

NOVA MUTUAL INSURANCE COMPANY
Consolidated Financial Statements
For the year ended December 31, 2020

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For the year ended December 31, 2020

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Independent Auditor's Report

To the Policyholders of Nova Mutual Insurance Company

Opinion

We have audited the consolidated financial statements of Nova Mutual Insurance Company (the Company), which comprise the consolidated statement of financial position as at December 31, 2020, the consolidated statement of comprehensive income, consolidated statement of members' surplus and consolidated statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2020, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Basis for Opinion

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

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

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, 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 controls 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 controls.
- 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 Group 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.

BDO Canada LLP

Chartered Professional Accountants, Licensed Public Accountants

Woodstock, Ontario
February 4, 2020

Nova Mutual Insurance Company
Consolidated Statement of Financial Position

As at December 31 **2020** **2019**

Assets

Cash	\$ 4,734,810	\$ 5,377,743
Investments (Note 4)	36,269,883	30,701,159
Investment income accrued	53,583	38,080
Due from policyholders	9,577,656	8,126,455
Reinsurer's share of provision for unpaid claims (Note 3)	9,506,242	9,309,365
Due from reinsurer (Note 3)	38,355	646,616
Due from facility association	38,760	12,250
Deferred policy acquisition expenses (Note 3)	2,852,040	2,284,484
Prepaid expenses (Note 11)	774,598	-
Property, plant & equipment (Note 12)	1,876,233	1,937,888
Deferred income taxes	85,400	75,400
	\$ 65,807,560	\$ 58,509,440

Liabilities

Accounts payable and accrued liabilities	\$ 1,924,058	\$ 1,419,996
Income taxes payable	311,496	303,993
Unearned premiums (Note 3)	14,875,648	12,525,035
Provision for unpaid claims and adjustment expenses (Note 3)	22,106,242	21,034,614
	39,217,444	35,283,638

Members' Surplus

Unappropriated members' surplus	26,590,116	23,225,802
	\$ 65,807,560	\$ 58,509,440

Signed on behalf of the Board by:


 _____, Director


 _____, Director

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

Nova Mutual Insurance Company
Consolidated Statement of Comprehensive Income

For the year ended December 31	2020	2019
Underwriting income		
Gross premiums written	\$ 30,250,269	\$ 25,207,529
Less reinsurance ceded	<u>(3,709,845)</u>	<u>(3,087,035)</u>
Net premiums written	26,540,424	22,120,494
Change in unearned premiums	<u>(2,350,613)</u>	<u>(1,984,792)</u>
Net premiums earned	24,189,811	20,135,702
Service charges	294,806	211,379
	<u>24,484,617</u>	<u>20,347,081</u>
Direct losses incurred		
Gross claims and adjustment expenses	13,086,891	13,801,593
Reinsurer's share of claims and adjustment expenses	<u>(1,428,586)</u>	<u>(3,064,946)</u>
	<u>11,658,305</u>	<u>10,736,647</u>
	<u>12,826,312</u>	<u>9,610,434</u>
Expenses		
Commissions	4,639,933	3,967,745
Other operating and administrative expenses (Note 7)	<u>5,329,125</u>	<u>4,067,882</u>
	<u>9,969,058</u>	<u>8,035,627</u>
Net underwriting income	2,857,254	1,574,807
Investment and other income (Note 5)	1,712,556	2,044,915
Income before taxes	4,569,810	3,619,722
Provision for income taxes (Note 9)	1,205,496	953,407
Comprehensive income for the year	\$ 3,364,314	\$ 2,666,315

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

Nova Mutual Insurance Company
Consolidated Statement of Members' Surplus

For the year ended December 31	2020	2019
Unappropriated members' surplus		
Balance, beginning of year	\$ 23,225,802	\$ 12,314,312
Increase in members' surplus upon amalgamation	-	8,245,175
Comprehensive income for the year	<u>3,364,314</u>	<u>2,666,315</u>
Balance, end of year	<u>\$ 26,590,116</u>	<u>\$ 23,225,802</u>

