comprehensive Loss.

Investment income

The table below provides additional details on net investment income:

	3 months ended March 31, 2014	3 months ended March 31, 2013
Interest income	3,390	3,046
Dividend income	457	467
Net realized gains	1,663	1,310
Impairment loss	-	(5)
Fair value change on FVTPL investments	552	291
Realized and unrealized foreign exchange gains (losses)	385	315
Investment expenses	(313)	(336)
Investment Income	6,134	5,088

7 Provision for unpaid claims

The fair value of the provision for unpaid claims approximates the carrying value determined in accordance with generally accepted actuarial methods in Canada, which discount estimated future cash flows and include a margin for adverse deviation.

The Company discounts its best estimate of claim provisions at a rate of interest of 2.05% (December 31, 2013 – 2.05%) for all lines of business. The Company determines the discount rate based on the expected return on its investment portfolio of assets with appropriate assumptions for interest rates relating to reinvestment of maturing investments.

The Company recorded a $3,259 reduction to the net provision for unpaid claims relating to redundancies in prior years' estimates (March 31, 2013 – $1,234).

To recognize the uncertainty in establishing these best estimates, to allow for possible deterioration in experience, and to provide greater comfort that the actuarial liabilities are adequate to pay future claims, the Company includes provisions for adverse deviations (PFADs) in some assumptions relating to claims development, reinsurance recoveries and future investment income. The PFADs selected are in the mid-range of those recommended by the Canadian Institute of Actuaries. The aggregate impact of the provision for adverse deviation is to increase the provision for unpaid claims on a gross basis by $25,446 as at March 31, 2014 (December 31, 2013 – $25,515).

(Unaudited, in thousands of Canadian dollars, except per share amounts)

Claims development

Provision for unpaid claims analysis	March 31, 2014	March 31, 2013
Unpaid claims, beginning of year, net	264,095	238,297
Change in undiscounted estimates for losses of prior years	(3,343)	(682)
Change in discount rate	–	1,770
Change in PFADs	(257)	(3,474)
Interest cost	344	1,152
Provision for claims occurring in current period	39,992	33,258
Paid on claims occurring during		
Current year	(7,941)	(6,869)
Prior year	(22,716)	(21,858)
Impact of discontinued items on claims	–	3,131
Unpaid claims, end of period, net	269,174	244,725
Reinsurers' share	33,595	30,296
Net Unpaid Claims	302,769	275,021

The development of insurance liabilities provides a measure of the Company's ability to estimate the ultimate value of claims.

Assumptions used to develop the provision estimate for unpaid claims and adjustment expenses are selected by class of business and geographic location. Consideration is given to the characteristics of the risks, historical trends, and the amount of data available on individual claims, inflation and any other pertinent factors. Some assumptions require a significant amount of judgment such as the expected impacts of future judicial decisions and government legislation. The diversity of these considerations results in it not being practical to identify and quantify all individual assumptions that are more likely than others to have a significant impact on the measurement of the Company's insurance contracts. There were no new assumptions identified in the period as having a potential or identifiable material impact on the overall claims estimate.

8 Risk management

As a provider of insurance products, effective risk management is fundamental to the Company's ability to protect the interests of its customers and shareholders. The Company is exposed to risks of loss pertaining to insurance products. These include risks surrounding product and pricing, underwriting and claims, catastrophic exposure, and matching of assets and liabilities. The Company is also exposed to potential loss from various risks, including interest rate risk, equity market fluctuation risk, credit risk, liquidity risk, and to a lesser extent foreign exchange risk.

(Unaudited, in thousands of Canadian dollars, except per share amounts)

These condensed consolidated interim financial statements do not include all financial risk management information and disclosures required in the annual financial statements and should be read in conjunction with the Company's annual financial statements as at December 31, 2013.

The Company has written principles for overall risk management, as well as written policies covering specific areas such as underwriting, reinsurance, foreign exchange risk, interest rate risk, credit risk, use of derivative financial instruments and non–derivative financial instruments and investment of excess liquidity. There has been no significant change in risk management since year end.

Insurance risk

The risk under any one insurance contract is the possibility that the event occurs and the uncertainty of the amount of the resulting claim. By the very nature of an insurance contract, the risk is random and therefore unpredictable. The principal risk that the Company faces under its insurance contract is that the actual claims payments exceed the carrying amount of the insurance liabilities. This could occur because the frequency or the severity of the claims is greater than estimated. Insurance events are random and the actual number and amount of claims will vary from year to year from the estimate.

The concentration of insurance risk by product line, country, province or state, and underlying currency, will also impact financial results depending on the nature and location of events.

Compared to year end there was no material change to insurance risk.

