Consolidated Financial Statements of

Echelon Financial Holdings Inc.

December 31, 2018

Management's Responsibility for Financial Reporting

Roles of Management, Board of Directors and Audit and Risk Committee

Management is responsible for the preparation and fair presentation of the financial statements, management's discussion and analysis and other information in the annual report. The financial statements of Echelon Financial Holdings Inc. ("the Company") were prepared in accordance with International Financial Reporting Standards. Where necessary, these financial statements reflect amounts based on the best estimates and judgement of management.

In meeting its responsibility for the reliability of the consolidated financial statements, management maintains the necessary system of internal controls. These controls are designed to provide management with reasonable assurance that the financial records are reliable for preparing financial statements and other financial information, assets are safeguarded against unauthorized use or disposition and liabilities are recognized. The Audit and Risk Committee, composed of directors who are not officers or employees of the Company, meets, as required, with management, the Appointed Actuary and the external auditor to review actuarial, accounting, reporting and internal control matters. The Audit and Risk Committee is responsible for reviewing the financial statements and management's discussion and analysis and recommending them to the Board of Directors for approval.

Role of Appointed Actuary

The Actuary is appointed by the Board of Directors, pursuant to the Insurance Companies Act. The Appointed Actuary is responsible for ensuring that the assumptions and methods used in the valuation of policy liabilities are in accordance with accepted actuarial practice, applicable legislation and associated regulations or directives. The Appointed Actuary is also required to provide an opinion regarding the appropriateness of the policy liabilities to meet all policyholder obligations of the Company at the balance sheet date. Examination of supporting data for accuracy and completeness and consideration of the Company's assets are important elements of the work required to form this opinion. The Appointed Actuary uses the work of the external auditor in verifying data used for valuation purposes. Policy liabilities include unearned premiums, provision for unpaid claims, reinsurers' share of unearned premiums and provision for unpaid claims and deferred policy acquisition costs.

Role of External Auditor

PricewaterhouseCoopers LLP, external auditor, has been appointed by the shareholders to conduct an independent audit of the consolidated financial statements of the Company in accordance with Canadian generally accepted auditing standards and report to the shareholders regarding the fairness of the annual financial statements. The external auditor considers the work of the Appointed Actuary in respect of policy liabilities included in the financial statements, on which the Appointed Actuary has rendered an opinion.

Toronto, Ontario
February 14, 2019

(Signed) Serge Lavoie	(Signed) Patrick Espeut
Chief Executive Officer	Interim Chief Financial Officer

Independent auditor's report

To the Shareholders of Echelon Financial Holdings Inc.

Our opinion

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of Echelon Financial Holdings Inc. and its subsidiaries (together, the Company) as at December 31, 2018 and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS) as issued by International Accounting Standards Board (IASB).

What we have audited
The Company's consolidated financial statements comprise:

- the consolidated balance sheet as at December 31, 2018;
- the consolidated statement of income and comprehensive income for the year then ended;
- the consolidated statement of changes in equity for the year then ended;
- the consolidated statement of cash flows for the year then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

Basis for opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence
We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada. We have fulfilled our other ethical responsibilities in accordance with these requirements.

Other information

Management is responsible for the other information. The other information comprises the Management's Discussion and Analysis and the information, other than the consolidated financial statements and our auditor's report thereon, included in the annual report.

PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto, Ontario, Canada M5J 0B2
T: +1 416 863 1133, F: +1 416 365 8215

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the consolidated financial statements

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

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

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

Auditor's responsibilities for the audit of the consolidated financial statements

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

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

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Company to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

The engagement partner on the audit resulting in this independent auditor's report is Akif Siddiqui.

PricewaterhouseCoopers LLP

Chartered Professional Accountants, Licensed Public Accountants

Toronto, Ontario
February 14, 2019

To the Shareholder of Echelon Financial Holdings Inc.

I have valued the policy liabilities and reinsurance recoverables of the following subsidiary insurance operations of Echelon Financial Holdings Inc.: The Insurance Company of Prince Edward Island, and the Warranty business of Echelon Financial Holdings Inc., for their statement of financial position at December 31, 2018 and their changes in the statements of income and comprehensive income for the year then ended in accordance with accepted actuarial practice in Canada including selection of appropriate assumptions and methods.

In my opinion, the amount of policy liabilities for The Insurance Company of Prince Edward Island and the Warranty business of Echelon Financial Holdings Inc. make appropriate provision for all their policy obligations. The financial statements of The Insurance Company of Prince Edward Island and the Warranty business of Echelon Financial Holdings Inc. fairly present the results of those companies. The consolidated financial statements are the sum of my valuation for The Insurance Company of Prince Edward Island and the Warranty business of Echelon Financial Holdings Inc., and the valuation of Echelon Insurance provided by Nicolas Beaudoin of Willis Towers Watson.

Eric Millaire-Morin
Fellow, Canadian Institute of Actuaries

Toronto, Ontario
February 14, 2019

To the Shareholder of Echelon Financial Holdings Inc.

I have valued the policy liabilities and reinsurance recoverables for Echelon Insurance, a subsidiary insurance operation of Echelon Financial Holdings Inc., for its statement of financial position at December 31, 2018 and their changes in the statements of income and comprehensive income for the year then ended in accordance with accepted actuarial practice in Canada including selection of appropriate assumptions and methods.

In my opinion, the amount of policy liabilities for Echelon Insurance makes appropriate provision for all its policy obligations. The financial statements of Echelon Insurance fairly present the results of the valuation of Echelon Insurance. The consolidated financial statements for Echelon Financial Holdings Inc. are the sum of my valuation for Echelon Insurance, and the valuation of The Insurance Company of Prince Edward Island and the Warranty business of Echelon Financial Holdings Inc. provided by Eric Millaire-Morin of Echelon Insurance.

Nicolas Beaudoin
Fellow, Canadian Institute of Actuaries

Toronto, Ontario
February 14, 2019

175 Bloor Street East
South Tower
Suite 1701
Toronto, Ontario
M4W 3T6

T +1 416 960.2700
F +1 416 960 2819
W willistowerswatson.com

Towers Watson Canada Inc.

ECHELON FINANCIAL HOLDINGS INC.
Consolidated Balance Sheet
(in thousands of Canadian dollars)

	Note	December 31, 2018	December 31, 2017
Assets			
Cash and short–term deposits	6	22,785	44,459
Accounts receivable		11,738	75,622
Loan receivable	7	—	6,553
Investments (including securities on loan)	6	45,576	370,933
Due from insurance companies		—	510
Deferred policy acquisition costs	9	3,995	40,888
Income taxes recoverable		—	1,001
Prepaid expenses and other assets		191	2,462
Reinsurers' share – unearned premiums	10	1,522	9,957
– provision for unpaid claims	11	4,889	23,471
Property and equipment		6	859
Intangible assets	14	—	8,037
Deferred income taxes	15	781	5,834
Assets of the disposal group held for sale	26	576,733	—
Total assets		668,216	590,586
Liabilities			
Income taxes payable	15	41	—
Accounts payable and accrued liabilities		11,075	18,116
Payable to insurance companies		1,041	610
Unearned premiums	10	16,848	160,577
Unearned commission	9	179	1,667
Provision for unpaid claims	11	24,090	262,966
Liabilities of the disposal group held for sale	26	465,433	—
Total liabilities		518,707	443,936
Equity			
Share capital	16	71,997	71,520
Contributed surplus		303	248
Retained earnings		76,244	73,887
Accumulated other comprehensive income	24	(2,877)	(2,833)
Equity attributed to shareholders of the Company		145,667	142,822
Non-controlling interest	27	3,842	3,828
Total equity		149,509	146,650
Total liabilities and equity		668,216	590,586

The accompanying notes are an integral part of these consolidated financial statements approved on February 14, 2019.

On behalf of the Board of Directors:

(Signed) Serge Lavoie
Chief Executive Officer

(Signed) Murray Wallace
Chairman of the Board

ECHELON FINANCIAL HOLDINGS INC.
Consolidated Statement of Income and Comprehensive Income
(in thousands of Canadian dollars, except per share amounts)

	Note	For the year ended December 31	
		2018	**2017**
Revenue			
Gross written and assumed premiums		33,937	32,489
Less: premiums ceded to reinsurers		(3,406)	(3,146)
Net written and assumed premiums		30,531	29,343
(Decrease) in gross unearned premiums		(656)	(1,397)
Increase in unearned premiums, reinsurers' share		62	124
Change in provision for unearned premiums		(594)	(1,273)
Net earned premiums		29,937	28,070
Investment income	6	1,463	6,909
Total revenue		31,400	34,979
Expenses			
Gross claims incurred		20,479	18,802
Less: claims recoveries from reinsurers		(676)	(697)
Net incurred claims		19,803	18,105
Gross acquisition costs		7,145	7,074
Less: acquisition recoveries from reinsurers		(82)	(48)
Net acquisition costs		7,063	7,026
Operating costs	19	7,898	6,015
Total expenses		34,764	31,146
(Loss) Income before taxes and discount rate impact on claims		(3,364)	3,833
Impact of change in discount rate on claims(1)		360	234
(Loss) Income before interest expense and income taxes		(3,004)	4,067
Income tax (recovery)	15	(603)	(705)
Net income on continued operations		(2,401)	4,772
Net Income (loss) on discontinued operations	26	4,776	(2,984)
Net income		2,375	1,788
Attributed to:			
Shareholders of the Company - continued operations		(2,419)	4,618
Shareholders of the Company - discontinued operations	26	4,776	(2,984)
Non-controlling interest - continued operations	27	18	154
Net income		2,375	1,788
Other comprehensive income (loss), net of taxes that may be classified subsequently to net income			
Available-for-sale investments:			
Change in net unrealized (losses)/gains		(614)	4
Reclassification of net realized (gains) losses to net income		376	23
Foreign exchange forward		—	(4,314)
Cumulative translation (loss)		(46)	—
Tax impact		3	689
Other comprehensive (loss) on continued operations		(281)	(3,598)
Other comprehensive income on discontinued operations	26	233	5,867
Other comprehensive (loss) income		(48)	2,269