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

Nova Mutual Insurance Company Consolidated Statement of Cash Flows

For the year ended December 31	2020	2019
Operating activities		
Comprehensive income for the year	\$ 3,364,314	\$ 2,666,315
Adjustments for:		
Depreciation of property, plant & equipment	141,043	87,694
Mutual and pooled fund, interest and dividend income	(885,766)	(1,062,777)
Provision for income taxes	1,205,496	953,407
Realized gain on disposal investments	(110,029)	(1,757,979)
Unrealized (gains) losses on investments	(825,891)	613,302
	2,889,167	1,499,962
Changes in working capital		
Change in due from policyholders	(1,451,201)	(1,677,965)
Change in prepaid expenses	(774,598)	-
Change in accounts payable and other liabilities	504,062	(254,354)
	(1,721,737)	(1,932,319)
Changes in insurance contract related balances		
Change in reinsurer's share of provision for unpaid claims	1,620,123	544,237
Change in amounts due from/to reinsurer	608,261	(546,941)
Change in due to/from facility association	(26,510)	362,715
Change in commissions receivable	-	40,854
Change in deferred policy acquisition expenses	(567,556)	(446,044)
Change in unearned premiums	2,350,613	2,324,606
Change in unearned commissions	-	(83,254)
Change in provision for unpaid claims and adjustment expenses	(745,372)	250,745
	3,239,559	2,446,918
Cash flows related to interest, dividends and income taxes		
Interest and dividends received	61,658	287,861
Mutual and pooled fund distributions received	808,605	795,004
Income taxes (paid) received	(1,207,993)	736,183
	(337,730)	1,819,048
Total cash inflows from operating activities	4,069,259	3,833,609
Investing activities		
Sale of investments	6,387,471	30,979,710
Purchase of investments	(11,130,865)	(31,494,654)
Loan receivable repayments	110,591	84,836
Purchase of property, plant & equipment	(79,389)	(887,533)
Total cash outflows from investing activities	(4,712,192)	(1,317,641)
Net (decrease) increase in cash and cash equivalents	(642,933)	2,515,968
Cash and cash equivalents, beginning of year	5,377,743	1,589,355
Increase in cash and cash equivalents upon amalgamation	-	1,272,420
Cash and cash equivalents, end of year	\$ 4,734,810	\$ 5,377,743

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

Nova Mutual Insurance Company

Notes to the Consolidated Financial Statements

December 31, 2020

1. CORPORATE INFORMATION

Nova Mutual Insurance Company (the Company) is incorporated under the laws of Ontario and is subject to the Ontario Insurance Act. It is licensed to write property, liability, automobile and farmers' accident insurance in Ontario. The Company's head office is located at 35 Talbot Street East, Jarvis, Ontario.

The Company's automobile insurance rates are subject to approval by the Financial Services Regulatory Authority of Ontario (FSRA). Applications for automobile rate changes are presented to FSRA by Farm Mutual Re on behalf of most members of the Ontario Mutual Insurance Association (OMIA). The rate filings include actuarial justification for the rate increases or decreases. All rate filings must be approved by FSRA prior to implementation. Rate regulation may affect the automobile revenues that are earned by the Company. The actual impact of rate regulation would depend on the competitive environment at the time.

These consolidated financial statements have been authorized for issue by the Board of Directors on February 4, 2020.

2. BASIS OF PREPARATION

These consolidated financial statements include the financial statements of Nova Mutual Insurance Company and those of its subsidiary, 2801969 Ontario Ltd.

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

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

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

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

- The calculation of unpaid claims and the related reinsurer's share, including the determination of the initial claim liability, the development of claims and the estimate of time until ultimate settlement (Note 3).
- The determination of the recoverability of deferred policy acquisition expenses (Note 3).
- The classification of financial assets at FVTPL, which includes assessing the business model within which the assets are held and whether the contractual terms of the assets are solely payments of principal and interest on the principal amount outstanding (Note 4).

Nova Mutual Insurance Company

Notes to the Consolidated Financial Statements

December 31, 2020

2. BASIS OF PREPARATION (CONTINUED)

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

3. INSURANCE CONTRACTS

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

Balances arising from insurance contracts primarily include the following:

(a) Premiums and unearned premiums

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

The Company recognizes premium income evenly over the term of the insurance policy generally using the pro rata method. The portion of the premium related to the unexpired portion of the policy at the end of the fiscal year is reflected in unearned premiums. Changes in unearned premiums recorded in the consolidated statement of financial position and their impact on net premiums earned are as follows:

<i>Unearned premiums</i>	2020	2019
Balance, beginning of the year	\$ 12,525,035	\$ 6,958,771
Increase in unearned premiums upon amalgamation	-	3,241,658
Premiums written	30,250,269	25,207,529
Premiums earned during year	(27,899,656)	(22,882,923)
Balance, end of the year	\$ 14,875,648	\$ 12,525,035

Pricing of property and liability policies are based on assumptions in regard to trends and past experience, in an attempt to correctly match policy revenue with the exposed risk. Automobile premiums are subject to approval by the Financial Services Regulatory Authority of Ontario and therefore may result in a delay in adjusting the pricing to exposed risk.