Interest rate risk

Fluctuations in interest rates have a direct impact on the fair valuation and future cash flow of the Company's fixed income investment portfolio. Generally, the Company's investment income will be reduced during sustained periods of lower interest rates as higher yielding fixed income investments mature or are sold and the proceeds are reinvested at lower rates. During periods of rising interest rates, the fair value of the Company's existing fixed income investments will generally decrease and gains on fixed income securities will likely be reduced.

The sensitivity analysis for interest rate risk as set out in the table below illustrates the impact of changes in interest rates on OCI relating to the fixed income investment portfolio as at March 31, 2014 and December 31, 2013 based on parallel 200 basis point shifts in interest rates up and down in 100 basis point increments.

Change in interest rates	Fair value of fixed income and preferred shares portfolio	Hypothetical change on fair value	Effect on OCI net of tax	Effect on Net Income
As at March 31, 2014				
200 basis point rise	388,300	(6%)	(16,804)	(2,309)
100 basis point rise	401,391	(3%)	(8,402)	(1,155)
No change	414,482	-	-	-
100 basis point decline	427,573	3%	8,402	1,155
200 basis point decline	440,664	6%	16,804	2,309

(Unaudited, in thousands of Canadian dollars, except per share amounts)

Change in interest rates	Fair value of fixed income and preferred shares portfolio	Hypothetical change on fair value	Effect on OCI net of tax	Effect on Net Income
As at December 31, 2013				
200 basis point rise	385,134	(7%)	(17,865)	(3,266)
100 basis point rise	399,254	(4%)	(9,190)	(1,634)
No change	414,081	–	–	–
100 basis point decline	429,669	4%	9,716	1,663
200 basis point decline	443,668	7%	18,274	3,325

Liquidity risk

Liquidity risk is the risk that the Company may not have sufficient liquid financial resources to meet its obligations when they fall due, or would have to incur excessive costs to do so. The Company's liquidity management strategy is to ensure that there is sufficient cash to meet its financial commitments as they become due. To manage cash flow requirements, the Company maintains a portion of invested assets in liquid investments.

The maturity profile of bonds as at March 31, 2014, and December 31, 2013, are as follows:

March 31, 2014	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Bonds	11,832	106,039	131,297	131,585	380,753
Percentage of total	3%	28%	34%	35%	100%

December 31, 2013	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Bonds	45,254	93,212	134,353	111,922	384,741
Percentage of total	12%	24%	35%	29%	100%

The following tables summarize the expected timing of cash flows arising from insurance obligations, on an undiscounted basis, as at March 31, 2014, and December 31, 2013:

March 31, 2014	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Actuarial liabilities (undiscounted)	99,522	104,874	53,306	36,171	293,873
Less: Reinsurance recoverable	12,535	11,798	5,421	3,586	33,340
Net actuarial liabilities	86,987	93,076	47,885	32,585	260,533

(Unaudited, in thousands of Canadian dollars, except per share amounts)

December 31, 2013	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Actuarial liabilities (undiscounted)	90,588	99,657	54,687	40,276	285,209
Less: Reinsurance recoverable	12,664	9,809	4,936	3,715	31,124
Net actuarial liabilities	77,924	89,848	49,752	36,561	254,085

All other financial liabilities are for duration of one year or less. The contractual maturities for lease commitments are listed in note 12.

Equity price risk

Fluctuations in the value of equity investments affect the level and timing of recognition of gains and losses on securities held, and cause changes in realized and unrealized gains and losses. General economic conditions, political conditions and many other factors can also adversely affect the stock and bond markets and, consequently, the value of the equity and fixed income investments held.

The Company has policies to limit and monitor its exposure to individual issuers and classes of issuers of equity securities.

The table below summarizes the potential impact of a 10% change in the value of the equity securities (common and preferred shares) on net income and OCI for the quarter ended March 31, 2014, and the year ended December 31, 2013. Certain shortcomings are inherent in the method of analysis presented, as the analysis is based on the assumption that all equity holdings increased/decreased by 10% with all other variables held constant.

Change in equity holdings	Effect on Net Income		Effect on OCI net of tax	
	March 31, 2014	December 31, 2013	March 31, 2014	December 31, 2013
10% rise	2,462	2,142	2,251	2,787
10% decline	(2,462)	(2,142)	(2,251)	(2,787)

Credit risk

The Company is exposed to credit risk principally through its investment securities and balances receivable from policyholders and reinsurers. The Company has policies to limit and monitor its exposure to individual issuers and classes of issuers of investment securities which do not carry the guarantee of a national or Canadian provincial government. The Company's credit exposure to any one individual policyholder is not material. The Company has policies that limit its exposure to individual reinsurers and regular review processes to assess the creditworthiness of reinsurers with whom it transacts business.

