Consolidated Financial Statements of

NORTH WATERLOO FARMERS MUTUAL INSURANCE COMPANY

(Subsequently amalgamated to form Heartland Farm Mutual Inc.)

Year ended December 31, 2015

NORTH WATERLOO FARMERS MUTUAL INSURANCE COMPANY
CONSOLIDATED FINANCIAL STATEMENTS
For the year ended December 31, 2015

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INDEPENDENT AUDITORS' REPORT

To the Policyholders and Directors of The North Waterloo Farmers Mutual Insurance Company

We have audited the accompanying consolidated financial statements of The North Waterloo Farmers Mutual Insurance Company, which comprise the consolidated statement of financial position as at December 31, 2015, the consolidated statements of income and comprehensive income, changes in surplus and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility 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.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of The North Waterloo Farmers Mutual Insurance Company as at December 31, 2015, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards.

Chartered Professional Accountants, Licensed Public Accountants

February 24, 2016
Waterloo, Canada

APPOINTED ACTUARY'S REPORT

To the Policyholders and Directors of The North Waterloo Farmers Mutual Insurance Company

I have valued the policy liabilities and reinsurance recoverable of The North Waterloo Farmers Mutual Insurance Company for its consolidated statement of financial position as at December 31, 2015 and their change in the consolidated statement 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 net of reinsurance recoverable makes appropriate provision for all policy obligations and the consolidated financial statements fairly present the results of the valuation.

Toronto, Ontario
February 24, 2016

Liam M. McFarlane
Fellow, Canadian Institute of Actuaries

THE NORTH WATERLOO FARMERS MUTUAL INSURANCE COMPANY

Consolidated Statement of Financial Position
(In thousands of dollars)

December 31, 2015, with comparative figures for December 31, 2014

	2015	2014
Assets		
Cash and cash equivalents	$ 19,659	$ 16,163
Invested assets (note 4)	124,914	115,164
Due from brokers	4,231	4,057
Premiums receivable from policyholders	20,672	19,727
Accrued investment income	580	627
Insurance and other receivables	395	1,611
Income taxes receivable (note 11)	---	1,169
Deferred income taxes (note 12)	218	172
Reinsurers' share of:		
Unearned premiums (note 10(b))	301	357
Unpaid claims and adjustment expenses (note 10)	21,209	19,033
Deferred policy acquisition costs	13,703	12,864
Property and equipment (note 8)	7,227	7,501
Intangible assets (note 9)	1,424	1,252
Other assets	396	318
	$ 214,929	$ 200,015
Liabilities		
Expenses due and accrued	$ 2,272	$ 1,639
Due to other insurers	1,690	1,392
Due to brokers	3,410	3,486
Income taxes payable (note 11)	642	---
Provision for unpaid claims (note 10)	86,022	84,821
Unearned reinsurance commissions	48	43
Unearned premiums (note 10(b))	50,875	47,656
	144,959	139,037
Surplus for the protection of policyholders		
Policyholders' equity	64,096	57,015
Accumulated other comprehensive income	5,874	3,963
	69,970	60,978
Subsequent event – formation of Heartland Farm Mutual Inc. (note 18)		
	$ 214,929	$ 200,015

See accompanying notes to consolidated financial statements.

On behalf of the Board: Helen J. Johns, Director, Carlos A. Rodrigues, Director

THE NORTH WATERLOO FARMERS MUTUAL INSURANCE COMPANY

Consolidated Statement of Income and Comprehensive Income
(In thousands of dollars)

December 31, 2015, with comparative figures for December 31, 2014

	2015	2014
Gross written premiums	$ 100,656	$ 93,853
Reinsurance ceded	(11,210)	(9,972)
Net written premiums	89,446	83,881
Change in unearned premiums:		
Gross amount	(3,219)	(2,951)
Reinsurer's share	(56)	215
	(3,275)	(2,736)
Net premiums earned	86,171	81,145
Other	1,417	1,129
Underwriting revenue	87,588	82,274
Underwriting expenses:		
Gross claims and adjustments expenses	57,680	62,776
Reinsurer's share of claims and adjustment expenses	(11,398)	(9,257)
Net claims and adjustment expense	46,282	53,519
Commissions	19,565	18,160
Premium taxes	2,837	2,723
Salaries and benefits	7,456	6,474
Operating expenses	5,286	4,139
	81,426	85,015
Underwriting income (loss)	6,162	(2,741)
Interest income	3,100	3,070
Investment expenses	(437)	(399)
Unrealized gain (loss) on financial assets at fair value through profit or loss	(241)	1,487
Income before income taxes	8,584	1,417
Income taxes (recovery): (note 11)		
Current	1,549	83
Deferred	(46)	(100)
	1,503	(17)
Net income	7,081	1,434
Other comprehensive income:		
Unrealized gain on available-for-sale assets arising during the period, net of tax $424 (2014 - $379)	1,911	1,623
Total comprehensive income	$ 8,992	$ 3,057

See accompanying notes to consolidated financial statements.

THE NORTH WATERLOO FARMERS MUTUAL INSURANCE COMPANY

Consolidated Statement of Changes in Surplus
(In thousands of dollars)

December 31, 2015, with comparative figures for December 31, 2014

		2015		2014
Policyholders' equity				
Balance, beginning of year	$	57,015	$	55,581
Net income		7,081		1,434
Balance, end of year		64,096	$	57,015
Accumulated other comprehensive income				
Balance, beginning of year	$	3,963	$	2,340
Change in unrealized gain on available-for-sale investments		1,911		1,623
Balance, end of year		5,874	$	3,963
Total surplus	$	69,970	$	60,978

Accumulated other comprehensive income ("AOCI") is composed of unrealized gains and losses on available-for-sale securities, net of income taxes of $1,308 (2014 - $884).

See accompanying notes to consolidated financial statements.

THE NORTH WATERLOO FARMERS MUTUAL INSURANCE COMPANY

Consolidated Statement of Cash Flows
(In thousands of dollars)

December 31, 2015, with comparative figures for December 31, 2014

	2015	2014
Operating activities:		
Premiums received, net of reinsurance $10,912 (2014 - $9,762)	$ 88,625	$ 83,049
Fee income received	1,519	1,421
Investment income received	2,710	2,663
	92,854	87,133
Claims payments	46,450	44,354
Policy acquisition expenses paid, net of commissions from reinsurers	22,897	21,208
Operating expenses	11,083	10,627
Mutual policyholders' premium rebates paid	102	292
Income taxes paid	146	2,117
	80,678	78,508
Cash provided by operating activities	12,176	8,625
Investing activities:		
Bonds and bond fund purchases	(43,120)	(61,388)
Bonds sold, redeemed or matured	40,209	58,535
Common equities and equity fund purchases	(5,000)	(5,000)
Broker loans	233	226
Proceeds from disposal of property and equipment	37	32
Purchase of property and equipment	(395)	(3,405)
Purchase of intangible assets	(644)	(434)
	8,680	(11,434)
Increase (decrease) in cash and cash equivalents	3,496	(2,809)
Cash and cash equivalents, beginning of year	16,163	18,972
Cash and cash equivalents, end of year	$ 19,659	$ 16,163

See accompanying notes to consolidated financial statements.

THE NORTH WATERLOO FARMERS MUTUAL INSURANCE COMPANY

Consolidated Schedule of Operating Expenses
(In thousands of dollars)

December 31, 2015, with comparative figures for December 31, 2014

	2015	2014
Education and training	$ 178	$ 184
Occupancy	662	512
Advertising	399	250
Automobile and travel	553	528
Bureaus and associations	671	432
Donations	84	80
Information technology	1,801	1,675
Furniture and equipment	139	79
Underwriting reports	395	379
Insurance	108	74
Postage and courier	245	205
Printing and stationery	117	103
Professional fees	1,174	666
Telephone and other communications	101	71
Bad debts	40	157
Miscellaneous	232	265
	6,899	5,660
Less portion allocated to net claims and adjustment expenses	1,613	1,521
Operating expenses	$ 5,286	$ 4,139

See accompanying notes to consolidated financial statements.