ECHELON FINANCIAL HOLDINGS INC.
Consolidated Statement of Income and Comprehensive Income
(in thousands of Canadian dollars, except per share amounts)

	Note	2018	2017
Attributed to:			
Shareholders of the Company - continued operations		(277)	(3,531)
Shareholders of the Company - discontinued operations	26	233	5,867
Non-controlling interest - continued operation	27	(4)	(67)
Non-controlling interest - discontinued operation	26	—	—
Other comprehensive (loss) income		(48)	2,269
Total comprehensive income		2,327	4,057
Attributed to:			
Shareholders of the Company - continued operations		(2,696)	1,087
Shareholders of the Company - discontinued operations	26	5,009	2,883
Non-controlling interest - continued operation	27	14	87
Non-controlling interest - discontinued operation	26	—	—
Total comprehensive income		2,327	4,057
Earnings per share attributable to shareholders of the Company	25		
Earnings per share continued operations - basic		$(0.20)	$0.39
Earning (Loss) per share discontinued operations - basic		$0.40	$(0.25)
Earnings per share - basic		$0.20	$0.14
Earnings per share continued operations - diluted		$(0.20)	$0.38
Earning (Loss) per share discontinued operations - diluted		$0.39	$(0.25)
Earnings per share - diluted		$0.19	$0.14
Net income		2,375	1,788

(1) As interest rates may change each period, and have an impact to the incurred claims and therefore management believes it is beneficial to the users to see the impact of this change separately in order to understand the true movement in claims incurred.

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

ECHELON FINANCIAL HOLDINGS INC.
Consolidated Statement of Changes in Equity
(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, 2018	71,520	248	(2,833)	73,887	142,822	3,828	146,650
Net income	—	—	—	2,357	2,357	18	2,375
Other comprehensive loss	—	—	(44)	—	(44)	(4)	(48)
Total comprehensive income	—	—	(44)	2,357	2,313	14	2,327
Common shares issued on stock options exercised	477	(46)	—	—	431	—	431
Stock compensation expense	—	101	—	—	101	—	101
Balance at December 31, 2018	71,997	303	(2,877)	76,244	145,667	3,842	149,509

	Share Capital	Contributed Surplus	Accumulated Other Comprehensive Income	Retained Earnings	Shareholders' Equity	Non-controlling interest	Total Equity
Balance at January 1, 2017	70,227	322	(5,070)	71,935	137,414	3,960	141,374
Net income	—	—	—	1,634	1,634	154	1,788
Other comprehensive income	—	—	2,336	—	2,336	(67)	2,269
Total comprehensive income	—	—	2,336	1,634	3,970	87	4,057
Transfer of currency translation adjustment	—	—	(99)	318	219	(219)	—
Common shares issued on stock options exercised	1,293	(147)	—		1,146	—	1,146
Stock options expense	—	73	—	—	73	—	73
Balance at December 31, 2017	71,520	248	(2,833)	73,887	142,822	3,828	146,650

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

ECHELON FINANCIAL HOLDINGS INC.
Consolidated Statement of Cash Flows
(in thousands of Canadian dollars)

	For the year ended December 31	
	2018	**2017**
Cash provided by (used in):		
Operating activities		
Net income from continued operations	(2,401)	4,772
Net Income (loss) from discontinued operations	4,776	(2,984)
Adjusted for:		
Reinsurers' share of unearned premiums	(62)	(124)
Reinsurers' share of unpaid claims	(509)	(697)
Provision for unpaid claims	(157)	1,411
Unearned premiums	656	1,397
Deferred income taxes	(127)	1,012
Unearned commissions	47	51
Deferred policy acquisition costs	(170)	(591)
Amortization on property plant equipment and intangible assets	3	4
Amortization of premiums on bonds	48	91
Fair value change on FVTPL investments	338	(3,503)
Options expense	101	73
Currency translation	(46)	—
Foreign exchange forward	—	(4,314)
Prepaid expenses & other assets	(154)	(10)
	(32)	(5,200)
Cash flow from changes in		
Accounts receivable	(1,266)	(898)
Net realized losses	408	1,352
Income taxes payable	349	99
Due to insurance companies	1,041	—
Other liabilities	5,604	39
Cash provided by continuing operating activities	3,703	164
Cash provided (used) by discontinued operating activities	46,852	(121,096)
Cash inflow (outflow) from operating activities	50,555	(120,932)
Financing activities		
Proceeds from issuing of common shares for stock options	431	1,146
Cash provided by continuing financing activities	431	1,146
Cash inflow from financing activities	431	1,146
Investing activities		
Purchases of property, equipment and intangible assets	(7)	—
Purchases of investments	(26,013)	(20,672)
Sale/maturity of investments	24,806	9,228

ECHELON FINANCIAL HOLDINGS INC.
Consolidated Statement of Cash Flows
(in thousands of Canadian dollars)

	2018	2017
Proceeds received from the sale of subsidiary	6,553	16,731
Cash provided (used) by continuing investing activities	5,339	5,287
Cash provided by discontinued investing activities	28,820	21,323
Cash from investing activities	34,159	26,610
Increase (decrease) in cash and short-term deposits	85,145	(93,176)
Cash and short-term deposits, beginning of year	44,459	137,635
Cash and short-term deposits, end of year	129,604	44,459
Supplementary information		
Income taxes paid (recovered)	(719)	93

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

1 Nature of operations

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

The Company's wholly-owned subsidiaries are Echelon Insurance ("Echelon"), CIM Reinsurance Company Ltd. ("CIM Re") and CUISA Managing General Agency Corporation ("CUISA MGA"). The Company also owns 75% of The Insurance Company of Prince Edward Island ("ICPEI").

The Company completed the sale of Qudos Insurance A/S ("Qudos") on March 7, 2017.

On November 9, 2018, the Company entered into a definitive agreement to sell Echelon Insurance, its main operating subsidiary, and the unregulated warranty business of Echelon Financial Holdings Inc. ("Discontinued Canadian Operations") and is awaiting regulatory approval.

2 Basis of preparation

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

These consolidated financial statements have been authorized for issue by the Board of Directors, on February 14, 2019.

3 Summary of significant accounting policies

Discontinued Operations

Assets and liabilities are classified as held for sale (discontinued operations) if their carrying amounts are recovered through a sales transaction rather than through continuing use. This condition is satisfied when the asset is available for immediate sale in its present condition, management is committed to the sale and it is highly probable to occur within one year. Assets classified as held-for-sale are measured at their lower of their previous carrying amount and fair value, less costs to sell, and are presented separately from other assets on our Consolidated Balance Sheets.

A disposal group is classified as a discontinued operation if it meets the following conditions: (a) it is a component that can be distinguished operationally and financially from the rest of our operations, and (b) it represents either a separate major line of business or is part of a single coordinated plan to dispose of a separate major line of business or geographical area of operations.

Basis of measurement

The consolidated financial statements have been prepared under the historical cost convention, except for investments and insurance contracts which are carried at fair value and in accordance with IFRS 4, respectively. Discontinued operations are held for sale as described below.

Balance sheet presentation

The Company does not classify its assets and liabilities as current and non-current on its balance sheets. As a financial institution, the Company provides insurance services over a period of years, rather than within a clearly identifiable short-term operating cycle. The consolidated statement of financial position is presented in the order of liquidity, based on expectations regarding recovery or settlement within 12 months after the reporting date, and more than 12 months after the reporting date as presented in the respective notes.

The maturity profile of the investment portfolio is described in note 13 based on expected settlements. The estimated payment period for insurance claims, less related reinsurance recoverable, is provided in note 13. Property and equipment assets are charged to expense over their estimated useful lives of up to three years. Intangible assets with finite useful lives are charged to expense over their estimated useful lives of two years while an impairment analysis is done on all other intangible assets. Cash and short term deposits, accounts receivables due from insurance companies, income taxes receivables and payable, accounts payable and accrued liabilities are expected to be recovered or settled within twelve months of the year end.

Consolidation

The consolidated financial statements of the Company consolidate the accounts of Echelon Financial Holdings Inc. and its subsidiaries. All inter-company transactions, balances and unrealized gains and losses from inter-company transactions are eliminated on consolidation.

Subsidiaries are those entities which Echelon Financial Holdings Inc., through its investment in the entity, are exposed or has rights to variable returns from its involvement with the investee, and has the ability to affect those returns through its power over the investee. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether Echelon Financial Holdings Inc. controls another entity. Subsidiaries are fully consolidated from the date on which control is obtained by Echelon Financial Holdings Inc. and are de-consolidated from the date that control ceases.

Non-controlling interests represent equity interests in subsidiaries owned by outside parties. The share of net assets of subsidiaries attributable to non-controlling interests is presented as a component of equity. Changes in the parent company’s ownership interest in subsidiaries that do not result in a loss of control are accounted for as equity transactions.

Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to senior management, the Chief Executive Officer and Board of Directors of the Company.

Foreign currency translation

(i) Functional and presentation currency

Items included in the financial statements of each consolidated entity of the Company are measured using the currency of the primary economic environment in which the entity operates (the “functional currency”). The consolidated financial statements are presented in Canadian dollars, which is the Company’s functional and presentation currency.

The financial statements of subsidiaries that have a functional currency different from the presentation currency of the Company (“foreign operations”) are translated into Canadian dollars as follows: assets and liabilities – at the closing rate at the date of the balance sheet; and, income and expenses – at the average rate of the period (as this is considered a reasonable approximation to actual rates). The accumulated gains or losses arising from translation of functional currencies to the presentation currency are included as a separate component of OCI within equity.

QIC Holdings ApS’s (QIC), Qudos Insurance A/S ("Qudos") and CIM Re’s functional currency is Danish Krone and is subject to foreign currency translation adjustments upon consolidation. Qudos was disposed in 2017 and is now part of Discontinued Operations, as noted above.