The Company is exposed to risk from reinsurers' inability to cover balances. 93.2% of the Company's reinsurance balances are from registered reinsurers. The Company holds sufficient collateral to cover the 6.8% of reinsurance balances from unregistered reinsurers.

(Unaudited, in thousands of Canadian dollars, except per share amounts)

The following table sets forth the Company's fixed income securities portfolio by credit quality as at March 31, 2014, and December 31, 2013.

Fixed income portfolio

	As at March 31, 2014		As at December 31, 2013	
	Fair value	**Fair value**	**Fair value**	**Fair value**
AAA	109,345	29%	138,283	36%
AA	81,271	21%	66,644	17%
A	87,601	23%	87,761	23%
BBB	60,252	16%	54,248	14%
BB	24,940	6%	23,730	6%
B	5,829	2%	4,554	1%
CCC	2,519	1%	1,969	1%
Unrated	8,996	2%	7,552	2%
Total	380,753	100%	384,741	100%

Preferred share portfolio

	As at March 31, 2014		As at December 31, 2013	
	Fair value	**Fair value**	**Fair value**	**Fair value**
P1	3,542	11%	3,428	12%
P2	27,788	82%	23,540	80%
P3	2,399	7%	2,372	8%
Total	33,729	100%	29,340	100%

9 Intangible assets

	Opening cost	Purchases	Sales	End of period cost	Accumulated amortization	Net
Software						
March 31, 2014	13,301	3,893	–	17,194	9,395	7,799
December 31, 2013	10,403	2,898	–	13,301	8,341	4,960
Goodwill						
March 31, 2014	400	–	–	400	–	400
December 31, 2013	595	–	195	400	–	400
Total intangible assets						
March 31, 2014	13,701	3,893	–	17,594	9,395	8,199
December 31, 2013	10,998	2,898	195	13,701	8,342	5,359

The Company purchased a policy administration system in the period for $3,500.

(Unaudited, in thousands of Canadian dollars, except per share amounts)

10 Related party transactions

The Co–operators Group Limited and Co–operators General Insurance Company (collectively Co–operators), significant shareholders of the Company, provide services to the Company, including but not limited to product distribution and investment management services under arms length contracts. Direct written premiums derived from Co–operators' agents were $1,731 (March 31, 2013 – $2,213), commissions paid were $200 (March 31, 2013 – $254) and investment management fees were $68 (March 31, 2013 – $113).

The Company has a 2001 100% Quota Share reinsurance treaty with Co–operators General Insurance Company. Reinsurers share of unpaid claims includes a recoverable of $92 (March 31, 2013 – $316) from Co-operators General Insurance Company. The payable to insurance companies balance includes amounts due to Co-operators General Insurance Company of $120 (March 31, 2013 – $96).

11 Income taxes

The income tax expense (recovery) is as follows:

	3 months ended March 31, 2014	**3 months ended March 31, 2013**
Current	1,526	39
Deferred	(255)	(255)
	1,271	(216)

The effective income tax rates are different from the combined federal and provincial income tax rates. The consolidated statements of income and comprehensive income contain items that are non-taxable or non-deductible for income tax purposes, which cause the income tax expense to differ from what it would have been if based on statutory rates. The difference is broken down as follows:

	Three months ended March 31	
	2014	**2013**
Income tax expense (recovery) calculated at statutory rates	27.0%	27.0%
Increase(decrease) in income tax rates resulting from:		
Non-taxable dividend income	(1.8)%	6.2%
Non-taxable income	(4.3)%	(3.7)%
Non-deductible expenses	1.4%	(4.2)%
Non-taxable portion of capital gains	(2.0)%	–
Other	(1.2)%	(4.3)%
Effective income tax rate	19.1%	21.1%

12 Lease commitments

The Company is committed under lease agreements for office premises and computer equipment with minimum lease payments of $6,802 as follows:

Lease commitments	
2014	1,151
2015	1,513
2016	1,471
2017	1,294
2018	594
2019 and thereafter	779
	6,802

13 Accumulated other comprehensive income

	As at March 31, 2014	As at December 31, 2013
Gross unrealized gains	10,393	6,694
Foreign currency translation adjustments	2,041	1,527
Tax impact	(2,040)	(1,051)
Ending balance	10,394	7,170