The Company is exposed to a pricing risk to the extent that unearned premiums are insufficient to meet the related future policy costs. Evaluation is performed regularly to estimate future claims costs, related expenses, and expected profit in relation to unearned premiums. There was no premium deficiency at December 31, 2020 and 2019.

Nova Mutual Insurance Company

Notes to the Consolidated Financial Statements

December 31, 2020

3. INSURANCE CONTRACTS (CONTINUED)

Amounts due from policyholders are short-term in nature consisting of a large number of policyholders. The Company applied judgment in its evaluation of its allowance for doubtful accounts and whether to consider flexible payment options due to COVID-19. They also used their experience during the crisis and in past economic downturns. Regular review of amounts outstanding is performed to ensure credit worthiness.

(b) Deferred policy acquisition expenses

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

<i>Deferred policy acquisition expense</i>	2020	2019
Balance, beginning of the year	\$ 2,284,484	\$ 1,438,440
Increase in deferred policy acquisition expense upon amalgamation	-	400,000
Acquisition costs incurred	5,780,209	4,705,919
Expensed during the year	(5,212,653)	(4,259,875)
Balance, end of the year	\$ 2,852,040	\$ 2,284,484

(c) Provisions for unpaid claims and adjustment expenses

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

Claims liabilities are carried on an undiscounted basis.

In relation to COVID-19, the Company applied judgment and actuarial standards to determine its unpaid claims, using different scenarios and assumptions based on the information currently available.

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

Nova Mutual Insurance Company Notes to the Consolidated Financial Statements

December 31, 2020

3. INSURANCE CONTRACTS (CONTINUED)

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

<i>Outstanding claims provision</i>	December 31, 2020		
	Gross	Reinsurance	Net
Long-term	\$ 11,126,612	\$ 4,195,988	\$ 6,930,624
Short-term	2,929,822	538,815	2,391,007
Facility Association and other residual pools	270,175	-	270,175
	14,326,609	4,734,803	9,591,806
Provision for claims incurred but not reported	7,509,852	4,771,439	2,738,413
Provision for internal loss adjustment expense	269,781	-	269,781
	7,779,633	4,771,439	3,008,194
	\$ 22,106,242	\$ 9,506,242	\$ 12,600,000
<i>Outstanding claims provision</i>	December 31, 2019		
	Gross	Reinsurance	Net
Long-term	\$ 11,545,229	\$ 5,617,900	\$ 5,927,329
Short-term	4,085,417	1,017,465	3,067,952
Facility Association and other residual pools	244,035	-	244,035
	15,874,681	6,635,365	9,239,316
Provision for claims incurred but not reported	4,890,152	2,674,000	2,216,152
Provision for internal loss adjustment expense	269,781	-	269,781
	5,159,933	2,674,000	2,485,933
	\$ 21,034,614	\$ 9,309,365	\$ 11,725,249

Nova Mutual Insurance Company

Notes to the Consolidated Financial Statements

December 31, 2020

3. INSURANCE CONTRACTS (CONTINUED)

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

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

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

<i>Claims and adjustment expenses</i>	2020	2019
Unpaid claim liabilities, beginning of year - net of reinsurance	\$ 11,725,249	\$ 5,988,924
Increase of unpaid claims - net of reinsurance upon amalgamation	-	4,941,343
Increase (decrease) in estimated losses and expenses, for losses occurring in prior years	908,959	(327,069)
Provision for losses and expenses on claims occurring in the current year	9,499,042	10,023,903
Payment on claims:		
Current year	(4,161,685)	(5,269,355)
Prior years	(5,371,565)	(3,632,497)
	12,600,000	11,725,249
Unpaid claims, end of year - net	12,600,000	11,725,249
Reinsurer's share	9,506,242	9,309,365
	\$ 22,106,242	\$ 21,034,614

Nova Mutual Insurance Company

Notes to the Consolidated Financial Statements

December 31, 2020

3. INSURANCE CONTRACTS (CONTINUED)

Claim development

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

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

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

The estimation of claim development involves assessing the future behaviour of claims, taking into consideration the consistency of the Company's claim handling procedures, the amount of information available, the characteristics of the line of business from which the claim arises and historical delays in reporting claims. In general, the longer the term required for the settlement of a group of claims the more variable the estimates. Short settlement term claims are those which are expected to be substantially paid within a year of being reported.

The tables that follow present the development of claims payments and the estimated ultimate cost of claims for the claim year 2013 to 2020. The tables show the cumulative amounts paid or estimated to be paid during successive years related to each claim year. The original estimates will be increased or decreased, as more information becomes known about the original claims.