Organization and nature of the business:

The North Waterloo Farmers Mutual Insurance Company (“the Company”) was incorporated under the laws of Canada and is subject to the Insurance Companies Act of Canada. It is licensed to write property, general liability, automobile, hail, boiler and machinery, fidelity and accident and sickness insurance in Ontario, Nova Scotia, Prince Edward Island, New Brunswick, Manitoba, Saskatchewan and Alberta, but only writes business in the province of Ontario. The Company’s Head Office is located in Waterloo, Ontario.

On January 16, 2015, the Company entered into an amalgamation agreement with another farm mutual insurance company, Oxford Mutual Insurance Company, providing for the amalgamation of the two companies. On August 27, 2015, the mutual policyholders of both companies voted and approved the amalgamation of the two companies to create Heartland Farm Mutual Inc. The amalgamation was completed January 1, 2016 (note 18).

The Company is subject to rate regulation in the automobile business that it writes. Before automobile insurance rates can be changed, a rate filing is prepared. The rate filing must include actuarial justification for rate increases or decreases. All rate filings are approved or denied by the Financial Services Commission of Ontario. Rate regulation may affect the automobile revenues that are earned by the Company.

1. Basis of presentation:

(a) Statement of compliance:

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

The financial statements were approved by the Board of Directors on February 24, 2016.

(b) Basis of measurement:

The consolidated financial statements have been prepared on a historical cost basis, except for the following items in the statement of financial position:

- financial instruments at fair value through profit or loss are measured at fair value
- available-for-sale financial assets which are measured at fair value

(c) Functional and presentation currency:

These consolidated financial statements are presented in Canadian dollars, which is the Company's functional currency. Except as otherwise indicated, all financial information presented in Canadian dollars has been rounded to the nearest thousand.

1. Basis of presentation (continued):

(d) Use of estimates and judgments:

The preparation of the consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, revenue and expenses. Actual results may differ from those estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the year in which the estimates are revised and in any future periods affected.

Information about critical judgments in applying accounting policies that have the most significant effect on amounts recognized in the consolidated financial statements is discussed in note 3.

2. Significant accounting policies:

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, unless otherwise indicated.

(a) Basis of consolidation:

(i) Subsidiaries:

Subsidiaries are entities controlled by the Company. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the Company.

The consolidated financial statements include all financial operations of North Waterloo Farmers Mutual Insurance Company and its wholly-owned subsidiaries 8037574 Canada Inc. and 3078191 Canada Inc.

(ii) Transactions eliminated on consolidation

Intra-company balances and transactions, and any unrealized revenue and expenses arising from intra-company transactions, are eliminated in preparing these consolidated financial statements.

2. Significant accounting policies (continued):

(b) Financial instruments:

The Company's financial instruments are classified into one of the following four categories, as defined below:

- Financial assets at fair value through profit or loss ("FVTPL")
- Available-for-sale ("AFS")
- Loans and receivables
- Other financial liabilities

All financial instruments are initially recognized at fair value and are subsequently accounted for based on their classification as described below. The classification depends on the purpose for which the financial instruments were acquired and their characteristics. Instruments classified as FVTPL may never be reclassified and, except in very limited circumstances, the classification of other instruments is not changed subsequent to initial recognition. Financial assets purchased and sold, where the contract requires the asset to be delivered within an established time frame, are recognized on a settlement date basis.

Transaction costs are expensed as incurred for FVTPL financial instruments. For other financial instruments, transaction costs are capitalized on initial recognition. The effective interest method of amortization is used for any transaction costs capitalized on initial recognition and for the premiums or discounts earned on AFS investments.

The fair value of a financial instrument on initial recognition is normally the transaction price, i.e. the fair value of the consideration given or received. Subsequent to initial recognition, the fair values are determined based on available information. The fair values of investments are based on the quoted market prices at bid. The fair values of commercial loans and other financial instruments are obtained using discounted cash flow analysis. Unless otherwise disclosed, the carrying values of financial instruments approximate their fair values.

(i) Financial assets at fair value through profit or loss:

A financial asset is classified as FVTPL if it was classified as held-for-trading or is designated as such upon initial recognition. FVTPL financial assets are purchased with the intention of generating profits in the near term or are voluntarily so designated by the Company. Changes in fair values are recorded as "Unrealized gain (loss) on financial assets at fair value through profit or loss" in the statement of income and comprehensive income with the related tax impact included in the current and future tax line items.

2. Significant accounting policies (continued):

(b) Financial instruments (continued):

(ii) Available-for-sale ("AFS"):

Changes in fair values are recorded, net of income taxes, in "Other Comprehensive Income" ("OCI") in the statement of income and comprehensive income until the financial instrument is disposed of, or where there has been a significant or prolonged decline in the fair value of an AFS financial asset. When the instrument is disposed of, the gain or loss is reclassified from OCI to "Realized gain (loss) on sale of investments" in the statement of income and comprehensive income. Gains and losses on the sale of AFS financial instruments are calculated on an average cost basis.

(iii) Loans and receivables/other financial liabilities:

Financial instruments classified as loans and receivables and other financial liabilities are carried at amortized cost using the effective interest rate method. When there is a significant or prolonged decline in value, the value of these financial instruments is written down to the estimated net realizable value.

(iv) Financial liabilities:

Financial liabilities are recognized initially on the trade date at which the Company becomes party to the contractual provisions of the instrument. The Company derecognizes a financial liability when its contractual obligations are discharged or cancelled or expire

(c) Investment income and expenses:

Interest income from fixed income securities is recognized on an accrual basis using the effective interest rate method and reported within interest and dividend income.

Dividends on equity investments are recognized when the shareholder's right to receive payment is established, which is the ex-dividend date, and are reported within interest and dividend income.

General investment expenses are recognized as incurred.

(d) Real estate:

Items of real estate are recorded at cost less accumulated depreciation and accumulated impairment losses. Any gain or loss on disposal of real estate calculated as the difference between the net proceeds from the disposal and the carrying amount of the item, is recognized in profit or loss.

2. Significant accounting policies (continued):

(e) Impairment:

(i) Financial assets:

A financial asset not carried at FVTPL is assessed at each reporting date to determine whether there is objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

Factors considered in determining whether a loss is significant or prolonged include the duration and extent to which fair value has been below cost, financial condition and near-term prospects of the issuer, and the Company's ability and intent to hold the investment for a period of time sufficient to allow for any anticipated recovery.

If an AFS investment becomes impaired, the loss is reclassified from OCI to "Impairment of AFS securities" in the statement of income and comprehensive income. The cumulative loss that is removed from accumulated other comprehensive income and recognized in income is the difference between the acquisition cost, net of any principal repayment and amortization, and the current fair value, less any impairment loss previously recognized in income.

If, in a subsequent period, the fair value of an impaired AFS debt security increases and the increase can be related objectively to an event occurring after the impairment loss was recognized in income, then the impairment loss is reversed, with the amount of the reversal recognized in income.

The Company considers evidence of impairment for receivables at both a specific asset and collective level. All individually significant receivables are assessed for specific impairment. Receivables that are not individually significant are collectively assessed for impairment. In assessing collective impairment, the Company uses historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgment as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical trends.

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognized in income and reflected in an allowance account against receivables. Interest on the impaired asset continues to be recognized through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through income.

2. Significant accounting policies (continued):

(e) Impairment (continued):

(ii) Non-financial assets:

The carrying amounts of the Company's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. An impairment loss is recognized if the carrying amount of an asset exceeds its estimated recoverable amount.

The recoverable amount of an asset is the greater of its value in use and its fair value less expected selling costs. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Impairment losses are recognized in income in the period in which the impairment is determined.

(f) Property and equipment:

(i) Recognition and measurement:

Head office property is stated at its revalued amounts, being the fair value at January 1, 2010, the date of revaluation upon adoption of IFRS ("deemed cost") plus subsequent additions less accumulated depreciation and accumulated impairment losses. Equipment and automobiles are recorded at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the asset.

Gains and losses on disposals of property and equipment are determined by comparing the proceeds with the carrying amount of the item disposed, and are recognized on a net basis within income.

(ii) Subsequent costs:

The cost of replacing a part of an item of property and equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Company, and its cost can be measured reliably. The carrying amount of the replaced part is derecognized. The costs of the day-to-day maintenance and repairs are expensed as incurred.