14 Earnings per share

	3 months ended March 31, 2014	3 months ended March 31, 2013
Basic earnings per share on continuing operations:		
Net continuing income available to shareholders	5,295	119
Average number of common shares (in thousands)	11,732	11,904
Basic earnings per share on continuing operations	$0.45	$0.01
Diluted earnings per share on continuing operations:		
Average number of common shares (in thousands)	11,732	11,904
Average number of dilutive common shares under employee stock option plan (in thousands)	392	–
Average number of diluted common shares (in thousands)	12,124	11,904
Diluted earnings per share on continuing operations	$0.44	$0.01

	3 months ended March 31, 2014	**3 months ended March 31, 2013**
Basic earnings per share:		
Net income available to shareholders	5,295	(821)
Average number of common shares (in thousands)	11,732	11,904
Basic earnings per share	$0.45	($0.07)
Diluted earnings per share:		
Average number of common shares (in thousands)	11,732	11,904
Average number of dilutive common shares under employee stock option plan (in thousands)	392	–
Average number of diluted common shares (in thousands)	12,124	11,904
Diluted earnings per share	$0.44	($0.07)

15 Non Controlling Interest

	3 months ended March 31, 2014	**3 months ended March 31, 2013**
Revenue		
Gross written and assumed premiums	17,725	7,293
Net earned premiums	4,854	1,716
Investment income	89	(9)
Total Revenue	4,943	1,707
Expenses		
Net incurred claims	2,428	899
Net acquisition costs	1,814	467
Operating costs	560	462
Total expenses	4,802	1,828
Income (loss) before income taxes	141	(121)
Income tax expense	41	(32)
Net income (loss) attributable to non-controlling interests	100	(89)

(Unaudited, in thousands of Canadian dollars, except per share amounts)

	March 31, 2014	December 31, 2013
Assets		
Cash and investments	15,889	18,937
Other assets	24,020	28,944
Total assets	39,909	47,881
Liabilities		
Unearned premium	21,166	27,056
Unpaid claims	8,644	1,923
Other liabilities	9,025	11,058
Total liabilities	38,835	50,037
Equity		
Share capital	1,734	–
AOCI	516	–
Retained earnings	(1,176)	(2,156)
Total equity	1,074	(2,156)
Total liabilities and equity	39,909	47,881

On February 28, 2014 the Company purchased an additional 20.1% ownership in QIC Holdings ApS (QIC) bringing the total ownership to 71.1%.

16 Commitments and Contingencies

On March 28, 2014 EGI announced that it has entered into a definitive agreement with SGI CANADA to acquire 75% of the Insurance Company of Prince Edward Island. The Company is awaiting regulatory approval and the transaction is expected to close in Q2 2014.

17 Segmented information

The Company operates through three segments: Personal Lines and Specialty Programs divisions in Canada and specialty business in the International division. Through its Personal Lines division, the Company is engaged primarily in the underwriting of high premium, non–standard automobile insurance.

Through its Specialty Programs division, the Company designs and underwrites specialized non–auto insurance programs, such as higher premium property, primary and excess liability, legal expense, accident and health insurance and warranty coverage. Through the International division the Company underwrites European property, automobile and other niche and specialty insurance products.

The effect of reinsurance is reflected in the revenue and results of each segment. The investment activities consist of managing the investment portfolio for the Company as a whole. Investment income is shown net of investment expenses. The corporate and other activities include holding company expenses not attributable to a division.

(Unaudited, in thousands of Canadian dollars, except per share amounts)

	3 months ended March 31	
	2014	**2013**
Revenue		
Earned premiums		
Canada – Personal Lines	30,555	30,237
– Specialty Programs	8,371	7,364
	38,926	37,601
International	23,172	6,965
Total earned premium	62,098	44,566
Net claims Incurred		
Canada – Personal Lines	17,751	22,599
– Specialty Programs	5,260	5,139
	23,011	27,738
International	12,725	4,286
Total net claims incurred	35,736	32,024
Net expenses		
Canada – Personal Lines	9,892	8,970
– Specialty Programs	4,740	3,344
	14,632	12,314
International	10,060	3,012
Corporate Expenses	1,138	731
Total net expenses	25,830	16,057
Income (loss) before income taxes		
Canada – Personal Lines	2,912	(1,332)
– Specialty Programs	(1,629)	(1,119)
	1,283	(2,451)
International	387	(333)
Corporate and other	(1,138)	(731)
Underwriting (loss) income	532	(3,515)
Impact of change in net claims discount rate		(1,759)
Investment income	6,134	5,088
Total income before income taxes – continuing operations	6,666	(186)

(Unaudited, in thousands of Canadian dollars, except per share amounts)

Segmented long-term assets

	As at March 31, 2014	As at December 31, 2013
Canada – Personal Lines	4,388	5,051
– Specialty Programs	787	804
	5,175	5,855
International	341	260
Total segmented long-term assets	5,516	6,115