When an entity disposes of its entire interest in a foreign operation, or loses control, joint control, or significant influence over a foreign operation, the foreign currency gains or losses accumulated in OCI related to the foreign operation are recognized in the income statement. If an entity disposes of part of an interest in a foreign operation which remains a subsidiary, a proportionate amount of foreign currency gains or losses accumulated in OCI related to the subsidiary are reallocated between controlling and non-controlling interests.

(ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates in effect at the date the transactions occurred. Foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at year-end exchange rates of monetary assets and liabilities are recognized in investment income in the consolidated statements of income and comprehensive income. Exchange gains and losses related to non-monetary investments classified as Available for Sale (AFS) are recorded in OCI. Changes in the fair value of monetary securities denominated in foreign currency classified as available for sale are analyzed between translation differences resulting from changes in the amortized cost of the security and other changes in the carrying amount of the security. Translation differences related to changes in amortized cost are recognized in profit or loss, and other changes in carrying amount are recognized in OCI.

Cash and short-term deposits

Cash and short-term deposits include cash-on-hand, cash balances with banks and short-term investments. Short-term investments are defined as loans of less than one year to maturity at the time of acquisition. These financial assets are classified as loans and receivables and are recorded at an amortized cost which approximates fair value.

Investments under securities lending program

Securities lending transactions are entered into on a collateralized basis. The securities lent are not derecognized on the consolidated balance sheet given that the risks and rewards of ownership are not transferred from the Company to the counterparties in the course of such transactions. Securities received from counterparties as collateral are not recorded on the consolidated balance sheet given that the risks and rewards of ownership are not transferred from the counterparties to the Company in the course of such transactions.

In the event that any loan made pursuant to the securities lending agreement is terminated and the loaned security, or any portion thereof, is not returned to the Company for any reason (including, without limitation, the insolvency or bankruptcy of the Borrower) within the time specified by the applicable Borrowing Agreement, the agent shall be jointly and severally liable, at its expense to:

i. Promptly replace such security, or any portion thereof, not so returned with other securities of the same issuer, class, and denomination and with the same interest/dividend rights and other economic benefits as such, should the security have been returned; or,

ii. If it is unable to purchase such security on the open market, the agent will credit Echelon in cash with the market value of such unreturned security, such market value to be determined as of the close of business on the date on which such security was required to be returned, including any future economic benefits that the company would have earned on holding the security.

Financial instruments

Financial assets and liabilities are recognized when the Company becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership.

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

At initial recognition, the Company classifies its financial instruments in the following categories depending on the purpose for which the instruments were acquired:

(i) *Financial assets and liabilities at fair value through profit or loss (FVTPL)*: A financial asset or liability is classified in this category if acquired principally for the purpose of selling or repurchasing in the short-term, or if it is designated at FVTPL by management. The Company has designated as FVTPL under the fair value option financial assets which contain embedded derivatives that significantly alter the cash flows of the underlying asset.

    Financial instruments in this category are recognized initially and subsequently at fair value. Gains and losses arising from changes in fair value are presented in the consolidated statements of income and comprehensive income within investment income in the year in which they arise. The Company's investments in preferred shares are classified as FVTPL.

(ii) *Available-for-sale (AFS) investments*: Non-derivative financial assets that are either designated in this category or not classified in any of the other categories are AFS investments. The Company's AFS investments are comprised of marketable securities and investments in debt and common equity securities.

AFS investments are recognized initially at fair value plus transaction costs and are subsequently carried at fair value. Gains or losses arising from changes in fair value are recognized in OCI.

Interest on AFS investments, calculated using the effective interest method, is recognized in the consolidated statements of income and comprehensive income within investment income. Dividends on AFS equity instruments are recognized in the consolidated statements of income and comprehensive income as part of investment income when the Company's right to receive payment is established. When an AFS investment is sold or impaired, the accumulated gains or losses are moved from accumulated OCI to the consolidated statements of income and comprehensive income and included within investment income.

(iii) *Loans and receivables*: Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Company's loans and receivables are comprised of accounts receivables, due from insurance companies, and cash and short-term deposits. Loans and receivables are initially recognized at fair value plus transaction costs. Subsequently, loans and receivables are measured at amortized cost using the effective interest method less any provision for impairment.

(iv) *Financial liabilities at amortized cost*: Financial liabilities at amortized cost include accounts payable. Accounts payable are initially recognized at fair value. Subsequently, accounts payable are measured at amortized cost using the effective interest method.

Impairment of financial assets and liabilities

The Company determines, at each reporting date, whether there is objective evidence that financial assets and liabilities are impaired. The criteria used to determine if objective evidence of an impairment loss include:

i. Significant financial difficulty of the obligor;
ii. Delinquencies in interest, principal or dividend payments; and
iii. it becomes probable that the borrower will enter bankruptcy or other financial reorganization.

If such evidence exists, the Company recognizes an impairment loss, as follows:

AFS investments: The impairment loss is the difference between the amortized cost of the asset and its fair value at the measurement date, less any impairment losses previously recognized in the consolidated statements of income and comprehensive income. This amount represents the cumulative loss in accumulated OCI that is reclassified to the consolidated statements of income and comprehensive income.

Loans and receivables carried at amortized costs: The loss is the difference between the amortized cost of the loan and receivables and the present value of the estimated future cash flows, discounted using the instrument's original effective interest rate. The carrying amount of the asset is reduced by this amount either directly or indirectly through the use of an allowance account.

Impairment losses on financial assets and accrued liabilities carried at amortized cost are reversed in subsequent years if the amount of the loss decreases or the fair value of financial assets and accrued liabilities carried at amortized cost increases and the decrease/increase can be related objectively to an event occurring after the impairment was recognized. In contrast, impairment losses on AFS equity instruments are not reversed.

Debt Impairment Model

- One or more loss events (a payment default for example) and change in credit rating that occurred after initial recognition and that has an impact on the estimated future cash flows of the financial asset.

Equity Impairment Model

- A significant, a prolonged, or a significant and prolonged decline in the fair value of an investment below cost.

Unrealized loss position	**Common shares**
Significant	Unrealized loss of 50% or more
Prolonged	Unrealized loss for 15 consecutive months or more
Significant and prolonged	Unrealized loss for 9 consecutive months or more and unrealized loss of 30%

Insurance contracts

Insurance contracts are those contracts that transfer significant insurance risk at the inception of the contract. Insurance risk arises when the Company agrees to compensate a policyholder if a specified uncertain future event adversely affects the policyholder. Significant risk is defined as the possibility of having to pay significantly more in a scenario where the insured event occurs than when it does not occur.

Provision for unpaid claims

Provision for unpaid claims, including adjustment expenses, represents the estimated amounts required to settle all outstanding and unreported claims incurred to the end of the year. Unpaid claims liabilities are discounted to take into account the time value of money. It also includes a provision for adverse deviation. Expected reinsurance recoveries on unpaid claims and adjustment expenses, net of any required provision for doubtful amounts, are recognized as assets at the same time, using principles consistent with the Company's method for establishing the related liability.

Structured settlements

In the normal course of claims adjudication, the Company settles certain obligations to claimants through the purchase of annuities from third party life insurance companies under structured settlement arrangements (structured settlements). In accordance with OSFI Guideline D-5, these contracts are categorized as either Type 1 or Type 2 based on the characteristics of the claim settlement. When the Company does not retain a reversionary interest under the contractual arrangement to any current or future benefits of the annuity, and the Company has obtained a legal release of the obligation from the claimant, it will be classified as a Type 1 structured settlement. For such contracts, any gain or loss arising on the purchase of an annuity is recognized in the consolidated statement of income at the date of purchase and the related claims liabilities are de-recognized. All other structured settlements that do not meet these criteria are classified as Type 2, with the Company recognizing the annuity contract in other investments within invested assets. A corresponding liability representing the outstanding obligation to the claimant is recognized in insurance contracts.

Reinsurance

Reinsurance assets include the reinsurers' share of claims liabilities and unearned premiums. The Company reports third party reinsurance balances on the consolidated balance sheets on a gross basis to indicate the extent of credit risk related to third party reinsurance. The estimates for the reinsurers' share of claims liabilities are presented as an asset and are determined on a basis consistent with the related claims liabilities. Reinsurance assets are reviewed for impairment at each reporting date or more frequently when an indication of impairment arises during the reporting period.

Revenue recognition

Premiums and unearned premiums

Insurance premiums written are deferred as unearned premiums and recorded in income as the premium is earned on a straight line basis over the terms of the underlying policies, except on certain long term policies for which premiums are earned using an actuarial risk assessment that matches claim expectations. The portion of the premiums related to the unexpired term of the policy at the end of the year is reflected in unearned premiums.

Ceded Premiums and reinsurers' share of unearned premiums

The reinsurers' share of unearned premiums, net of a provision for doubtful amounts, is recognized as an asset at the same time and using principles consistent with the Company's method for determining the unearned premium liability.

Deferred policy acquisition costs

Commissions, premium taxes and general expenses incurred in the writing of premiums are deferred only to the extent that they are expected to be recovered from unearned premiums and are amortized to income as the related premiums are earned. If unearned premiums are not sufficient to pay expected claims and expenses, including policy maintenance expenses and unamortized policy acquisition costs, a premium deficiency is said to exist. Premium deficiency is recognized by a charge to income initially by writing down deferred policy acquisition costs. If the premium deficiency is greater than the deferred policy acquisition costs, a liability would be accrued for the excess deficiency.

Unearned commission

Unearned commissions are based on ceded premiums with a coverage period beyond the current year end. Unearned commissions are recognized as liabilities using principles consistent with the Company's method of determining policy acquisition costs.

Property and equipment

Property and equipment are recorded at cost less accumulated amortization and impairment. Amortization is provided over the estimated useful lives of the assets using the straight-line method over the following terms:

Furniture and equipment	3 years
Computer hardware	3 years

Intangible assets

Intangible assets with finite useful lives, comprised primarily of computer software, are recorded at cost less accumulated amortization and impairment. Amortization is provided over the estimated useful life of the asset (2-3 years) using the straight-line method. Intangible assets with indefinite lives are recorded at lower of cost and recoverable amount.