2. Significant accounting policies (continued):

(f) Property and equipment (continued):

(iii) Depreciation:

Depreciation is recognized in net income and is amortized over the estimated useful life of the assets as follows:

Buildings	25 years
Computer hardware	3 years
Furniture and fixtures	20% declining balance
Vehicles	30% declining balance

Depreciation methods, useful lives and residual values are reviewed periodically and adjusted if necessary. Depreciation is prorated over the number of months of functional use in both the year of purchase and disposal.

(iv) Reclassification of real estate:

When the use of a property changes between owner-occupied and investment property, the property is reclassified based on its carrying value.

(g) Intangible assets:

Intangible assets consist of computer software which is not integral to the computer hardware owned by the Company. Software is recorded at cost less accumulated amortization and accumulated impairment losses. Software is amortized on a straight-line basis over its estimated useful life of 3 to 5 years. The amortization expense is included within the other operating expenses in the statement of income and comprehensive income.

(h) Insurance contracts:

(i) Classification:

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 the policyholder if a specified uncertain future event adversely affects the policyholder. Contracts not meeting the definition of insurance contracts are classified as investment contracts, derivative contracts or service contracts. The Company has reviewed all the contracts issued to its policyholders and concluded that they all meet the definition of insurance contracts.

2. Significant accounting policies (continued):

(h) Insurance contracts (continued):

(ii) Premiums and unearned premiums:

Premiums are taken into income on a pro rata basis over the contract period. Premiums on policies written with monthly payment terms are accounted for on an annualized basis. Premiums related to the unexpired portion of the policy at the end of the fiscal year are reflected in unearned premiums. Amounts receivable from policyholders represents the premiums due for the remaining months of the contracts. The Company records a liability for the unearned portion of premiums.

(iii) Deferred policy acquisition expenses:

Commissions, premium taxes and other acquisition costs related to securing new insurance contracts and renewing existing insurance contracts are deferred to the extent they are considered recoverable. All other costs are recognized as expenses when incurred. The deferred policy acquisition expenses are subsequently amortized over the terms of the related policies. To the extent they are considered non-recoverable, they are expensed as incurred.

(iv) Provision for unpaid claims and adjustment expenses:

The provision for unpaid claims is calculated based on Canadian accepted actuarial practice. The provision consists of case estimates prepared by claims adjusters and a provision for incurred but not reported claims “IBNR”. The estimates include related investigation, settlement and adjustment expenses. The valuation of claims liabilities, which is valued on a discounted basis, is disclosed in note 10.

(v) Liability adequacy test:

At the end of each reporting period, the Company performs a liability adequacy test on its insurance liabilities less deferred policy acquisition expenses to ensure the carrying value is adequate. In performing these tests, current best estimates of future contractual cash flows and claims handling and administration expenses, as well as investment income from the assets backing such liabilities are used. Any deficiency is immediately charged to income initially by writing off deferred policy acquisition expenses and by subsequently establishing a provision for losses arising from liability adequacy tests (the “premium deficiency”). Impairment losses resulting from liability inadequacy can be reversed in future years if the impairment no longer exists.

2. Significant accounting policies (continued):

(h) Insurance contracts (continued):

(vi) Reinsurance contracts held:

Contracts entered into by the Company with the reinsurer under which the Company is compensated for losses on one or more contracts issued by the Company and that meet the classification requirements for insurance contracts are classified as reinsurance contracts held.

Reinsurance does not relieve the Company of its liability to its policyholders and is reflected on the statement of financial position on a gross basis to indicate the extent of credit risk related to reinsurance and the obligations to policyholders.

The benefits to which the Company is entitled under its reinsurance contracts held are recognized as amounts recoverable from reinsurer (reinsurance asset). These assets consist of short-term balances due from reinsurer, as well as longer term receivables that are dependent on the expected claims and benefits arising under the related reinsured insurance contracts. Amounts recoverable from reinsurer are measured consistently with the amounts associated with the reinsured insurance contracts and in accordance with the terms of each reinsurance contract.

The Company assesses its reinsurance assets for impairment on a yearly basis. If there is objective evidence that the amount recoverable is impaired, the Company reduces the carrying amount of the reinsurance asset to its recoverable amount and recognizes that impairment loss in the statement of income and comprehensive income. The carrying amount is reduced through the use of an allowance account.

(vii) 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.

(i) Income taxes:

Income tax expense comprises current and deferred taxes. Current tax and deferred tax are recognized in income except to the extent that it relates to items recognized directly in equity or in OCI.

2. Significant accounting policies (continued):

(i) Income taxes (continued):

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to taxes payable in respect of previous years.

Deferred tax is a result of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amount used for tax purposes. Deferred tax assets are recognized only to the extent it is probable that sufficient taxable profits will be available against which the benefit of these deferred tax assets can be utilized.

Deferred tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Changes in deferred income taxes related to a change in tax rates are recognized in income in the period in which the tax change was enacted or substantively enacted.

Deferred income tax assets and liabilities are offset when they arise from the same taxation authority and the Company has both the legal right and the intention to settle on a net basis or to realize the asset and settle the liability simultaneously.

(j) Future changes in accounting policies:

(i) IFRS 9 *Financial Instruments* (“IFRS 9”):

In July 2014, the IASB published an amended version of IFRS 9 Financial Instruments, which replaces IAS 39 Financial Instruments: Recognition and Measurement, and includes guidance on the classification and measurement of financial instruments, impairment of financial assets, and a new general hedge accounting model. Financial asset classification is based on the cash flow characteristics and the business model in which an asset is held. The classification determines how a financial instrument is accounted for and measured. IFRS 9 also introduces a single impairment model for financial instruments not measured at fair value through profit or loss that requires recognition of expected credit losses at initial recognition of a financial instrument and the recognition of full lifetime expected credit losses if certain criteria are met. The new model for hedge accounting aligns hedge accounting with risk management activities. The financial reporting impact of adopting IFRS 9 is being assessed.

2. Significant accounting policies (continued):

(j) Future changes in accounting policies (continued):

(i) IFRS 9 *Financial Instruments* ("IFRS 9") (continued):

While the new standard is generally effective for years beginning on or after January 1, 2018, in December 2015 the IASB published an Exposure Draft Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts, which proposes to allow some insurers optional transitional relief until the forthcoming insurance accounting standard is available for implementation. The proposed options would allow (a) entities whose predominant activity is issuing insurance contracts within the scope of IFRS 4 to defer the implementation of IFRS 9 to as late as January 1, 2021, which may allow alignment of the implementation of IFRS 9 with the forthcoming insurance accounting standard, or alternatively (b) give entities issuing insurance contracts the option to remove from profit or loss the incremental volatility caused by changes in the measurement of specified financial assets upon application of IFRS 9.

(ii) IFRS 4 *Insurance Contracts* ("IFRS 4"):

In June 2013, the IASB issued a revised exposure draft proposing a comprehensive measurement approach for all types of insurance contracts, which would replace the existing IFRS 4 *Insurance Contracts*. Deliberations of the exposure draft continue and a final standard is expected to be issued in late 2016. The effective date of the final standard is not expected to be before 2020.

(iii) IFRS 15 *Revenue from Contracts with Customers* ("IFRS 15"):

In May 2014, the IASB issued a new standard that revises previous guidance on revenue recognition, from sources other than insurance premiums and investment income, which are unaffected. The financial reporting impact of adopting IFRS 15 is being assessed. The new standard is effective for years beginning on or after January 1, 2018.

(iv) IFRS 16 *Leases* (IFRS 16"):

IFRS 16 was issued on January 13, 2016. The new standard will replace existing lease guidance in IFRS and related interpretations, and requires companies to bring most leases on-balance sheet. The financial reporting impact of adopting IFRS 16 is being assessed. The new standard is effective for years beginning on or after January 1, 2019.

3. Significant judgments and estimates:

The Company makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgments are continually evaluated and based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The effect of a change in an accounting estimate is recognized in income in the period of the change, if the change affects that period only; or in the period of the change and future periods, if the change affects both.

(a) Significant judgments:

Significant judgments made in applying accounting policies are as follows:

(i) Impairments on AFS financial assets:

As of each reporting date, the Company evaluates AFS financial assets in an unrealized loss position for impairment on the basis described in note 2(e).