Nova Mutual Insurance Company
Notes to the Consolidated Financial Statements

December 31, 2020

3. INSURANCE CONTRACTS (CONTINUED)

Gross claims	2013	2014	2015	2016	2017	2018	2019	2020	Total
Gross estimate of cumulative claims cost									
At the end year of claim	\$ 2,153,857	\$ 2,141,987	\$ 2,627,160	\$ 2,951,101	\$ 4,440,948	\$ 9,488,978	\$ 10,543,858	\$ 9,035,202	
One year later	2,230,883	1,951,472	2,895,685	3,804,691	4,191,502	14,718,787	12,988,904		
Two years later	2,400,226	1,955,138	2,983,753	4,687,573	9,949,470	14,337,277			
Three years later	2,341,171	1,969,368	3,597,719	9,615,911	8,089,637				
Four years later	2,321,270	1,972,948	7,091,210	9,191,402					
Five years later	2,321,270	8,514,814	7,157,548						
Six years later	5,587,858	8,508,819							
Seven years later	5,587,858								
Current estimate of cumulative claims cost	5,587,858	8,508,819	7,157,548	9,191,402	8,089,637	14,337,277	12,988,904	9,035,202	\$ 74,896,647
Cumulative payments	5,583,858	8,508,819	6,030,953	7,771,933	6,977,729	12,438,662	8,477,396	5,371,565	61,160,915
Outstanding claims	\$ 4,000	\$ -	\$ 1,126,595	\$ 1,419,469	\$ 1,111,908	\$ 1,898,615	\$ 4,511,508	\$ 3,663,637	13,735,732
Outstanding claims 2012 and prior									320,702
Facility association and other residual pools									270,175
IBNR and ILAE									7,779,633
Total gross outstanding claims including claims handling expense									\$ 22,106,242
Net of Reinsurance	2013	2014	2015	2016	2017	2018	2019	2020	Total
Net estimate of cumulative claims cost									
At the end year of claim	\$ 1,705,295	\$ 2,126,227	\$ 2,563,877	\$ 2,742,962	\$ 4,440,948	\$ 7,789,974	\$ 10,023,903	\$ 9,023,627	
One year later	1,796,113	1,936,653	2,511,585	3,480,519	4,191,502	11,324,491	10,447,266		
Two years later	1,932,455	1,940,318	2,533,993	3,853,452	6,360,159	11,385,483			
Three years later	1,911,937	1,954,548	2,509,346	6,612,800	6,668,412				
Four years later	1,892,036	1,958,128	4,658,782	6,523,109					
Five years later	1,892,036	4,820,856	4,729,951						
Six years later	3,922,958	4,835,259							
Seven years later	4,352,192								
Current estimate of cumulative claims cost	4,352,192	4,835,259	4,729,951	6,523,109	6,668,412	11,385,483	10,447,266	9,023,627	\$ 57,965,299
Cumulative payments	4,313,192	4,835,259	4,477,759	5,592,213	5,846,564	9,968,657	8,238,459	5,371,565	48,643,668
Outstanding claims	\$ 39,000	\$ -	\$ 252,192	\$ 930,896	\$ 821,848	\$ 1,416,826	\$ 2,208,807	\$ 3,652,062	9,321,631
Facility association and other residual pools									270,175
IBNR and ILAE									3,008,194
Total net outstanding claims including claims handling expense									\$ 12,600,000

Nova Mutual Insurance Company

Notes to the Consolidated Financial Statements

December 31, 2020

3. INSURANCE CONTRACTS (CONTINUED)

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

Results of sensitivity testing based on expected loss ratios are as follows, impact on pre-tax income:

	Property claims		Auto claims		Liability claims	
	2020	2019	2020	2019	2020	2019
5% change in loss ratios would result in the following increase/decrease:						
Gross	\$ 853,992	\$ 685,531	\$ 486,217	\$ 430,115	\$ 158,192	\$ 134,394
Net	\$ 775,096	\$ 617,285	\$ 421,572	\$ 375,559	\$ 145,080	\$ 123,697

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

(d) Liability adequacy test

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

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

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

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

Nova Mutual Insurance Company Notes to the Consolidated Financial Statements

December 31, 2020

3. INSURANCE CONTRACTS (CONTINUED)

The Company follows a policy of underwriting and reinsuring contracts of insurance which, in the main, limit the liability of the Company to an amount on any one claim of \$500,000 in the event of a property claim, an amount of \$500,000 in the event of an automobile claim and \$500,000 in the event of a liability claim. The Company also obtained reinsurance which limits the Company's liability to \$1,500,000 in the event of a series of claims arising out of a single occurrence. In addition, the Company has obtained stop loss reinsurance which limits the liability of all claims in a specific year to 70% of gross net earned premiums incurred.