Impairment of non-financial assets

Property, plant and equipment and intangible assets are tested for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. For the purpose of measuring recoverable amounts, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units – or "CGUs"). Recoverable amount is the higher of an asset's fair value less costs to sell and value in use (being the present value of the expected future cash flows of the relevant asset or CGU, as determined by management).

The Company evaluates impairment losses, for potential reversals when events or circumstances warrant such consideration.

Employee benefits

The Company contributes to a group registered savings plan for employees as services are incurred. Contributions are charged to operating expenses. There are no other post-employment benefit expenses.

Income taxes

Income taxes are recognized in the consolidated statements of income and comprehensive income except to the extent that it relates to items recognized in OCI or directly in equity. In those cases, the related taxes are also recognized in OCI or directly in equity, respectively.

Current income tax is based on the results of the operations, adjusted for items that are not taxable or not deductible, that is payable for the current year. Current income tax is calculated based on income tax laws and rates enacted or substantively enacted as at the balance sheet date.

The Company follows the asset and liability method of accounting for income taxes, whereby deferred income tax assets and liabilities are recognized for the future income tax consequences attributable to differences between the carrying values of existing assets and liabilities and their respective income tax bases and taxable losses and tax credit carry-forwards. Deferred income tax assets and liabilities are measured using enacted or substantively enacted income tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in income tax rates on future income tax assets and liabilities is recognized in income or OCI or equity in the year which includes the date of enactment or substantive enactment. Deferred income tax assets are recognized only to the extent the realization of such assets is probable. Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income tax assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is intention to settle the balances on a net basis.

Stock-based compensation

The Company has a Stock Option Plan that provides for the issuance of shares of the Company's common stock not exceeding 10% of the total issued and outstanding shares (on a diluted basis) and shares reserved for issuance under the employee stock option plans, options for services and employee stock purchase plans.

The Company utilizes the fair-value-based method of accounting for stock based compensation. The fair value of stock based compensation determined using an option pricing model, is recorded over the vesting period as a charge to net earnings with a corresponding credit to contributed surplus. Awards are equity settled.

Stock options which contain a graded vesting feature (the total options granted vest on a graded basis such as annually over 5 years) are accounted for separately based on the date of vesting. At the time the options are granted, expected forfeiture rates are estimated and used to reduce the amount expensed over the life of the options. The estimated forfeiture rate is adjusted to actual forfeiture experience as information becomes available.

The Company has established a Share Unit Plan, under which the Board of Directors may from time to time determine (i) those eligible employees and directors (a "participant") who shall receive a grant of Restricted Share Units ("RSUs") and/or Performance Share Units ("PSUs") (RSUs and PSUs are collectively referred to as "Share Units"), (ii) the number of such RSUs and/or PSUs and (iii) the grant date(s) applicable to such RSUs and/or PSUs. Compensation expense and the related liability are recorded equally over the vesting period, taking into account fluctuations in the market price of the Company's share price.

Each Share Unit granted under the Share Unit Plan will entitle the participant, upon satisfying all applicable vesting criteria, to receive one common share or a cash payment equal to the market value of such share, calculated based on the weighted average trading price per common share on the Toronto Stock Exchange for the 5 trading days prior to a fixed date. The grant of a Share Unit will not entitle the participant to exercise any voting rights, or exercise any other right which attaches to ownership of common shares.

Grant date fair value of each Share Unit is calculated based on the weighted average trading price per common share on the Toronto Stock Exchange for the 5 trading days prior to a fixed date. The fair value of the Share Unit is re-measured each period for subsequent changes in the market value of common shares.

Members of the Board, who are not otherwise employees of the Company or any affiliate and are not employed by a corporation that holds at least 100,000 Shares of the Corporation, are eligible to participate in a Deferred Share Unit Incentive Plan, which allows them to elect to defer all or a portion of their annual retainer received in the form of Deferred Share Units (DSUs), each of which is equivalent in value to one common share of the Company. The number of DSUs is established by dividing the amount of retainers not paid in cash by the weighted average trading price of the Common Shares for the last 5 trading days preceding the determination. Whenever cash dividends are paid on the common shares, the director's account under the

DSU plan is credited with additional DSUs corresponding to the dividend paid on the common shares. The fair value of the DSUs is re-measured each period for subsequent changes in the market value of common shares.

Provisions

Provisions are recognized as liabilities when the Company has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Provisions are measured at management's best estimate of the expenditure required to settle the obligation at the end of the reporting period, and are discounted to present value where the effect is material. The Company performs evaluations to identify onerous contracts and, where applicable, records provisions for such contracts.

Share capital

Incremental costs directly attributable to the issuance of shares are recognized as a deduction from equity. The cost method is used to account for the shares purchased under a normal course issuer bid with the average cost of the shares reducing share capital and any excess recorded as a deduction to retained earnings.

Dividends

Dividends on common shares are recognized in the Company's consolidated financial statements in the year in which the dividends are approved by the Board of Directors.

Earnings per share

Basic earnings per share ("EPS") are calculated by dividing the net income (loss) for the year attributable to shareholders of the Company by the weighted average number of common shares outstanding during the year. Diluted EPS is calculated by adjusting the weighted average number of common shares outstanding for dilutive instruments. The number of shares included with respect to options, and similar instruments is computed using the treasury stock method. The Company's potentially dilutive common shares comprise stock options, DSUs and RSUs granted to employees and directors.

Standards, amendments and interpretations adopted or in effect

IFRS 15, Revenue from contracts with customers

IFRS 15, Revenue from contracts with customers deals with revenue recognition and establishes principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. The standard replaces IAS 18 'Revenue' and IAS 11 'Construction contracts' and related interpretations. The standard is effective for annual periods beginning on or after January 1, 2018. Revenue arising from insurance contracts and from financial instruments is outside the scope of IFRS 15. There are no other revenues arising from other sources of income.

Standards, amendments and interpretations not yet adopted or effective

IFRS 9, Financial Instruments

In July 2014, the IASB published the complete version of IFRS 9 which is effective for annual periods beginning on or after January 1, 2018, with retrospective application. The new standard includes requirements on the classification and measurement of financial assets and liabilities, an expected credit loss model that replaces the existing incurred loss impairment model, and new hedge accounting guidance. The Company has evaluated and meets the requirements to defer the adoption of IFRS 9, since the percentage of liabilities connected with insurance contracts over total liabilities is above the 90% threshold. The company has deferred adoption, until the new insurance contracts standard is adopted effective January 1, 2022.

IFRS 16, Leases

In January 2016, the IASB published IFRS 16, which is effective January 1, 2019. The new standard requires the capitalization of all leases by recognizing the present value of the lease payments and showing them as lease assets, and recognizing a financial liability representing an obligation to make future lease payments. The Company has evaluated the impact of IFRS 16 on its Consolidated Financial Statements, and the impact will be minimal on equity.

IFRS 17, Insurance Contracts

In May 2017, the IASB published IFRS 17 which is effective January 1, 2022, with retrospective application. The standard replaces IFRS 4. The standard is comprehensive in scope and addresses recognition, measurement, presentation and disclosure for insurance contracts. The standard requires the entity to recognize a group of insurance contracts it issues from the earliest of the following: (a) the beginning of the coverage period of the group of contracts; (b) the date when the first payment from a policyholder in the group becomes due; and (c) for a group of onerous contracts, when the group becomes onerous. The measurement approach is based on the following building blocks: (i) a current, unbiased probability-weighted estimate of future cash flows expected to arise as the insurer fulfills the contract; (ii) the effect of the time value of money; (iii) a risk adjustment that measures the effects of uncertainty about the amount and timing of future cash flows; and (iv) a contractual service margin which represents the unearned profit in a contract (that is recognized in net earnings as the insurer fulfills its performance obligations under the contract). Estimates are required to be re-measured each reporting period. In addition, a simplified measurement approach is permitted for short-duration contracts in which the coverage period is approximately one year or less. The Company is currently evaluating the impacts of IFRS 17 on its consolidated financial statements.

4 Critical accounting estimates and judgements

The preparation of the Company's consolidated 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.

Valuation of provisions for unpaid claims

Provision for unpaid claims are maintained to cover the Company's estimated ultimate liability for unpaid losses and loss adjustment expenses with respect to reported and unreported claims incurred as of the end of each accounting period. The provision for unpaid claims and adjustment expenses is first determined on a case-by-case basis as claims are reported and then reassessed as additional information becomes known. The provision also accounts for the future development of these claims, including claims incurred but not reported (IBNR). Provision for unpaid claims do not represent an exact calculation of liability, but instead represent estimates developed using projection techniques in accordance with Canadian accepted actuarial practice. These estimates are expectations of the ultimate cost of settlement and administration of claims based on the Company's assessment of facts and circumstances then known, its review of historical settlement patterns, estimates of trends in claims severity and frequency, legal theories of liability and other factors. The appointed actuary of the Company's subsidiaries, using appropriate actuarial techniques, evaluates the adequacy of the policy liabilities at the end of each reporting period.

Variables in the reserve estimation process can be affected by both internal and external events, such as changes in claims handling procedures, economic inflation, legal trends and legislative changes. Many of these items are not directly quantifiable, particularly on a prospective basis. Additionally, there may be significant reporting lags between the occurrence of the insured event and the time it is actually reported to the insurer. These estimates are refined in a systematic ongoing process as historical loss experience develops and additional claims are reported and settled. Because the establishment of reserves is an inherently uncertain process involving estimates, current reserves may not be sufficient. Adjustments to reserves, both positive and negative, are reflected in the consolidated statements of income and comprehensive income for the year in which such estimates are updated. Please see note 11.

Valuation of Reinsurer's share of provision for unpaid claims

Reinsurer's share of the provision for unpaid claims include amounts for expected recoveries related to provision for unpaid claims. Amounts recoverable from reinsurers are estimated in a manner consistent with claim and claim adjustment expense reserves. The ceding of an insurance liability to a reinsurer does not discharge the Company's primary liability to the policyholders. The Company's policy is to record an estimated allowance for doubtful accounts on the basis of periodic evaluations of balances due from reinsurers, reinsurer solvency, credit ratings of reinsurers, collateral held by the Company, management's experience and current economic conditions.