For investments in bonds and debentures, evaluation of whether impairment has occurred is based on the Company's best estimate of the cash flows expected to be collected at the individual investment level. The Company considers all available information relevant to the collectability of the investment, including information about past events, current conditions, and reasonable and supportable forecasts. Estimating such cash flows is a quantitative and qualitative process that incorporates information received from third party sources along with certain internal assumptions and judgments regarding the future performance of any underlying collateral for asset-backed securities. Where possible, this data is benchmarked against third party sources.

Impairments for bonds and debentures in an unrealized loss position are deemed to exist when the Company does not expect full recovery of the amortized cost of the investment based on the estimate of cash flows expected to be collected or when the Company intends to sell the investment prior to recovery from its unrealized loss position.

For equity investments, the Company recognizes an impairment loss in the period in which it is determined that an investment has experienced significant and prolonged losses and is not expected to recover to its cost.

There were no write-downs of AFS equities in 2015 (2014 - $nil).

3. Significant judgments and estimates (continued):

(b) Estimates:

Information about assumptions and estimation uncertainties that have a risk of resulting in material adjustment within the next 12 months are as follows:

(i) Provision for unpaid claims:

The Appointed Actuary is appointed by the Board of Directors of the Company. With respect to preparation of these consolidated financial statements, the Appointed Actuary is required to carry out a valuation of the policy liabilities and to provide an opinion to the Company's policyholders regarding their appropriateness at the reporting date. The factors and techniques used in the valuation are in accordance with accepted actuarial practice, applicable legislation and associated regulations.

Provisions for unpaid claims and adjustment expenses are valued based on Canadian accepted actuarial practice, which are designed to ensure the Company establishes an appropriate reserve on the statement of financial position to cover insured losses with respect to the reported and unreported claims incurred as of the end of each accounting period and claims expenses. The policy liabilities consist of the provisions for, and reinsurance recovery of, net actuarial liabilities under insurance policies, unpaid claims and adjustment expenses on insurance policies in force, and future obligations on the unearned portion of insurance policies in force, including deferred policy acquisition costs. In performing the valuation of the liabilities, the Appointed Actuary makes assumptions, which are by their nature inherently variable, as to future loss ratios, trends, rates of claims frequency and severity, inflation, reinsurance recoveries, investment rates of return, expenses and other contingencies, taking into consideration the circumstances of the Company and the nature of the insurance policies.

The assumptions underlying the valuation of provisions for unpaid claims are reviewed and updated by the Company on an ongoing basis to reflect recent and emerging trends in experience and changes in risk profit of the business.

(ii) Deferred policy acquisition expenses:

Deferred policy acquisition expenses are deferred and amortized in accordance with the accounting policy in note 2(h) (iii). The Company estimates expenses eligible for deferral based on the nature of expenses incurred.

(In thousands of dollars)

4. Invested assets:

(a) Classification:

The Company manages its investments according to the directives outlined in its Investment Policy Statement, which is reviewed and approved by the Finance and Audit Committee on an annual basis. The Company's financial risk management objectives are to maximize the long-term surplus of the Company, and to offset the effects of discounting the Company's claims liabilities at the fair value yield.

Invested asset balances at carrying values by financial instrument classification are as follows:

2015	Real Estate	FVTPL	AFS	Loans & Receivables	Total
Bonds:					
Federal government	$ ---	$ 20,859	$ ---	$ ---	$ 20,859
Provincial government	---	44,094	---	---	44,094
Corporate	---	32,726	---	---	32,726
Pooled funds:					
Canadian	---	---	7,987	---	7,987
Global	---	---	18,303	---	18,303
Commercial loans	---	---	---	478	478
Real estate	467	---	---	---	467
	$ 467	$ 97,679	$ 26,290	$ 478	$ 124,914

2014	Real Estate	FVTPL	AFS	Loans & Receivables	Total
Bonds:					
Federal government	$ ---	$ 24,955	$ ---	$ ---	$ 24,955
Provincial government	---	40,405	---	---	40,405
Corporate	---	29,649	---	---	29,649
Pooled funds:					
Canadian	---	---	6,559	---	6,559
Global	---	---	12,397	---	12,397
Commercial loans	---	---	---	711	711
Real estate	488	---	---	---	488
	$ 488	$ 95,009	$ 18,956	$ 711	$ 115,164

(In thousands of dollars)

4. Invested assets (continued):

(b) Fair value hierarchy:

The table below provides an analysis of the basis of measurement used to fair value financial instruments carried at fair value, categorized by the following fair value hierarchy:

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities

Level 2: 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)

Level 3: Inputs for the asset or liability not based on observable market data (unobservable inputs).

2015	Level 1	Level 2	Level 3	Total
Bonds:				
Federal government	$ ---	$ 20,859	$ ---	$ 20,859
Provincial government	---	44,094	---	44,094
Corporate	---	32,726	---	32,726
Pooled funds:				
Burgundy Canadian equity	7,987	---	---	7,987
Burgundy global equity	18,303	---	---	18,303
	$ 26,290	$ 97,679	$ ---	$ 123,969

2014	Level 1	Level 2	Level 3	Total
Bonds:				
Federal government	$ ---	$ 24,955	$ ---	$ 24,955
Provincial government	---	40,405	---	40,405
Corporate	---	29,649	---	29,649
Pooled funds:				
Burgundy Canadian equity	6,559	---	---	6,559
Burgundy global equity	12,397	---	---	12,397
	$ 18,956	$ 95,009	$ ---	$ 113,965

There were no transfers between Level 1 and Level 2 for the years ended December 31, 2015 and December 31, 2014. There were no Level 3 investments for the years ended December 31, 2015 and December 31, 2014.

(In thousands of dollars)

4. Invested assets (continued):

(c) Term to maturity:

2015	Within 1 year	1 - 5 years	5 - 10 years	10 years or more	Total
Bonds	$ 6,191	$ 64,828	$ 18,849	$ 7,811	$ 97,679
Pooled funds	26,290	---	---	---	26,290
Commercial loans	---	478	---	---	478
Total	$ 32,481	$ 65,306	$ 18,849	$ 7,811	$ 124,447
Percent of total	26.1%	52.5%	15.1%	6.3%	100.0%

2014	Within 1 year	1 - 5 years	5 - 10 years	10 years or more	Total
Bonds	$ 12,224	$ 55,161	$ 22,388	$ 5,236	$ 95,009
Pooled funds	18,956	---	---	---	18,956
Commercial loans	---	711	---	---	711
Total	$ 31,180	$ 55,872	$ 22,388	$ 5,236	$ 114,676
Percent of total	27.2%	48.7%	19.5%	4.6%	100.0%

The effective interest rate of the bonds portfolio held at December 31, 2015 is 1.89% (2014 – 2.0%).

5. Determination of fair values:

A number of the Company's accounting policies and disclosures require the determination of fair values for assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

As described in Note 4(b), the fair value of FVTPL and AFS financial assets is determined by reference to their quoted closing bid price at the reporting date (Level 1 fair values), or values determined based on market prices for similar assets and other observable inputs such as market interest rates (Level 2 fair values).

(In thousands of dollars)

6. Reinsurance:

The Company follows the policy of underwriting and reinsuring contracts of insurance, which limits the Company's exposure. The Company's retained risk is $400 in the case of each property claim, $1,200 each property catastrophe, $600 for each automobile and $500 for each general liability claim in 2015 (2014 - $400 for property, $1,200 for a property catastrophe, $600 for automobile and $500 for general liability).

7. Company pension plan:

The Company has a defined contribution pension plan for employees. The Company's portion of payments to the plan amounted to $367 in 2015 (2014 - $358) and these payments were charged to employee benefits expense as incurred.

8. Property and equipment:

	Land and land improvements	Buildings	Furniture and equipment	Computer equipment	Automobiles	Total
Cost or deemed cost:						
Balance, December 31, 2014	$ 1,100	$ 5,742	$ 1,933	$ 2,090	$ 438	$ 11,303
Additions	---	127	28	139	101	395
Disposals	---	---	---	---	(98)	(98)
Balance, December 31, 2015	$ 1,100	$ 5,869	$ 1,961	$ 2,229	$ 441	$ 11,600
Accumulated depreciation:						
Balance, December 31, 2014	$ ---	$ 402	$ 1,437	$ 1,784	$ 179	$ 3,802
Depreciation for the year	---	187	135	229	90	641
Disposals	---	---	---	---	(70)	(70)
Balance, December 31, 2015	$ ---	$ 589	$ 1,572	$ 2,013	$ 199	$ 4,373
Net book value:						
Balance, December 31, 2014	$ 1,100	$ 5,340	$ 496	$ 306	$ 259	$ 7,501
Balance, December 31, 2015	$ 1,100	$ 5,280	$ 389	$ 216	$ 242	$ 7,227

Depreciation of property and equipment included in operating expenses amounted to $641 in 2015 (2014 - $491).