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

<i>Due from reinsurer</i>	2020	2019
Balance, beginning of the year	\$ 646,616	\$ 5,855
Increase in due from reinsurer upon amalgamation	-	93,820
Submitted to reinsurer for claims	1,228,594	3,740,940
Received from reinsurer	(1,836,855)	(3,193,999)
Balance, end of the year	\$ 38,355	\$ 646,616

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

Nova Mutual Insurance Company Notes to the Consolidated Financial Statements

December 31, 2020

3. INSURANCE CONTRACTS (CONTINUED)

Changes in reinsurer's share of provision for unpaid claims recorded in the consolidated statement of financial position and their impact on net premiums earned are as follows:

<i>Reinsurer's share of provision for unpaid claims</i>	2020	2019
Balance, beginning of the year	\$ 9,309,365	\$ 3,598,193
Increase in reinsurer's share of provision for unpaid claims upon amalgamation	-	6,255,409
New claims reserve	42,218	519,955
Change in prior years reserve	(433,747)	2,676,748
Submitted to reinsurer	588,406	(3,740,940)
Balance, end of the year	\$ 9,506,242	\$ 9,309,365

(f) Refund of premium

Under the discretion of the board of directors, the Company may declare a refund to qualifying property policy holders based on the premiums paid in the fiscal period. This refund is recognized as a reduction of underwriting income in the period for which it is declared.

(g) Salvage and subrogation recoverable

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

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

Nova Mutual Insurance Company

Notes to the Consolidated Financial Statements

December 31, 2020

4. INVESTMENTS

(a) Recognition and initial measurement

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

On December 31, 2020, 2801969 Ontario Inc. a wholly owned subsidiary of Nova Mutual Insurance Company entered into an agreement to acquire 35% of the issued and outstanding shares of Haldimand Insurance Brokers for cash consideration of \$858,385. Upon initial recognition the investment was measured at fair value. This was the only activity in the wholly owned subsidiary for the year ended December 31, 2020.

(b) Classification and subsequent measurement

The Company classifies its GIC's, bonds and private loans as amortized cost as the company holds to collect contractual cash flows until maturity of the debt instrument.

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

The Company classifies its equity instruments in Canadian non-public companies without significant influence, as FVTPL.

When accounting for its equity instruments in Canadian non-public under significant influence companies, as defined under IAS 28, the Company subsequently applies the equity method of accounting.

The pooled funds and mutual funds are subsequently measured at fair value where the net gains and losses, including any interest or dividend income and foreign exchange gains and losses, are recognized in comprehensive income.

(c) Derecognition

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

Nova Mutual Insurance Company Notes to the Consolidated Financial Statements

December 31, 2020

4. INVESTMENTS (CONTINUED)

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

	December 31, 2020		December 31, 2019	
	Cost	Fair Value	Cost	Fair Value
GICs	\$ 2,045,220	\$ 2,045,220	\$ 2,761,500	\$ 2,761,500
Pooled Funds				
Fixed Income	-	-	211,612	211,725
Canadian Equity	-	-	70,839	86,766
Canadian Infrastructure	-	-	223,006	217,260
Canadian Multi Strategy	-	-	29,469	28,922
Global Equity	-	-	89,846	134,460
	-	-	624,772	679,133
Bonds				
Bonds Not Rated	600,000	600,000	-	-
Mutual Funds				
Fixed Income	21,732,356	22,357,851	20,997,286	20,831,472
Canadian Equity	4,493,851	4,565,615	3,982,347	3,872,829
Global Equity	1,628,524	1,569,932	1,292,755	1,254,384
Real Estate	2,400,000	2,420,505	-	-
	30,254,731	30,913,903	26,272,388	25,958,685
Equity Investments				
Canadian non-public	403,489	406,793	403,489	408,875
Canadian non-public under significant influence	895,385	895,385	-	-
	1,298,874	1,302,178	403,489	408,875
Other Investments				
Private loans	1,344,418	1,344,419	827,131	827,131
Fire Mutuals Guarantee Fund	38,532	38,532	37,957	37,957
Other	25,631	25,631	27,878	27,878
	1,408,581	1,408,582	892,966	892,966
Total investments	\$ 35,607,406	\$ 36,269,883	\$ 30,955,115	\$ 30,701,159

Nova Mutual Insurance Company Notes to the Consolidated Financial Statements

December 31, 2020

4. INVESTMENTS (CONTINUED)

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

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

Liquidity risk is the risk that the Company will not be able to meet all cash outflow obligations as they come due. The Company mitigates this risk by monitoring cash activities and expected outflows. The Company's current liabilities arise as claims are made. The Company does not have material liabilities that can be called unexpectedly at the demand of a lender or client. Claim payments are funded by current operating cash flow including investment income.