The Company is exposed to disputes on, and defects in, contracts with reinsurers and the possibility of default by reinsurers. Please see note 12.

Valuation of deferred tax asset

Deferred income taxes, accumulated as a result of temporary differences, which are probable to reverse, are included in the consolidated balance sheet. In addition, the consolidated statements of income and comprehensive income contains items that are non-taxable or non-deductible for income tax purposes, which cause the income tax provision to differ from what it would be if based on statutory rates. Recoverability of deferred tax assets is primarily based on current and expected profitability applicable to the Company and its ability to utilize any recorded tax assets taking into consideration of tax planning strategies and the expiry date of tax losses. Please see note 15.

5 Seasonality

The P&C insurance business is seasonal in nature. While net earned premiums reflect the premium volume from quarter to quarter, net underwriting income can be driven by weather conditions, which may vary significantly by quarter.

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

6 Investments

The following table provides a breakdown of the investment portfolio:

	Fair values	
Available-for-sale	**As at December 31, 2018**	**As at December 31, 2017**
Fixed income		
Canadian		
Federal	4,254	39,408
Provincial	3,047	29,883
Municipal	—	14
Corporate	4,592	127,701
	11,893	197,006
Fixed income lent through securities lending program		
Federal	—	63,864
Provincial	—	17,564
Municipal	—	1,322
Corporate	—	8,535
	—	91,285
Foreign fixed income		
Corporate	—	2,014
	—	2,014
Total fixed income	11,893	290,305
Corporate value pooled fund	4,998	—
Money market pooled funds	459	1,014
Short-term fixed income and mortgage pooled funds	14,610	19,303
Specialty pooled fund	—	8,240
Total pooled funds	20,067	28,557
Common shares		
Canadian	1,138	889
Foreign	1,481	1,043
Global Equity Pooled Fund	7,417	7,385
Total common shares	10,036	9,317
Total available-for-sale	41,996	328,179
Fair value through profit or loss		
Preferred shares	3,580	42,754
Total preferred shares	3,580	42,754
Total investments	45,576	370,933
Cash and short-term deposits	22,785	44,459
Total investments including cash and short-term deposits	68,361	415,392

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 December 31, 2018, the Company had nil collateral in continued operations (December 31, 2017 – $98,798).

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 technique employed has remained the same from December 31, 2017. 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, commercial mortgage pooled funds, money market pooled funds 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 rationality 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.

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

The following table provides the classification of the Company's investments within the fair value hierarchy, as outlined, as at December 31, 2018 and December 31, 2017:

December 31, 2018	**Level 1**	**Level 2**	**Level 3**	**Total**
Fixed income	—	11,893	—	11,893
Corporate value pooled funds	—	4,998	—	4,998
Money market pooled funds	—	459	—	459
Short-term fixed income and mortgage pooled funds	—	14,610	—	14,610
Global Equity Pooled Fund	—	7,417	—	7,417
Common Shares	2,619		—	2,619
Preferred Shares	3,580	—	—	3,580
	6,199	39,377	—	45,576

December 31, 2017	**Level 1**	**Level 2**	**Level 3**	**Total**
Fixed income	—	290,305	—	290,305
Money market pooled funds	—	1,014	—	1,014
Short-term fixed income and mortgage pooled funds	—	19,303	—	19,303
Specialty pooled fund	—	—	8,240	8,240
Common Shares	1,932	7,385	—	9,317
Preferred Shares	42,754	—	—	42,754
	44,686	318,007	8,240	370,933

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. There were no transfers from the existing portfolio for the year ended December 31, 2018 or 2017.

The fair values of cash and short-term deposits, account receivables and financial liabilities approximate their carrying values due to their short-term nature.

The Company has interests in unconsolidated structured entities, through investments in pooled funds, which are included in investments on the balance sheet. These entities are not controlled by the Company. The carrying value of pooled funds and maximum exposure to loss as of December 31, 2018 was $27,484 (December 31, 2017 – $28,557). Investments in pooled funds consist of units invested in underlying money market and mortgage securities managed by third-party managers in addition to units invested in a Global Equity Pooled Fund. The pooled funds are perpetual private trusts created under trust agreements. Financing is only provided to the pooled funds through the purchase of units and is therefore limited to the investment made.

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

Impaired assets and provisions for losses

A gross unrealized loss of $886 on Available for Sale (AFS) investments at December 31, 2018 (December 31, 2017 – $3,326) is recorded, net of tax, in the amount of $663 (December 31, 2017 – $2,415) in Accumulated Other Comprehensive Income, primarily due to the impact of higher government bond yields on the Company's fixed income portfolio.

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 records the difference between the amortized cost of the financial assets and its fair value as an impairment which reduces investment income recorded in the year.

Impairments of $129 on AFS investments were recognized for the year ended December 31, 2018 (December 31, 2017 - nil).

Investment income

The table below provides additional details on net investment income for the year ended December 31, 2018 and December 31, 2017:

	2018	2017
Interest income	1,741	1,665
Dividend income	626	277
Net realized losses	(279)	(176)
Impairment loss recognized on AFS investment	(129)	—
Fair value change on FVTPL investments	(338)	410
Realized and unrealized foreign exchange gains	63	4,896
Investment expenses	(221)	(163)
Investment income	1,463	6,909

7 Loan receivable

The loan outstanding amount from New Nordic for the sale of Qudos was repaid in full on June 29, 2018.

8 Line of credit

For the year ended December 31, 2018, the Company has expensed nil on the income statement, related to the maintenance of the credit facility (December 31, 2017 – $0.2 million).

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

9 Deferred policy acquisition costs (DPAC)

Commissions, premium taxes and general expenses incurred in the writing of premiums are deferred in accordance with the Accounting Policy set out in Note 3.

A reconciliation of DPAC is shown below as at December 31:

	2018		2017	
	Gross	**Ceded**	**Gross**	**Ceded**
Balance at the beginning of the year	40,888	1,667	30,689	2,288
Acquisition costs during the year	7,315	129	68,258	5,444
Amortization of acquisition costs during the year	(7,145)	(82)	(58,059)	(6,065)
Discontinued operations	(37,063)	(1,535)	—	—
Acquisition costs deferred at end of the year	3,995	179	40,888	1,667

10 Unearned premiums

The following table shows unearned premiums by line of business and nature of risk as at December 31:

	2018		2017	
	Gross	**Ceded**	**Gross**	**Ceded**
Automobile				
– accident benefits	1,191	84	18,122	562
– liability	6,028	431	52,882	2,758
– other	4,670	372	31,393	587
Property				
– commercial	1,830	213	8,732	538
– personal	2,003	233	42,395	4,650
Liability	991	80	3,607	103
Accident and sickness	—	—	116	—
Surety	—	—	2,812	538
Other	135	109	518	221
	16,848	1,522	160,577	9,957

A reconciliation of unearned premium is shown below as at December 31:

	2018		2017	
	Gross	**Ceded**	**Gross**	**Ceded**
Unearned premium at the beginning of the year	160,577	9,957	120,184	8,975
Premium written and ceded during the year	33,937	3,406	285,718	18,911
Premium earned in income	(33,281)	(3,344)	(245,325)	(17,929)
Discontinued operations	(144,385)	(8,497)	—	—
Unearned premium at the end of the year	16,848	1,522	160,577	9,957

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

11 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 discounts future cash flows and includes a margin for adverse deviation.

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 investment portfolio has experienced an increase in yields compared to December 31, 2017. The Company discounts its best estimate as follows which is for all lines of business within the reporting entity:

Entity	December 31, 2018	December 31, 2017
ICPEI	3.67%	2.80%

The Company recorded a $1,835 addition to the net provision for unpaid claims relating to favourable development in prior years' estimates (December 31, 2017 – $25,745).

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 net basis by $1,484 as at December 31, 2018 (December 31, 2017 – $19,349).

The provision for unpaid claims on an actuarial present value (APV) gross and ceded basis by line of business is shown below as at December 31:

	2018		2017	
	Gross	Ceded	Gross	Ceded
Automobile				
– accident benefits	3,012	601	94,675	14,135
– liability	14,602	2,783	120,762	6,715
– other	2,831	1,303	11,061	209
Property				
– commercial	711	77	5,508	611
– personal	1,286	10	10,051	620
Liability	1,838	98	18,051	563
Accident and sickness	—	—	1,182	318
Commercial Auto	—	—	75	—
Surety	—	—	1,361	300
Other (PFAD and discounting)	(190)	17	240	—
Total unpaid claims	24,090	4,889	262,966	23,471

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

Claims development

The table below provides additional details on the provision for unpaid claims as at December 31, 2018 and December 31, 2017:

Provision for unpaid claims analysis	December 31, 2018	December 31, 2017
Unpaid claims, beginning of year, net	239,495	228,106
Favourable prior year claims development	(1,835)	(25,745)
Net claims incurred in current year	21,278	179,305
Paid on claims occurring during		
Current year	(13,798)	(79,120)
Prior year	(6,311)	(63,051)
Discontinued Operations	(219,628)	—
Unpaid claims, end of year, net	19,201	239,495
Reinsurers’ share	4,889	23,471
Gross unpaid claims	24,090	262,966

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 judgement 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 year as having a potential or identifiable material impact on the overall claims estimate.

Claims development table, net of reinsurance

The following tables show the estimates of cumulative incurred claims, including IBNR, with subsequent developments during the periods and together with cumulative payments to date. The original reserve estimates are evaluated quarterly for redundancy or deficiency. The evaluation is based on actual payments in full or partial settlement of claims and current estimates of claims liabilities for claims still unreported.