(In thousands of dollars)

9. Intangible assets:

		Computer Software
Cost:		
Balance, December 31, 2014	$	3,102
Additions		644
Balance, December 31, 2015	$	3,746
Accumulated amortization:		
Balance, December 31, 2014	$	1,850
Amortization for the year		472
Balance, December 31, 2015	$	2,322
Net book value:		
December 31, 2014	$	1,252
December 31, 2015	$	1,424

Amortization of intangible assets included in operating expenses amounted to $472 in 2015 (2014 - $504).

10. Insurance contracts:

The following is a summary of the contract provisions and related reinsurance assets:

Gross		2015		2014
Outstanding claims provision	$	53,348	$	54,617
Provision for claims incurred but not reported		26,035		23,831
Effect of discounting		(3,001)		(3,050)
Provision for adverse deviations		7,604		7,264
Other		2,036		2,159
Total provision for gross unpaid claims and adjustment expenses	$	86,022	$	84,821

Ceded		2015		2014
Outstanding claims provision	$	16,069	$	15,519
Provision for claims incurred but not reported		4,354		2,973
Effect of discounting		(660)		(601)
Provision for adverse deviations		1,446		1,142
Other		---		---
Total reinsurer’s share of unpaid claims and adjustment expenses	$	21,209	$	19,033

(In thousands of dollars)

10. Insurance contracts (continued):

Net	2015	2014
Outstanding claims provision	$ 37,279	$ 39,098
Provision for claims incurred but not reported	21,681	20,858
Effect of discounting	(2,341)	(2,449)
Provision for adverse deviations	6,158	6,122
Other	2,036	2,159
Total provision for net unpaid claims and adjustment expenses	$ 64,813	$ 65,788

The following is a summary of the insurance contracts by line of business as at December 31, 2015 and December 31, 2014.

2015	Gross	Reinsurance ceded	Net
Long-term settlement:			
Automobile - Injury	$ 56,400	$ 14,050	$ 42,350
General liability	11,022	1,630	9,392
	67,422	15,680	51,742
Short-term settlement:			
Automobile	2,854	168	2,686
Property	11,137	4,575	6,562
	13,991	4,743	9,248
Total undiscounted	81,413	20,423	60,990
Discounting with PfAD	4,609	786	3,823
Total discounted insurance contract liabilities	$ 86,022	$ 21,209	$ 64,813

2014	Gross	Reinsurance ceded	Net
Long-term settlement:			
Automobile - Injury	$ 49,826	$ 8,435	$ 41,391
General liability	11,601	2,148	9,453
	61,427	10,583	50,844
Short-term settlement:			
Automobile	1,922	33	1,889
Property	17,258	7,876	9,382
	19,180	7,909	11,271
Total undiscounted	80,607	18,492	62,115
Discounting with PfAD	4,214	541	3,673
Total discounted insurance contract liabilities	$ 84,821	$ 19,033	$ 65,788

10. Insurance contracts (continued):

(a) Nature of the provision for unpaid claims:

The provision for unpaid claims represent an estimate of the amounts which, together with estimated future premiums and investment income, will be sufficient to pay outstanding claims, estimated future benefits, expenses and taxes on all policies in force.

(i) Methodology and assumptions:

Determining the provision for unpaid claims, adjustment expenses and the related reinsurer's share involves an assessment of the future development of claims. The provision for unpaid claims is determined using a range of accepted actuarial claims projection techniques determined based on the line of business. The key assumption in developing these estimates is that claims recorded to date will continue to develop in a similar manner in the future. Other factors include changing regulatory and legal environment, actuarial studies, professional experience and expertise of the Company's claims personnel and independent adjusters retained to handle individual claims, the effect of inflationary trends on future claims settlement costs, investment rates of return, court decisions, economic conditions and public attitudes.

The unpaid claims projections are reported net of non-reinsurance recoveries, including salvage and subrogation. The actuarially determined carrying value of unpaid claims and adjustment expenses is considered an indicator of fair value, as there is no ready market for the trading of insurance policy liabilities.

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

(ii) Canadian accepted actuarial practices:

Under Canadian accepted actuarial practice, the appropriate amount representing future obligations is defined as policy liabilities, which takes into consideration the time value of money and include provisions for adverse deviation. Consequently, the provisions for unpaid claims, adjustment expenses and related reinsurance recoveries have been recorded on a discounted basis. The discount rate used in the December 31, 2015 valuation was 1.89% (2014 - 1.93%).

For 2015 and 2014, the discount rate used to determine the actuarial value of claims liabilities is based on the yield of the Company's FVTPL bond portfolio, which has been matched to the claims liabilities. In assessing the risks associated with investment income, the Company considers the nature of the investment portfolio and the timing of claim payments and their matching to investment cash flows.

10. Insurance contracts (continued):

(a) Nature of the provision for unpaid claims (continued):

(iii) Methodology and assumptions (continued):

Future changes in the investment portfolio could change the value of these claims. A 1% increase in this rate would decrease claims liabilities by $1,491 (2014 - $1,507), while a 1% decrease in this rate would increase claims liabilities by $1,566 (2014 - $1,586).

The basic assumptions made in establishing actuarial liabilities are best estimates. To allow for possible deterioration in experience, and to increase the likelihood that the actuarial liabilities are adequate to pay future benefits, actuaries are required to include margins in some assumptions. A range of allowable margins is prescribed by the Canadian Institute of Actuaries relating to claim development, reinsurance recoveries and investment income variables. The effect of the margins produces the provision for adverse deviation which for December 31, 2015 amounted to $6,158 (2014 - $6,122) on a net basis.

(iv) Changes in assumptions:

These provisions for unpaid claims and adjustment expenses are estimates and, as such, are subject to variability, which could be material in the near term. Changes to the estimates could result from future events such as receiving additional claim information, changes in judicial interpretation of contracts or significant changes in severity or frequency of claims from past trends. In general, the longer the term required for the settlement of claims, the more variable the estimates. As additional experience and other data becomes available, the estimates could be revised. Any future changes in estimates would be reflected in the statement of income and comprehensive income for the period in which the change occurred. The historical studies are regularly compared to current emerging experience so that adjustments may be made as necessary.

The actual amount of ultimate claims can only be ascertained once all claims are closed. The effect of changes in assumptions is disclosed in note 15(a)(vi) sensitivity analysis.

(In thousands of dollars)

10. Insurance contracts (continued):

(b) Movements in insurance liabilities and reinsurance assets:

(i) The following changes have occurred in the provision for unearned premiums during the year.

	2015	2014
Provision for gross unearned premiums, beginning of year	$ 47,656	$ 44,705
Less: Reinsurer's share of unearned premiums, beginning of year	357	142
Provision for net unearned premiums, beginning of year	$ 47,299	44,563
Net premiums written	89,446	83,881
Less: net premiums earned	86,171	81,145
Change in provision for net unearned premiums	3,275	2,736
Provision for net unearned premiums, end of year	50,574	47,299
Plus: Reinsurer's share of unearned premiums, end of year	301	357
Provision for gross unearned premiums, end of year	50,875	$ 47,656

The net premiums earned of $86,171 (2014 - $81,145) represents the income arising from insurance contracts.

(ii) The table below summarizes the change in the provision for unpaid claims:

	2015	2014
Gross claims reserve, beginning of year	$ 84,821	$ 70,389
Current year claims	53,859	57,892
Prior year unfavourable claims development	667	1,885
Total claims incurred	54,526	59,777
Claims paid	(53,325)	(45,345)
Gross claims reserve, end of year	$ 86,022	$ 84,821

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

(In thousands of dollars)

10. Insurance contracts (continued):

(b) Movements in insurance liabilities and reinsurance assets (continued):

(iii) The following changes have occurred in the reinsurers' claims reserve:

		2015		2014
Reinsurer's share in claims reserve, beginning of year	$	19,030	$	14,097
Reinsurer's share in total claims incurred		11,273		9,258
Reinsurer's share in total claims payments		(9,094)		(4,322)
Reinsurer's share in claims reserve, end of year	$	21,209	$	19,033

(c) Structured settlements:

The Company has purchased a number of annuities with an estimated fair value of $1,077 in settlement of claims. These annuities have been purchased from registered Canadian life insurers with the highest claims paying ability ratings as determined by outside ratings organizations. The Company has a contingent credit risk with respect to the failure of these life insurers, with a maximum contingent credit risk applicable to any one life insurer of $2,730. Management has concluded that no provision for credit loss is required as at December 31, 2015.