The Company's investment policy requires that 50% to 90% of the Company's portfolio be held in investment grade fixed income instruments, which mitigates liquidity risk.

Maturity profile of GICs, bonds and private loans held is as follows:

	Within 1 year	2 to 5 years	6 to 10 years	Over 10 years	Fair value
December 31, 2020	\$ 1,120,500	\$ 924,720	\$ 744,418	\$ 1,200,000	\$ 3,989,638
Percent of Total	28.09 %	23.18 %	18.66 %	30.08 %	
December 31, 2019	\$ 1,527,300	\$ 1,234,200	\$ 827,131	-	\$ 3,588,631
Percent of Total	42.56 %	34.39 %	23.05 %	-	

The effective interest rate of the GICs, bonds and private loans held is 1.87% at December 31, 2020 (2019 - 2.45%).

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

Nova Mutual Insurance Company

Notes to the Consolidated Financial Statements

December 31, 2020

4. INVESTMENTS (CONTINUED)

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

The Company's investment policy operates within the guidelines of the Insurance Act of Ontario. An investment policy is in place and its application is monitored by the Investment Committee and the Board of Directors.

The Company's currency risk is related to holdings in global equity mutual funds.

The Company is exposed to interest rate risk through its interest bearing investments (GICs, bonds, private loan and fixed income mutual and pooled funds).

The Company is exposed to equity risk through its equity holdings within its investment portfolio.

The Company manages these risks by designating and allocating amounts within limited categories and asset ranges as follows (mutual funds are managed by "looking through" for fund make-up):

Cash and cash equivalents	from 0 to 30%
Investment grade fixed income	from 50 to 70%
High yield fixed income	from 0 to 10%
Canadian equities	from 0 to 25%
Global equities	from 0 to 6.25%
Other	from 0 to 10%

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

The Company's investment portfolio is not significantly exposed to market, currency and interest rate risk.

Nova Mutual Insurance Company

Notes to the Consolidated Financial Statements

December 31, 2020

4. INVESTMENTS (CONTINUED)

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

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

	Level 1	Level 2	Level 3	Total
December 31, 2020				
Mutual funds	-	30,913,903	-	30,913,903
Equity investments	-	8,875	397,918	406,793
Other investments	-	38,532	-	38,532
<hr style="border: 1px solid black;"/>				
December 31, 2019				
Pooled funds	-	679,133	-	679,133
Mutual funds	-	25,958,685	-	25,958,685
Equity investments	-	8,875	400,000	408,875
Other investments	-	37,957	-	37,957
<hr style="border: 1px solid black;"/>				

There were no transfers between any of the levels of the fair value hierarchy for the years ended December 31, 2020 and 2019.

The following table presents a reconciliation of the equity investments which are the only Level 3 investments:

	2020	2019
Balance, beginning of the year	\$ 400,000	\$ -
Gains / losses recognized in net income	(2,082)	-
Purchases	-	400,000
	<hr style="border: 1px solid black;"/>	<hr style="border: 1px solid black;"/>
Balance, end of the year	\$ 397,918	\$ 400,000

The fair value is based on the valuation of the Company as provided by management. Due to the use of unobservable data and their limited liquidity, this investment is classified as Level 3

Nova Mutual Insurance Company Notes to the Consolidated Financial Statements

December 31, 2020

5. INVESTMENT AND OTHER INCOME

	2020	2019
Mutual and pooled fund income	\$ 808,605	\$ 795,004
Interest income	77,161	225,201
Dividend income	-	42,572
Realized gain on disposal of investments	110,029	1,757,979
Unrealized gain (loss) on investments	825,891	(613,302)
Investment fees	(109,130)	(162,539)
	\$ 1,712,556	\$ 2,044,915

6. CAPITAL MANAGEMENT

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

The Company's objectives with respect to capital management are to maintain a capital base that is structured to exceed regulatory requirements and to best utilize capital allocations. The regulators measure the financial strength of property and casualty insurers using a minimum capital test (MCT). The regulators require property and casualty companies to comply with capital adequacy requirements. This test compares a Company's capital against the risk profile of the organization. The risk-based capital adequacy framework assesses the risk of assets, policy liabilities and other exposures by applying various factors that are dependent on the risks associated with the Company's assets. Additionally, an interest rate risk margin is included in the MCT by assessing the sensitivity of the Company's interest-sensitive assets and liabilities to changes in interest rates. The regulator indicates that the Company should produce a minimum MCT of 150%. As at December 31, 2020, the Company has consistently exceeded this minimum. The regulator has the authority to request more extensive reporting and can place restrictions on the Company's operations if the Company falls below this requirement or deemed necessary.