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

Claims development table, net of reinsurance

	Accident Year									
	2009	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**
Net ultimate loss at the end of:	11,088	11,445	14,434	10,895	13,460	17,537	16,808	12,631	15,563	17,969
1 year later	9,868	10,653	13,979	10,736	12,772	15,377	14,966	12,130	14,956	
2 years later	9,234	10,328	13,673	10,205	12,768	14,925	14,914	12,127		
3 years later	8,643	10,348	14,359	9,886	12,803	15,125	14,982			
4 years later	8,582	10,209	13,714	9,866	12,911	15,102				
5 years later	8,840	10,207	14,005	9,627	12,900					
6 years later	8,797	10,289	14,049	9,392						
7 years later	8,852	10,126	13,955							
8 years later	8,921	10,177								
9 years later	9,044									
Cumulative favourable loss development	(2,044)	(1,268)	(479)	(1,503)	(560)	(2,435)	(1,826)	(504)	(607)	
Cumulative loss development as a % of original ultimate loss	(18.43)%	(11.08)%	(3.32)%	(13.80)%	(4.16)%	(13.88)%	(10.86)%	(3.99)%	(3.90)%	

	Accident Year										
	2009	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**Total**
Current estimate of net ultimate loss	9,044	10,177	13,955	9,392	12,900	15,102	14,982	12,127	14,956	17,969	
Cumulative paid	(8,911)	(10,043)	(13,531)	(8,972)	(12,088)	(13,428)	(12,218)	(10,233)	(11,899)	(11,190)	
Net provision of unpaid claims by recent accident years	133	134	424	420	812	1,674	2,764	1,894	3,057	6,779	18,091
Other reconciling Items											(182)
Net provision for unpaid claims											17,909

The provision for unpaid claims relating to the and Discontinued Canadian and Discontinued International operations, was treated as paid in the development table above.

12 Underwriting policy and reinsurance ceded

In the normal course of business, the Company seeks to reduce the loss that may arise from catastrophes or other large loss events by purchasing reinsurance to share all or part of the insurance risks originally accepted by the Company in writing premiums. This does not relieve the Company of its primary obligation to policyholders.

During 2018, the Company followed the policy of underwriting and reinsuring contracts of insurance, which limits the net exposure of the Company to a maximum amount on any one loss to $500 (2017 – $500). In addition, the Company obtained catastrophe reinsurance which limits the loss from a series of claims arising from a single occurrence to $500 (2017 – $500), to a maximum coverage of $99,500 (2017 – $89,500).

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

The Company places all its automobile reinsurance with registered reinsurers.

Failure of reinsurers to honour their obligations could result in losses to the Company. Consequently, the Company continually evaluates the financial condition of its reinsurers and monitors concentrations of credit risk to minimize its exposure to significant losses. There have been no defaults and no provision made in the accounts for defaults based on management's review of the creditworthiness of its reinsurers.

Reinsurance recoverable

The following tables summarize the balances outstanding from reinsurers, by risk rating, as at December 31:

December 31, 2018			
Credit rating	**Gross reinsurance recoverable**	**Less: Deposits held in trust**	**Net exposure**
A or higher	4,529	—	4,529
Not rated	1,882	—	1,882
	6,411	—	6,411

December 31, 2017			
Credit rating	**Gross reinsurance recoverable**	**Less: Deposits held in trust**	**Net exposure**
A or higher	32,582	—	32,582
Not rated	1,355	1,221	134
	33,937	1,221	32,716

Included in gross reinsurance recoverable is reinsurers' share of unearned premiums of $1,522 (December 31, 2017 – $9,957), reinsurers' share of provision for unpaid claims of $4,889 (December 31, 2017 – $23,471), and receivables from reinsurers presented as due from insurance companies of $0 (December 31, 2017 – $510). No balances due from reinsurers are considered past due as at December 31, 2018 and 2017. There is no valuation allowance or amounts written off during the years ended December 31, 2018 and 2017.

13 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 foreign exchange risk.

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.

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

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.

Direct Written Premium	December 31, 2018	December 31, 2017
Lines		
Automobiles	71%	70%
Property	29%	30%
Regions		
New Brunswick	29%	30%
Nova Scotia	40%	38%
Prince Edward Island	31%	32%

Sensitivity to insurance risk

The table below shows the sensitivity of earnings from operations before income taxes and total equity after giving effect to a one percentage point increase in the loss ratio and claims settlement costs. The loss ratio is regarded as a non-IFRS measure and is calculated by the Company with respect to its ongoing insurance operations as losses on claims incurred (including losses and loss adjustment expenses) expressed as a percentage of net premiums earned. Such an increase could arise from higher frequency of losses, increased severity of losses, or from a combination of both. The sensitivity analysis presented below does not consider the probability of such losses to loss frequency or severity occurring or any non-linear effects of reinsurance and, as a result, each additional percentage point increase in the loss ratio would result in a linear impact on earnings from operations before income taxes and total equity.

	December 31, 2018		December 31, 2017	
Sensitivity Factor	Net income before income taxes	Shareholders' equity	Net income before income taxes	Shareholders' equity
Increase of 1% to loss ratio	(299)	(209)	(281)	(196)
Increase of 1% to claims settlement costs	(192)	(134)	(199)	(139)

Product and pricing

The Company prices its products taking into account numerous factors, including claims frequency and severity trends, product line expense ratios, special risk factors, the capital required to support the product line, and the investment income earned on that capital. The Company's pricing process is designed to ensure an appropriate return on capital and long-term rate stability avoiding wide fluctuations in rates, unless necessary. These factors are reviewed and adjusted periodically to ensure they reflect the current environment.

Pricing for automobile insurance must be submitted to each provincial government regulator and, in certain provinces, pre-approved by the regulator. Regulatory decisions may impede automobile rate increases or other actions that the Company may wish to take. Also, during periods of intense competition for any product line, to gain market share, the Company's competitors may price their products below the rates the Company considers acceptable. Although the Company may adjust its pricing up or down to maintain a competitive position, the Company strives to ensure its pricing will produce an appropriate return on invested capital. There is no assurance that the Company will not lose market share during periods of pricing competition.

Underwriting and claims

The Company is exposed to loss resulting from the underwriting of risks being insured and the exposure to financial loss resulting from greater than anticipated adjudication, settlement and claims costs.

The Company's underwriting objectives are to develop business within target markets on a prudent and diversified basis and to achieve profitable underwriting results. The Company underwrites automobile business after a review of the applicant's driving record and claims experience. Specialty commercial and personal risks are selected by the Company, working with its external brokers, after consideration of various risk factors associated with these lines of business. Despite its best efforts, and consideration of all known risk factors, there can be no assurance that all risks associated with the insurance policies that it writes can be identified and assessed, and the Company may, therefore, experience increased adjudication, settlement and claims costs.

The Company estimates its claims reserves on a quarterly basis and this is supported by quarterly assessments by the independent appointed actuary. Every quarter, for each line of business, the Company compares actual and expected claims development. To the extent that actual results differ from expected development, assumptions are re-evaluated and new estimates are derived. Although the Company believes its overall provision levels to be adequate to satisfy its obligations under existing policies, actual losses may deviate, perhaps substantially, from the amounts reflected in the Company's consolidated financial statements. To the extent provisions prove to be inadequate, the Company would have to re-evaluate such provisions and may incur a charge to earnings in the future.

Unpredictable catastrophic events

Catastrophes can be caused by various natural and unnatural events. Natural catastrophic events include hurricanes, windstorms, earthquakes, hailstorms, explosions, severe winter weather and fires. Unnatural catastrophic events include hostilities, terrorist acts, riots, crashes and derailments. The incidence and severity of catastrophes are inherently unpredictable. The extent of losses from a catastrophe is a function of both the total amount of insured exposure in the area affected by the event and the severity of the event. Most catastrophes are restricted to small geographic areas; however, hurricanes, windstorms and earthquakes may produce significant damage in large, heavily populated areas.

Catastrophes can cause losses in a variety of business lines. Claims resulting from natural or unnatural catastrophic events could cause substantial volatility in the Company's financial results and could materially reduce the Company's profitability or harm the Company's financial condition. The Company manages the impact of losses which may result from catastrophic events by purchasing excess of loss and catastrophe reinsurance to share all or part of the insurance risks originally accepted by the Company as well as geographic diversification.

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

Asset and liability matching

The Company is exposed to:

- changes in the value of its fixed income investments and policy liabilities to the extent that market interest rates change;
- equity price fluctuations, which affect the fair values of equities held by the Company;
- the risk of losses to the extent that the sale of an investment prior to its maturity is required to provide liquidity to satisfy policyholder and other cash outflows;
- the risk that future inflation of policyholder cash flows exceed returns on long-term investments; and
- foreign exchange risks with respect to investments, derivatives, receivables and policy liabilities denominated in foreign currencies.

The Company's exposures are monitored on a regular basis and actions are taken to balance investment positions when approved risk tolerance limits are exceeded.

Risk management is carried out by the Audit and Risk Committee under policies approved by the Board of Directors.

Market risk

Market risk is the risk of loss arising from adverse changes in market rates and prices, such as interest rates, equity market fluctuations, foreign exchange rates and other relevant market rate or price changes. Market risk is directly influenced by the volatility and liquidity in the markets in which the related underlying financial assets are traded. Below is a discussion of the Company’s primary market risk exposures and how these exposures are currently managed.

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 other comprehensive income ("OCI") relating to the fixed income investment portfolio as at December 31, 2018, and December 31, 2017, based on parallel 200 basis point shifts in interest rates up and down in 100 basis point increments.