(d) Claims development tables:

The following table shows the estimates of cumulative incurred claims, including both claims notified and IBNR for each successive loss year at each reporting date, together with cumulative payments to date.

THE NORTH WATERLOO FARMERS MUTUAL INSURANCE COMPANY

Notes to Consolidated Financial Statements (continued)
(In thousands of dollars)

Year ended December 31, 2015

10. Insurance contracts (continued):

(d) Claims development tables (continued):

Gross basis:

				Total all Insurance risks					
Year of loss	2007	2008	2009	2010	2011	2012	2013	2014	2015
Estimate of ultimate claims costs at end									
of the year of loss	$ 32,059	$ 41,584	$ 32,600	$ 33,162	$ 47,525	$ 42,352	$ 40,075	$ 54,680	$50,871
one year later	31,049	41,400	33,579	31,892	49,244	41,725	40,716	54,448	---
two years later	30,656	41,567	32,922	32,312	48,412	43,454	42,728	---	---
three years later	31,757	41,153	32,603	31,645	49,183	44,317	---	---	---
four years later	31,513	41,032	33,337	31,804	49,876	---	---	---	---
five years later	31,357	40,158	33,363	31,591	---	---	---	---	---
six years later	31,189	39,673	33,359	---	---	---	---	---	---
seven years later	31,175	39,358	---	---	---	---	---	---	---
eight years later	30,999	---	---	---	---	---	---	---	---
Current estimate of ultimate claims	30,999	39,358	33,359	31,591	49,876	44,317	42,728	54,448	50,871
Cumulative payments to date	$ 30,804	$ 38,805	$ 32,012	$ 28,839	$ 43,651	$ 29,969	$31,420	$40,418	$26,301

(In thousands of dollars)

10. Insurance contracts (continued):

(d) Claims development tables (continued)

Net basis:

					Total all Insurance risks					
Year of loss	2007	2008	2009	2010	2011	2012	2013	2014	2015	Total
Estimate of ultimate claims costs at end										
of the year of loss	$ 25,703	$ 34,322	$ 29,951	$ 30,537	$ 37,443	$ 33,470	$ 37,336	$ 47,104	$44,017	
one year later	24,808	34,706	30,629	30,010	38,528	33,073	37,379	46,355	---	
two years later	24,592	34,313	29,827	30,717	38,981	34,486	37,908	---	---	
three years later	25,639	34,076	30,485	30,378	38,902	34,431	---	---	---	
four years later	25,224	34,678	30,484	30,549	38,577	---	---	---	---	
five years later	25,039	33,253	30,411	29,921	---	---	---	---	---	
six years later	25,109	33,265	30,527	---	---	---	---	---	---	
seven years later	24,956	33,180	---	---	---	---	---	---	---	
eight years later	24,788	---	---	---	---	---	---	---	---	
Current estimate of ultimate claims	24,788	33,180	30,527	29,921	38,577	34,431	37,908	46,355	44,017	
Cumulative payments to date	24,646	32,814	29,298	27,638	34,419	27,151	28,597	34,822	24,843	
Outstanding claims	$ 142	$ 366	$ 1,229	$ 2,283	$ 4,158	$ 7,280	$ 9,311	$ 11,533	$ 19,174	$ 55,476
Outstanding claims 2006 and prior										153
Unallocated loss adjustment expense										3,330
Facility Association										2,031
Effect of discounting and PfAD										3,823
Liability recoverable from reinsurers										21,209
Gross liabilities in statement of financial position										$ 86,022

(In thousands of dollars)

11. Income taxes:

(a) Components of income tax expense:

The major components of income tax expense are:

		2015		2014
Current tax expense:				
Current period taxes on income	$	1,586	$	426
Adjustment for prior years		(37)		(343)
Deferred tax expense				
Origination and reversal of temporary differences		(58)		(103)
Reduction in tax rate		12		3
Total income tax expense (recovery)	$	1,503	$	(17)
Income tax recognized in other comprehensive income:				
Unrealized gain on AFS financial assets	$	424	$	379
Total income charged directly to OCI	$	424	$	379

(b) Reconciliation of effective tax rate:

The Company's provision for income taxes varies from the expected provision at statutory rates for the following reasons:

		2015		2014
Income before income taxes	$	8,584	$	1,417
Exempt portion		(2,765)		(649)
Income subject to tax		5,819		768
Combined basic Canadian federal and provincial income tax rate		26.5%		26.5%
Provision based on combined basic income tax rate		1,542		203
Legislated change in prior year tax rate		12		59
Other decrease in taxes		(51)		(279)
Income tax expense (recovery)	$	1,503	$	(17)

(In thousands of dollars)

12. Deferred tax assets and liabilities:

(a) Recognized deferred tax assets and liabilities:

Deferred tax assets and liabilities are attributable to the following:

2015		Assets		Liabilities		Net
Property and equipment	$	---	$	(346)	$	(346)
Available-for-sale financial assets		---		(24)		(24)
Provisions		588		---		588
Net tax assets (liabilities)	$	588	$	(370)	$	218

2014		Assets		Liabilities		Net
Property and equipment	$	---	$	(423)	$	(423)
Available-for-sale financial assets		---		(28)		(28)
Provisions		623		---		623
Net tax assets (liabilities)	$	623	$	(451)	$	172

(b) Movement in temporary differences during the year:

	Property and equipment	AFS financial assets	Provisions	Other items	Total
Balance, December 31, 2013	$ (431)	$ (32)	$ 535	$ ---	$ 72
Recognized in income	8	---	88	---	96
Recognized in OCI	---	4	---	---	4
Balance, December 31, 2014	$ (423)	$ (28)	$ 623	$ ---	$ 172
Recognized in income	77	---	(35)	---	42
Recognized in OCI	---	4	---	---	4
Balance, December 31, 2015	$ (346)	$ (24)	$ 588	$ ---	$ 218

(In thousands of dollars)

13. Equity:

Accumulated Other Comprehensive Income:

AOCI is comprised of unrealized gain (loss) on equity investments designated AFS financial assets. AFS differences comprise the cumulative net change in the fair value of AFS financial assets until the investments are derecognized or impaired.

14. Related party transactions:

The Company entered into the following transactions with key management personnel. Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company, including all directors, executive, non-executives and senior management.

	2015	2014
Compensation:		
Salaries and short term employee benefits and directors' fees	$ 1,297	$ 1,499
Total pension and other post-employment benefits	107	97
	$ 1,404	$ 1,596
Premiums	$ 23	$ 36
Claims paid	$ ---	$ 6

Amounts were owing to key management personnel at December 31, 2015 totalling $nil (2014 - $nil) and $2 (2014 - $1) was due from key management personnel. The amounts are included in due from policyholders and accounts payable and accrued liabilities on the statement of financial position.

15. Financial risk management:

The primary goals of the Company's financial risk management are to ensure that the outcomes of activities involving elements of risk are consistent with the Company's objectives and risk tolerance, and to maintain an appropriate risk/reward balance while protecting the Company's statement of financial position from events that have the potential to materially impair its financial strength.

15. Financial risk management (continued):

Risks identified as potentially significant are managed through a combination of Board policy, management monitoring and other management practices. The Company's Investment Policy Statement establishes asset mix parameters and risk limits to help minimize undue exposure to these risks in the investment portfolio while attempting to maximize the long-term value of policyholders' surplus. The Investment Policy Statement is reviewed annually by the Finance and Audit Committee. Compliance with the Investment Policy is monitored quarterly by the Finance and Audit Committee of the Board of Directors.

The Company’s exposure to potential loss is primarily due to underwriting risk along with various market risks, including interest rate risk, liquidity risk, as well as credit risk.