Nova Mutual Insurance Company Notes to the Consolidated Financial Statements

December 31, 2020

7. OTHER OPERATING AND ADMINISTRATIVE EXPENSES

	2020	2019
Advertising	\$ 231,313	\$ 116,409
Amalgamation costs	-	6,854
Automobile and travel	146,048	212,164
Bad debts	37,441	1,483
Interest and bank charges	135,946	74,200
Bureaus and associations	101,506	111,737
Computer expense	524,119	780,527
Consulting fees	75,530	99,740
Directors' remuneration	130,760	135,936
Furniture and equipment	105,749	64,434
Inspections	54,562	39,214
Insurance	79,921	82,792
Occupancy costs	124,310	123,518
Postage	35,739	43,207
Printing and stationery	74,327	62,563
Premium taxes	80,034	52,052
Professional fees	132,591	56,102
Regulatory expense	1,180	12,577
Salaries	2,742,425	1,565,096
Benefits	470,225	403,947
Telephone	45,399	23,330
	\$ 5,329,125	\$ 4,067,882

8. SALARIES, BENEFITS AND DIRECTORS' FEES

	2020	2019
Salaries and benefits	\$ 3,041,267	\$ 2,049,751
Directors' fees and benefits	134,750	145,050
Salaries and benefits included in gross claims and adjustment expenses	511,549	442,665
Salaries and benefits included in commissions	243,302	307,121
	\$ 3,930,868	\$ 2,944,587

Nova Mutual Insurance Company

Notes to the Consolidated Financial Statements

December 31, 2020

9. INCOME TAXES

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

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

	2020	2019
Current tax expense		
Based on current year taxable income	\$ 1,215,496	\$ 303,993
Adjustments to provision of prior periods	-	(48)
	1,215,496	303,945
Deferred tax expense		
Origination and reversal of temporary differences	(10,000)	649,462
	\$ 1,205,496	\$ 953,407

Reasons for the difference between the provision for income taxes and the expected income taxes based on the statutory tax rate of 26.5% are as follows:

	2020	2019
Income before taxes	\$ 4,569,810	\$ 3,619,722
Expected taxes based on the statutory rate of 26.5%	1,211,000	959,226
Canadian dividend income	-	(10,439)
Other non deductible expenses	(5,504)	4,668
Over provision in prior years	-	(48)
	\$ 1,205,496	\$ 953,407

Nova Mutual Insurance Company

Notes to the Consolidated Financial Statements

December 31, 2020

10. FIRE MUTUALS GUARANTEE FUND AND FINANCIAL GUARANTEE CONTRACTS

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

The Company is a member of the Farm Mutual Reinsurance Plan Inc. ("Farm Mutual Re"), which is a general reinsurer that shares in the insurance risks originally accepted by member insurance companies. As a member of the Farm Mutual Re, the Company may be required to contribute additional capital to Farm Mutual Re in the form of subordinated debt should its capital fall below a prescribed minimum.

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

11. PREPAID EXPENSES

In 2020, the Company signed a Letter of Intent (LOI) with a software company to develop and deploy an insurance carrier system expected to launch in 2023. The applicable project and system costs, once deployed, will be amortized into income over the term of the initial contract.

Nova Mutual Insurance Company Notes to the Consolidated Financial Statements

December 31, 2020

12. PROPERTY, PLANT & EQUIPMENT

Property, plant & equipment

Property, plant & equipment is initially recorded at cost and subsequently measured at cost less accumulated depreciation and accumulated impairment losses, with the exception of land which is not depreciated. Depreciation is recognized in comprehensive income and is provided on a straight-line basis over the extended useful life of the asset.