Change in interest rates As at December 31, 2018	Fair value of fixed income	Hypothetical change on fair value	Effect on OCI net of tax
200 basis point rise	30,353	(5)%	(1,120)
100 basis point rise	31,156	(3)%	(560)
No change	31,960	—	—
100 basis point decline	32,763	3 %	560
200 basis point decline	33,567	5 %	1,120

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

Change in interest rates As at December 31, 2017	Fair value of fixed income	Hypothetical change on fair value	Effect on OCI net of tax
200 basis point rise	30,221	(5)%	(1,206)
100 basis point rise	31,086	(3)%	(603)
No change	31,952	—	—
100 basis point decline	32,817	3 %	603
200 basis point decline	33,683	5 %	1,206

As discussed in note 11, the discount rate used in the determination of the provision for unpaid claims is based on the expected return of assets on its investment portfolio with appropriate assumptions for interest rates relating to reinvestment of maturing investments. Fluctuations in market interest rates will therefore have an impact on the discount rate used in the valuation of the net provision for unpaid claims. The table below shows the potential impact of interest rate fluctuations on the net provision for unpaid claims and income statement:

Change in discount rate	Net provision for unpaid claims	Hypothetical change in value	Effect on net income net of tax
As at December 31, 2018			
100 basis point rise	18,740	(2)%	(321)
No change	19,200	—%	—
100 basis point decline	19,677	2%	333
As at December 31, 2017			
100 basis point rise	234,437	(2)%	(3,692)
No change	239,495	—%	—
100 basis point decline	244,807	2%	3,878

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 are as follows, as at December 31, 2018 and December 31, 2017:

December 31, 2018	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Bonds	161	2,975	5,921	2,836	11,893
Cash and cash equivalents	22,785	—	—	—	22,785
Accounts receivable	11,738	—	—	—	11,738
Total	34,684	2,975	5,921	2,836	46,416
Percentage of total	75%	6%	13%	6%	100%

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

December 31, 2017	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Bonds	24,001	117,230	84,152	64,922	290,305
Cash and cash equivalents	44,459	—	—	—	44,459
Accounts receivable	82,175	—	—	—	82,175
Total	150,635	117,230	84,152	64,922	416,939
Percentage of total	36%	28%	20%	16%	100%

The following tables summarize the expected timing of cash flows arising from insurance obligations, on an undiscounted basis, as at December 31, 2018 and December 31, 2017:

December 31, 2018	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Gross claim liabilities (undiscounted)	9,038	7,725	3,878	3,638	24,279
Less: Reinsurance recoverable (undiscounted)	1,982	1,752	723	415	4,872
Net actuarial liabilities	7,056	5,973	3,155	3,223	19,407

December 31, 2017	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Gross claim liabilities (undiscounted)	93,874	89,302	46,779	25,803	255,758
Less: Reinsurance recoverable (undiscounted)	10,877	7,758	2,661	1,464	22,760
Net actuarial liabilities	82,997	81,544	44,118	24,339	232,998

All other financial assets and liabilities are for a duration of one year or less. The contractual maturities for lease commitments are listed in note 20.

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.

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

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 twelve months ended December 31, 2018, and the year ended December 31, 2017. 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 (loss) net of tax**		**Effect on OCI net of tax**	
	December 31, 2018	December 31, 2017	December 31, 2018	December 31, 2017
10% rise	249	288	21	24
10% decline	(249)	(288)	(21)	(24)

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's maximum exposure to credit risk, without taking into account amounts held as collateral, is:

	As at December 31, 2018	**As at December 31, 2017**
Bonds	11,893	290,305
Gross reinsurance recoverable	6,411	32,582
Accounts receivable	11,738	75,622
Structured settlements (note 21)	868	36,472
Cash	22,785	44,459
Total	53,695	479,440

(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 December 31:

Fixed income portfolio

A breakdown of the fixed income portfolio by credit rating is shown below:

	As at December 31, 2018		As at December 31, 2017	
	Fair value	**%**	**Fair value**	**%**
AAA	5,347	45%	125,595	43%
AA	2,211	19%	50,040	17%
A	3,483	29%	81,816	28%
BBB	852	7%	28,156	10%
BB	—	—%	1,420	1%
B and lower	—	—%	1,925	1%
Unrated	—	—%	1,353	—%
Total	11,893	100%	290,305	100%

Preferred share portfolio

A breakdown of the preferred shares portfolio by credit rating is shown below:

	As at December 31, 2018		As at December 31, 2017	
	Fair value	**%**	**Fair value**	**%**
P2	3,137	88%	36,335	85%
P3	443	12%	6,419	15%
Total	3,580	100%	42,754	100%

Capital management

Capital is comprised of the Company's total equity. As at December 31, 2018, the Company's equity was $145,667 (December 31, 2017 – $142,822).

The Company's objectives when managing capital consists of:

- Maintaining capital to be above minimum regulatory levels,
- Ensuring capital is above internally determined risk management levels,
- Maintaining creditworthiness, financial strength and protect its claims paying abilities.
- Maximizing returns to shareholders over the long term.

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

14 Intangible assets

A reconciliation of the movement in Intangible Assets is shown below, as at December 31, 2018 and December 31, 2017:

	Opening cost	Additions	Disposals	Assets held for sale	End of year cost	Accumulated amortization	Net
Software							
December 31, 2018	33,210	5,838	—	9,200	29,848	29,848	—
December 31, 2017	28,712	4,498	—	—	33,210	25,573	7,637
Goodwill							
December 31, 2018	400	—	—	400	—	—	—
December 31, 2017	400	—	—	—	400	—	400
Total intangible assets							
December 31, 2018	33,610	5,838	—	9,600	29,848	29,848	—
December 31, 2017	29,112	4,498	—	—	33,610	25,573	8,037

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

15 Income taxes

The income tax is as follows for the year ended December 31, 2018 and December 31, 2017:

	2018	2017
Current	(349)	(665)
Deferred	(254)	(40)
	(603)	(705)

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 company's effective tax rate in 2018 reflects the recognition of a deferred tax asset from the utilization of capital losses through the transfer of information technology assets. The capital losses arose from the sale of Qudos.

The difference is broken down as follows:

	2018	2017
Income tax expense calculated at statutory rates	27.0 %	27.0 %
Increase (decrease) in income tax rates resulting from:		
Non-taxable dividend income	2.0 %	1.6 %
Non-taxable (income) loss	(0.4)%	— %
Non-deductible expenses	(0.1)%	(0.1)%
Tax benefit of losses not previously recognized	(9.6)%	— %
Tax benefit of losses previously recognized	— %	(25.5)%
Statutory rate differences	0.3 %	0.9 %
Non-taxable portion of capital gains	— %	9.6 %
Other	0.9 %	1.5 %
Effective income tax rate	20.1 %	15.0 %

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

Deferred income taxes are comprised of the following as at December 31:

	Losses Carried Forward	Reserves	Investments	Property, equipment and intangible assets	Total
Balance - January 1, 2018	129	4,680	(23)	1,048	5,834
Amounts recorded in discontinued operations	—	(5,272)	22	(522)	(5,772)
Amounts recorded in the income statement	(128)	1,375	1	(529)	719
Balance - December 31, 2018	1	783	—	(3)	781

	Losses Carried Forward	Reserves	Investments	Property, equipment and intangible assets	Total
Balance - January 1, 2017	355	4,689	(25)	841	5,860
Amounts recorded in the income statement	(226)	(9)	2	207	(26)
Balance - December 31, 2017	129	4,680	(23)	1,048	5,834

Management reviews the recoverability of the deferred income tax asset on an ongoing basis and adjusts as necessary, to reflect its anticipated realization. Management expects that the recorded deferred income tax asset will be realized in the normal course of operations.

The Company has tax losses available resulting from capital losses of $39,222. Deferred tax assets have not been setup on $7,140 of this amount as there is no certain probability that these losses will be utilized.

Income taxes included in OCI

The amounts included in the consolidated statements of comprehensive income are shown net of the following tax benefit, for the years ended December 31:

	2018	2017
Change in unrealized gains	(82)	(124)
Reclassification to net income of (gains) and losses	79	(565)
Total income tax expense included in OCI	(3)	(689)

Income taxes payable are expected to be settled within one year of the financial statement date.

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

16 Share capital

	As at December 31, 2018	As at December 31, 2017
Authorized		
Unlimited common shares (no par value)		
Unlimited special shares issuable in Series (no par value)		
Issued		
11,925,906 common shares (December 31, 2017 – 11,891,076 common shares)	71,997	71,520

In 2018, 2,000 common shares (2017 – 63,006) were issued for the exercise of stock options and 32,830 common shares (2017 – 80,334) were issued pursuant to the Share Unit Plan for eligible employees with a value of $477 (2017 – $1,293).

17 Employee stock option plan

For the year ended December 31, 2018, the Company recorded a compensation expense of $101 (2017 – $73), with an offsetting credit to contributed surplus in relation to its stock option plan. Stock options granted have varying vesting periods. It also recorded an expense of $720 (2017 – $899) in relation to its Share Unit Plan and Options.

The following is a continuity schedule of stock options outstanding as at December 31.

	Number of options		Weighted average exercise price per share	
	2018	2017	2018	2017
Outstanding, beginning of year	400,308	202,350	11.83	8.27
Granted during year	—	299,308	—	12.9
Exercised during year	(16,625)	(87,350)	8.68	7.77
Canceled during year	(6,500)	(12,000)	8.89	8.89
Expired during year	—	(2,000)	—	7.19
Outstanding, end of year	377,183	400,308	12.02	11.83

The outstanding stock options consist of the following, as at December 31, 2018:

Stock Option price per share	Number	Average remaining contractual life	Number of options exercisable
$8.90-13.16	284,683	6.5	—
$8.01-$8.89	71,500	1.1	92,625
$7.18-$8.00	21,000	1.25	23,000

The weighted average grant-date fair value per share option to date is $1.90.

Restricted share unit (RSU) plan

The restricted share units are share-settled awards for which the provision recorded as at December 31, 2018 was $516 (2017 – $613).