(a) Underwriting risk:

Underwriting risk is the risk that the total cost of claims and acquisition expenses will exceed premiums received and can arise from numerous factors, including pricing risk, reserving risk, catastrophic loss risk and reinsurance coverage risk.

Our underwriting objective is to develop business within our target market on a prudent and diversified basis and to achieve profitable underwriting results.

In Canada, automobile insurance premium rates, other than for fleet automobile, are regulated by provincial government authorities. Regulation of premium rates is based on claims and other costs of providing insurance coverage, as well as projected profit margins. Regulatory approvals can limit or reduce premium rates that can be charged, or delay the implementation of changes in rates. Accordingly, a significant portion of the Company's revenue is subject to regulatory approval.

The business risk of insurance is primarily in pricing and underwriting the product, in managing investment funds, and in estimating and settling claims. To mitigate some of its risks, the Company purchases reinsurance to share part of the risk originally accepted in writing the policy. The Company cedes approximately 11.1% (2014 - 10.6%) of its premiums with external reinsurers. The Company has established risk management policies and procedures to measure and control risk. These policies and procedures are reviewed periodically by senior management, the Board of Directors, external auditors and regulators.

15. Financial risk management (continued):

(a) Underwriting risk (continued):

(i) Pricing risk:

Pricing risk arises when actual claims experience differs from the assumptions included in pricing calculations. Historically, the underwriting results of the property and casualty industry have fluctuated significantly due to the cyclicality of the insurance market. The market cycle is affected by the frequency and severity of losses, levels of capacity and demand, general economic conditions and price competition. Our pricing process is designed to ensure an appropriate return on capital while also providing long-term rate stability. These factors are reviewed and adjusted regularly to ensure our prices are responsive to the current environment and competitor behaviour.

(ii) Reserving risk:

Reserving risk arises due to the length of time between the occurrence of a loss, the reporting of the loss to the insurer and ultimate resolution of the claim.

Claim provisions are expectations of the ultimate cost of resolution and administration of claims based on an assessment of facts and circumstances then known, a review of historical settlement patterns, estimates of trends in claim severity and frequency, legal theories of liability and other factors. Variables in the reserve estimation process can be affected by receipt of additional claim information and other internal and external factors, such as changes in claims handling procedures, economic inflation, legal and judicial trends, legislative changes, inclusion of exposures not contemplated at the time of policy inception, and significant changes in severity or frequency of claims relative to historical trends. Due to the amount of time between the occurrence of a loss, the actual reporting of the loss and the ultimate payment, provisions may ultimately develop differently from the assumptions made when initially estimating the provision for claims.

Reserving risk is reduced through various internal and external control processes including: minimum reserve standards, quality assurance reviews, monthly review, and legal counsel. The year-end provision for unpaid claims is reviewed by an independent appointed actuary who reports on the adequacy of the reserves. The work of the appointed actuary is also subject to audit and peer review.

15. Financial risk management (continued):

(a) Underwriting risk (continued):

(iii) Regulatory risk:

Regulation covers a number of areas including solvency, change in control and capital movement limitations. The Company works closely with regulators and monitors regulatory developments to assess their potential impact on its ability to meet solvency and other requirements.

In Ontario, automobile insurance premium rates, other than for fleet automobile, are regulated by provincial government authorities. Regulation of premium rates is based on claims and other costs of providing insurance coverage, as well as projected profit margins. Regulatory approvals can limit or reduce premium rates that can be charged, or delay the implementation of changes in rates. Accordingly, a significant portion of the Company's revenue is subject to regulatory approvals.

(iv) Concentration risk:

The Company writes property and casualty insurance contracts over twelve-month durations. The most significant risks arise from natural disasters, climate change and other catastrophes. The Company has a reinsurance program to limit the exposure to catastrophic losses from any one event.

The Company has a concentration of business in automobile and property insurance in the province of Ontario. For the year ended December 31, 2015, automobile premiums represented 38.2% (2014 - 40.0%) and property premiums represented 61.8% (2014 - 60.0%) of gross written premiums. Of gross written premiums in 2015, Ontario accounted for 100% (2014 - 100%).

(v) Catastrophic loss risk:

Catastrophic loss risk is the exposure to losses resulting from multiple claims arising out of a single catastrophic event. Property and casualty insurance companies experience large losses arising from man-made or natural catastrophes that can result in significant underwriting losses. Catastrophes can cause losses in a variety of property and casualty lines and may have continuing effects which could delay or hamper efforts to timely and accurately assess the full extent of the damage they cause. The incidence and severity of catastrophes are inherently unpredictable. The Company evaluates catastrophic events and assesses the probability of occurrence and magnitude of catastrophic events through various modeling techniques and through the aggregation of limits exposed. The Company's exposure to catastrophic loss is also managed through geographic and product diversification as well as through the use of reinsurance.

15. Financial risk management (continued):

(a) Underwriting risk (continued):

(v) Catastrophic loss risk:

The Company reinsures claims from a single catastrophe when the sum exceeds $1,200 (2014 - $1,200) represents less than 1.7% (2014 – 2.0%) of the Company's policyholder's equity. Reinsurance coverage risk arises because reinsurance terms, conditions and/or pricing may change on renewal, particularly following catastrophes.

(vi) Sensitivity analysis:

The Company has exposures to risks in each class of business that may develop and that could have a material impact on the Company's financial position. Risks associated with property and casualty insurance contracts are complex and subject to a number of variables which complicate quantitative sensitivity analysis. The Company considers that the liability for its unpaid claims and adjustment expenses is adequate. However, actual experience will differ from the expected outcome.

To ensure that the Company has sufficient capital to withstand a variety of significant and plausible adverse event scenarios, the Company performs Dynamic Capital Adequacy Testing ("DCAT") on the capital adequacy of the Company. DCAT is performed annually as required by the Canadian Institute of Actuaries, and is prepared by the appointed actuary. The adverse event scenarios are reviewed annually to ensure that the appropriate risks are included in the DCAT process. Plausible adverse event scenarios used include consideration of claims frequency and severity risk, inflation risk, premium risk, reinsurance risk and investment risk. The exposure of the peril of earthquake with default of reinsurers is also applied in a stress test analysis. The most recent results indicated that the Company's future financial and capital positions are satisfactory under the assumptions applied.

(b) Credit risk:

Credit risk is the risk of financial loss as the result of the Company's counterparties not being able to meet payment obligations as they become due. The Company's credit risk is concentrated in the bond portfolio. Unless otherwise stated, the Company's credit exposure is limited to the carrying amount of these assets.

15. Financial risk management (continued):

(b) Credit risk (continued):

(i) Invested assets:

The Company's Investment Policy Statement requires the Company to invest in bonds and preferred stocks of high credit quality and to limit exposure with respect to any one issuer. No more than 10% of the market value of the bond portfolio may be in any one issuer, except for Federal or Provincial issuers with at least an “AA” rating. At least 95% of all bonds shall be rated not less than “A” or equivalent and remaining 5% shall be rated not less than “BBB” or equivalent. Common shares, preferred stocks or convertible securities of Canadian Corporations, cannot represent more than 30% of the market value of the equity portfolio. Common shares, preferred shares or convertible securities of US Corporations cannot represent more than 30% of the market value of the equity portfolio and common shares of a non-controlling interest or an external segregated mutual fund comprising common shares of US Corporations. Not more than 5% of the equity portfolio shall be invested in any one corporation unless when invested in an equity pooled fund where not more than 10% shall be invested in any one corporation and any investments in a single industry group should not exceed 25% of the equity portfolio unless invested in an equity pooled fund where not more than 35% shall be invested in a single industry group. 100% of the bonds held at December 31, 2015 (2014 - 99.8%) were rated "BBB" or better. The Company did not own any preferred stock as at December 31, 2015 and December 31, 2014.

The Company performed a review of all AFS securities with unrealized losses at December 31, 2015 and concluded that, due to no objective evidence of impairment, a provision for impairment was not required.

The Company periodically lends amounts to brokers in order to finance the growth of their business. Sufficient collateral, in the form of an assignment over the ownership interest in the brokerage, is held to protect the Company against default on these loans. Annual financial reviews are undertaken to determine if the broker will be able to make the required payments when due. The Company's credit exposure on these loans is limited to the carrying value of commercial broker loans as disclosed in note 4(a). At December 31, 2015, all loans are neither past due nor impaired and, therefore, no provision is required.