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

		2020		
	Useful life	Cost	Accumulated Depreciation	Net Book Value
Land	N/A	\$ 254,550	\$ -	254,550
Buildings & parking lot	10 to 40 years	1,723,645	474,701	1,248,944
Automotive equipment	5 years	23,956	15,112	8,844
Office equipment	10 years	384,007	161,878	222,129
Computer equipment	5 years	398,715	256,949	141,766
		<u>\$ 2,784,873</u>	<u>\$ 908,640</u>	<u>\$ 1,876,233</u>

		2019		
	Useful life	Cost	Accumulated Depreciation	Net Book Value
Land	N/A	\$ 254,550	\$ -	254,550
Buildings & parking lot	10 to 40 years	1,685,252	427,832	1,257,420
Automotive equipment	5 years	23,956	9,215	14,741
Office equipment	10 years	353,509	120,697	232,812
Computer equipment	5 years	388,219	209,854	178,365
		<u>\$ 2,705,486</u>	<u>\$ 767,598</u>	<u>\$ 1,937,888</u>

Nova Mutual Insurance Company

Notes to the Consolidated Financial Statements

December 31, 2020

13. GROUP RETIREMENT SAVINGS PLAN AND PENSION PLAN

The Company makes contributions on behalf of its employees to "The Retirement Annuity Plan for Employees of the Ontario Mutual Insurance Association and Member Companies" ("the plan"). This pension plan is a multi-employer pension plan as defined by IAS 19 Employee Benefits. The Company accounts for the plan as if it were a defined contribution plan, recognizing contributions as an expense in the year to which they related as sufficient information is not available to use the defined benefit accounting.

The Company matches employee contributions, and funds the excess defined benefit based on the Company's percentage of pensionable earnings as calculated by the Pension Plan actuaries. The Pension Plan agreement states that the Company is responsible for its share of any deficit as a result of any actuarial valuation or cost certificate. The minimum funding requirement is the solvency valuation amount determined by the Pension Plan actuary on the valuation dates prescribed by the Pensions Benefit Act. In the event of a wind-up, voluntary withdrawal or bankruptcy, either by the Company or the group as a whole, the Company is responsible for its portion of all expenses and deficit related to such. According to the most recent actuarial valuation dated January 1, 2018, the going concern valuation for the defined plan shows a surplus. The next pension valuation is scheduled for January 1, 2021.

The Company makes contributions to the plan on behalf of members of its staff. The plan is a money purchase plan, with a defined benefit option at retirement available to some employees, which specifies the amount of the retirement benefit plan to be received by the employees based on length of service and rates of pay.

The amount contributed to the plan in 2020 was \$78,189 (2019 - \$101,383). The contributions were made for the current service and these have been recognized in comprehensive income. These contributions amount to 1.91% (2019 - 1.90%) of the total contributions made to the Ontario Mutual Insurance Association Pension Plan by all the participating entities during the current fiscal year.

Expected contributions to the plan for 2021 amount to \$72,000.

The defined benefit plan has been closed to future eligible employees effective July 1, 2013. The Company and all current employees who are accruing benefits under the defined benefit plan continue to contribute to the defined benefit plan according to the existing terms of the agreement. Future eligible employees are enrolled in the defined contribution plan.

Due to the complexity of the valuation and its long-term nature, the funding valuation is highly sensitive to changes in the assumptions, which are reviewed at each reporting date. The COVID-19 crisis has created additional uncertainty which could impact assumptions going forward. This uncertainty could create volatility in the funding status of the plan.

The amount contributed to the defined contribution plan in 2020 was \$189,354 (2019 - \$60,861). The contributions were made for the current service and these have been recognized in comprehensive income.

Expected contributions to the defined contribution plan for 2021 amount to \$215,000.

Nova Mutual Insurance Company Notes to the Consolidated Financial Statements

December 31, 2020

14. RELATED PARTY TRANSACTIONS

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

	2020	2019
Compensation		
Short-term employee benefits and directors' fees	\$ 854,160	\$ 769,314
Pension benefits	30,288	27,102
	\$ 884,448	\$ 796,416
Premiums	\$ 30,942	\$ 46,610
Claims paid	\$ 10,914	\$ 7,380

15. NEW STANDARDS, INTERPRETATIONS AND AMENDMENTS NOT YET EFFECTIVE

Certain new standards, amendments to standards, and interpretations were issued by the IASB or the IFRS Interpretations Committee that are mandatory for accounting years beginning after January 1, 2021 or later that the Company has decided not to adopt early.

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

- IFRS 17 Insurance Contracts supersedes IFRS 4 Insurance Contracts. IFRS 17 establishes the principles for the recognition, measurement, presentation and disclosure of insurance contracts. IFRS 17 requires entities to measure insurance contract liabilities using updated estimates and assumptions that reflect the timing of cash flows and any uncertainty relating to insurance contracts. Additionally, IFRS 17 requires entities to recognize profits as it delivers insurance services. The effective date for IFRS 17 is January 1, 2023. The Company has not yet determined the impact of adoption, however is expected to significantly impact the overall consolidated financial statements.