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

18 Related party transactions

Key management

Key management includes named executive officers. Compensation to these individuals are summarized in the following table for the year ending December 31:

Compensation	**2018**	**2017**
Salaries and other short-term benefits	3,140	1,766
Equity-settled and cash-settled compensation benefits	—	1,069
	3,140	2,835

19 Operating Costs by nature

The table below presents operating costs by major category for the year ended December 31, 2018 and December 31, 2017:

	2018	**2017**
Salaries and benefits	2,169	2,046
Systems costs	455	441
Professional fees	3,501	1,977
Occupancy	178	174
Printing and Postage	235	264
Facility	385	293
Other expenses	975	820
	7,898	6,015

20 Operating lease commitments

The Company is committed under lease agreements for office and property operating leases with minimum lease payments of $11,628 as at December 31, 2018:

Lease commitments	
2019	2,235
2020	1,989
2021	1,969
2022	1,737
2023	1,441
2024 and thereafter	2,257
	11,628

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

21 Structured settlements

In the normal course of claims adjudication, the Company may settle certain long-term losses through the purchase of annuities (structured settlements) from life insurance companies. The fair estimated value of these annuity contracts amounts to $868 (December 31, 2017 – $36,472) using a discount rate of 2.18% (December 31, 2017 – 2.26%). It is the policy of the Company to purchase annuities from life insurers with proven financial stability. The net risk to the Company is the credit risk related to the life insurance companies and this risk is reduced to the extent of coverage provided by Assuris, the life insurance compensation insurance plan. The Company has determined that no credit risk provision is required.

22 Contingencies

From time to time, in connection with its insurance operations, the Company is named as a defendant in actions for damages and costs allegedly sustained by the plaintiffs. While it is not possible to estimate the outcome, such actions have generally been resolved with minimal damage or expense in excess of amounts provided as policy liabilities. The Company does not believe that it will incur any significant additional loss or expense in connection with such actions.

On October 29, 2018, the company filed a Statement of Defence in response to a claim filed with the Danish Institute of Arbitration by New Nordic Advisors Limited (NNAL). The claim by NNAL relates to the sale of the Company's European Operations to NNAL. The Company denies all allegations made against it by NNAL and believes there is no merit to NNAL's claim for €45.8 million in damages.

23 Rate regulations

The Company writes business subject to rate regulation, which comprises approximately 71% (2017 — 70%) of gross premiums written and assumed. The Company's automobile insurance premiums can be impacted by mandatory rate rollbacks and mandatory rate assessments as legislated by provincial law and by regulation in certain provinces. This could result in lower future premium rates or reductions to premium rates charged by the Company in prior years. In addition, the Company is required, under certain provincial legislation, to participate in risk sharing pools, which may impact positively or negatively on underwriting results. Certain benefit payments are also subject to provincial government regulation, including automobile accident benefits.

24 Accumulated other comprehensive income

A breakdown of the accumulated other comprehensive income is shown below as at December 31, 2018 and December 31, 2017:

	As at December 31, 2018	**As at December 31, 2017**
Gross unrealized losses	(3,877)	(3,966)
Foreign currency translation adjustments	453	499
Tax impact	547	634
Ending balance	(2,877)	(2,833)

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

25 Earnings per share

The table below presents earnings per share as at December 31, 2018, and December 31, 2017:

Earnings Per Share on Continued Operations	**2018**	**2017**
Basic earnings per share on continued operations:		
Net (loss)income available to shareholders	(2,419)	4,618
Average number of common shares	11,908	11,819
Basic (loss) earnings per share on continued operations	$(0.20)	$0.39
Diluted earnings per share:		
Average number of common shares	11,908	11,819
Average number of dilutive common shares under employee stock compensation plan	293	249
Average number of diluted common shares	12,201	12,068
Diluted (loss) earnings per share on continued operations	$(0.20)	$0.38

Earnings Per Share on Discontinued Operations	**2018**	**2017**
Basic (loss) per share on discontinued operations:		
Net income(loss) available to shareholders	4,776	(2,984)
Average number of common shares	11,908	11,819
Basic earnings (loss) per share on discontinued operations	$0.40	$(0.25)
Diluted earnings per share:		
Average number of common shares	11,908	11,819
Average number of dilutive common shares under employee stock compensation plan	293	249
Average number of diluted common shares	12,201	12,068
Diluted earnings(loss) per share on discontinued operations	$0.39	$(0.25)

Total Earnings Per Share	**2018**	**2017**
Basic earnings per share:		
Net income available to shareholders	2,357	1,634
Average number of common shares	11,908	11,819
Basic earnings per share	$0.20	$0.14
Diluted earnings per share:		
Average number of common shares	11,908	11,819
Average number of dilutive common shares under employee stock compensation plan	293	249
Average number of diluted common shares	12,201	12,068
Diluted earnings per share	$0.19	$0.14

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

26 Held for sale classification and discontinued operations

On August 4, 2016, Echelon entered into a definitive stock purchase agreement to sell Qudos, subject to regulatory approval. On February 28, 2017, regulatory approval was received from the Danish Financial Supervisory Authority, which completed the necessary approvals required for the sale. The Company completed the sale on March 7, 2017, and retains no residual insurance risk or other financial risk, other than credit risk associated with the loan receivable from the sale. The loan was repaid on June 29, 2018.

On November 9, 2018, the Company entered into a definitive agreement to sell it's Discontinued Canadian Operations. The agreement was approved by the Company's shareholders on January 23, 2019 and is now subject to regulatory approval.

Assets and liabilities of the disposal group held for sale

The assets and liabilities of the disposal group classified as held for sale included in the consolidated balance sheet as at December 31, 2018 were as follows:

	As at December 31, 2018
Assets of the disposal group held for sale	
Cash and short-term deposits	106,819
Investments	282,662
Accounts Receivable	92,619
Deferred policy acquisition costs	49,002
Reinsurers' share -unpaid claims	12,032
Reinsurer share-unearned premiums	10,453
Property Plant and Equipment	1,064
Intangible assets	9,600
All other assets	12,482
Total assets of disposal group held for sale	576,733
Liabilities of the disposal group held for sale	
Accounts payable and accrued liabilities	16,262
Unearned premiums	192,479
Provision for unpaid claims	253,921
All other liabilities	2,771
Total liabilities of disposal group held for sale	465,433

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

Net income (loss) from discontinued operations

The table below presents results of discontinued operations for the year ended December 31, 2018 and December 31, 2017:

	2018	2017
Revenue		
Gross written and assumed premiums	351,495	269,125
Net written premium	340,835	250,248
Decrease in provision for unearned premium	(46,137)	(31,963)
Net earned premiums	294,698	218,285
Investment Income (loss)	5,690	(275)
Total revenue	300,388	218,010
Expenses		
Net incurred claims	191,347	149,101
Net acquisition costs	70,988	51,222
Operating costs	31,180	26,477
Transaction cost	5,941	—
Total expenses	299,456	226,800
Profit (Loss) before income taxes	932	(8,790)
Impact of change in discount rate on claims	5,653	3,020
Interest expense	—	155
Income tax expense (recovery)	1,809	(397)
Net Income (loss) on discontinued operations	4,776	(5,528)
Revaluation of the net assets of disposal group held for sale	—	2,544
Net Income (loss) on discontinued operations	4,776	(2,984)
Other comprehensive income on discontinued operations	233	5,867
Comprehensive income on discontinued operations	5,009	2,883

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

27 Non-controlling interest

The Company has non-controlling interests attributable to the subsidiary of ICPEI. Please refer to Note 1. The following tables summarize the comprehensive income attributable to the non-controlling shareholders for the year ended December 31, 2018 and December 31, 2017:

	2018	**2017**
Revenue		
Gross written and assumed premiums	8,484	8,122
Net earned premiums	7,484	7,017
Investment income	199	351
Total revenue	7,683	7,368
Expenses		
Net incurred claims	4,861	4,468
Net acquisition costs	1,766	1,757
Operating costs	1,054	942
Total expenses	7,681	7,167
income before income taxes	2	201
Income tax expense (recovery)	(16)	47
Net income attributable to NCI	18	154
Other comprehensive loss attributable to NCI	(4)	(67)
Comprehensive income attributable to NCI	14	87

The following tables summarize the net assets of the non-controlling shareholders as at December 31, 2018 and December 31, 2017:

	December 31, 2018	**December 31, 2017**
Assets		
Cash and investments	9,294	9,430
Other assets	5,640	5,018
Total assets	14,934	14,448
Liabilities		
Unearned premium	4,212	4,048
Unpaid claims	6,023	6,062
Other liabilities	857	510
Total liabilities	11,092	10,620
Equity		
Share capital	—	—
AOCI	(115)	(109)
Retained earnings	3,957	3,937
Total equity	3,842	3,828
Total liabilities and equity	14,934	14,448

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

The prior year equity balance in the previous table excludes discontinued operations, and will therefore differ from the non-controlling interest amount disclosed on the balance sheet of these financial statements.

	As at December 31, 2018	As at December 31, 2017
Cash flow from operating activities	36	70
Cash flow from investing activities	(30)	(720)
Net (decrease) Increase in cash and short-term deposits	6	(650)

28 Segmented information

The Company operates through two segments: Personal Lines and Commercial Lines businesses. Through its Personal Lines segment, the Company is engaged primarily in the underwriting of non-standard automobile insurance and insurance for motorcycles, antique and classic vehicles, trailers, motor-homes, recreational vehicles and personal property.

Through its Commercial Lines, the Company designs and underwrites specialized insurance programs, such as commercial property, commercial automobile, long-haul trucking, surety, liability, creditor insurance, and extended warranty.

Qudos operations and Discontinued Canadian Operations are excluded. Please refer to note 26.

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.

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

The following table summarizes the net income before interest and income taxes by Personal and Commercial Lines for the year ended December 31, 2018 and December 31, 2017:

	2018	**2017**
Revenue		
Net earned premiums		
– Personal Lines	19,846	18,399
– Commercial Lines	10,091	9,671
Total net earned premium	29,937	28,070
Net claims incurred		
– Personal Lines	14,535	13,060
– Commercial Lines	5,268	5,045
Net Claims	19,803	18,105
Net expenses		
– Personal Lines	7,178	6,938
– Commercial Lines	4,102	3,860
Total	11,280	10,798
Corporate Expenses	3,681	2,243
Total net expenses	34,764	31,146
(Loss) income before income taxes		
– Personal Lines	(1,867)	(1,599)
– Commercial Lines	721	766
Total	(1,146)	(833)
Corporate and other	(3,681)	(2,243)
Underwriting loss	(4,827)	(3,076)
Impact of change in net claims discount rate	360	234
Investment income	1,463	6,909
Total income before interest expense and income taxes	(3,004)	4,067