The Company's broker appointment process ensures a full financial review of each brokerage before they are granted a contract. This review includes an assessment by the finance department on the ability of the brokerage to meet payment obligations as they become due. Periodic broker reviews are conducted to ensure continued profitability or solvency.

(In thousands of dollars)

15. Financial risk management (continued):

(b) Credit risk (continued):

(ii) Reinsurance recoverable and receivables:

The Company relies on reinsurance to manage underwriting risk, however, reinsurance does not release the Company from its primary commitments to its policyholders. Therefore, the Company is exposed to the credit risk associated with the amounts ceded to reinsurers.

The Company regularly assesses the financial soundness of the reinsurer it deals with. An allowance for losses on reinsurance contracts is established when a reinsurance counterparty becomes unable or unwilling to fulfill its contractual obligations. The allowance for loss is based on current recoverable and ceded claim liabilities. No information has come to the Company's attention indicating weakness or failure of its current reinsurer; consequently, no impairment provision has been made in the accounts due to credit risks. The Company's credit exposure to any one individual policyholder included in premiums receivable from policyholders is not material.

The following table summarizes the Company’s maximum exposure to credit risk related to financial instruments. The maximum credit exposure is the carrying value of the asset net of any allowances for losses:

	2015	2014
Cash and cash equivalents	$ 19,659	$ 16,163
Bonds	97,679	95,009
Commercial loans	478	711
Accrued investment income	580	627
Due from brokers	4,231	4,057
Premium receivable from policyholders	20,672	19,727
Unpaid claims and adjustment expenses	21,209	19,033
Insurance and other receivables	395	1,769
Structured settlements	--	--
	$ 165,980	$ 157,096

15. Financial risk management (continued):

(c) 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 currency 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 assets are traded. Below is a discussion of the Company's primary market risk exposures and how those exposures are currently managed.

(i) Interest rate risk:

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments. Typically, investment income will be reduced during sustained periods of low interest rates but this will also create unrealized gains within the bond portfolio. It will also create realized gains to be recognized in net income to the extent any bonds are sold during the period. The reverse is true during a sustained period of increasing interest rates.

Duration is a measure used to estimate the extent fair values of fixed income instruments change with changes in interest rates. Using this measure, it is estimated that an immediate hypothetical 100 basis points or 1% parallel increase in interest rates, with all other variables held constant, would decrease the fair value of FVTPL bonds as well as net income by $4,086 (2014 - $3,777). Similarly, a 100 basis point or 1% parallel decrease in interest rates would generate a corresponding increase in the fair value of FVTPL bonds and net income. For both FVTPL and AFS bonds that the Company sold during the period, the change in fair market value would be recognized as part of "Realized gain on sale of investments" in net income during the period.

(ii) Equity market risk:

Economic trends, the political environment and other factors can positively and adversely impact the equity markets and consequently the value of equity investments the Company holds. The Company's portfolio includes Canadian equities with fair values that move as a result of market pressures as reflected in the Toronto Stock Exchange Composite Index, and foreign index equities that move with the Standard & Poor's 500 Index as the Canadian and foreign equities are all classified as AFS investments. A 10% movement in the stock markets, with all other variables held constant, would have an estimated effect on the fair values of the Company's Canadian and foreign equities and OCI of $2,629 (2014 - $1,896) to the extent the Company did not dispose of the equities during the period. For equities that the Company sold during the period, the impact would be recognized as part of "Realized gain on sale of investments" in net income during the period.

15. Financial risk management (continued):

(c) Market risk (continued):

(iii) Foreign exchange risk:

Foreign exchange risk is the risk that the value of a financial instrument will fluctuate due to change in foreign exchange rates. The Company's foreign exchange risk is related to the underlying investments in its pooled fund investments.

Of the pooled fund investments 4.3% is cash, 26.1% are Canadian equities, 40.2% are US equities, 23.5% are European equities, 4.7% are Asian equities and 1.2% are Emerging Market equities. (2014 - 5.9% is cash, 39.2% are Canadian equities, 33.2% are US equities, 17.1% are European equities, 3.8% are Asian equities and 0.8% are Emerging Market equities).

(d) Liquidity risk:

Liquidity risk is the risk of having insufficient cash resources to meet current financial obligations. Liquidity risk arises from the Company's general business activities and in the course of managing the assets and liabilities. The liquidity requirements of the Company's business are met primarily by funds generated by operations, asset maturities and investment returns. Cash provided from these sources normally exceeds cash requirements to meet claims costs and operating expenses.

At December 31, 2015, the Company had $19,659 (2014 - $16,163) of cash and cash equivalents. The Company also has a highly liquid investment portfolio. Canadian fixed-income securities issued or guaranteed by domestic governments and investment grade corporate bonds held by the Company had a fair value of $97,679 as at December 31, 2015 (2014 - $95,009).

The maturity profile of the Company's investment portfolio is shown in note 4(c). The Company's bond portfolio designated as FVTPL is managed to match the Company's claim liability profile in order to ensure sufficient funding to meet claim liabilities.

The Company believes that it has the flexibility to obtain, from internal sources, the funds needed to meet cash and regulatory requirements on an ongoing basis.

16. Capital management:

Management develops the capital strategy for the Company and oversees the capital management processes. As a federally regulated property and casualty insurance company, the Company's capital position is monitored by the Office of the Superintendent of Financial Institutions “OSFI”. OSFI evaluates the Company's financial strength through the Minimum Capital Test ("MCT") which measures available capital against required risk-weighted capital. Available capital comprises total policyholders' surplus plus or minus adjustments prescribed by OSFI. Capital required is calculated by applying risk factors to the assets and liabilities of the Company. The Company’s MCT is 319% (2014 - 289%).Management actively monitors the MCT ratio and the effect that external and internal actions have on the capital base of the Company. In particular, management determines the effect on capital before entering into any significant transactions to ensure that policyholders are not put at risk through the depletion of capital to unacceptable levels.

Reinsurance is also used to protect the Company's capital level from large losses, including those of a catastrophic nature, which could have a detrimental impact on capital. The Company has adopted policies that specify tolerance for financial risk retention. Once the retention limits are reached, reinsurance is utilized to cover the excess risk.

On an annual basis, the Company performs a Dynamic Capital Adequacy Testing on the MCT ratio to ensure that the Company has sufficient capital to withstand certain significant adverse event scenarios.

17. Operations subject to rate regulation:

The Company writes insurance only in the Province of Ontario. Auto insurance in Ontario is regulated by the Financial Services Commission of Ontario. Underwriting rules, risk selection criteria and pricing are all subject to review and approval by the regulator, prior to implementation. Auto insurance represents 38.2% (2014 - 40.0%) of the direct premium written of the Company.

18. Subsequent event – formation of Heartland Farm Mutual Inc.:

On January 16, 2015, the Company entered into a merger agreement with another farm mutual insurance company, Oxford Mutual Insurance Company, providing for the amalgamation of the two companies. On August 27, 2015, the mutual policyholders of both companies voted and approved the amalgamation of the two companies to create Heartland Farm Mutual Inc. The amalgamation was completed January 1, 2016.

18. Subsequent event – formation of Heartland Farm Mutual Inc. (continued):

The following is the estimated consolidated opening balance sheet of the amalgamated company on January 1, 2016, reflecting the audited December 31, 2015 financial statements of the predecessor companies, but without reflecting any fair value adjustments to property and intangible assets that may be reflected in the 2016 financial statements of Heartland Farm Mutual Inc.

Estimated Consolidated Statement of Financial Position as of January 1, 2016
(In thousands of dollars)

	North Waterloo Farmers Mutual Insurance Company	Oxford Mutual Insurance Company	Heartland Farm Mutual Inc.
Assets			
Cash and cash equivalents	$ 19,659	$ 2,022	$ 21,681
Invested assets	124,914	23,468	148,382
Due from brokers	4,231	3,163	7,394
Premiums receivable from policyholders	20,672	---	20,672
Accrued investment income	580	5	585
Insurance and other receivables	395	11	406
Income taxes receivable	---	183	183
Deferred income taxes	218	30	248
Reinsurers' share of:			
Unearned premiums	301	---	301
Unpaid claims and adjustment expenses	21,209	1,463	22,672
Deferred policy acquisition costs	13,703	871	14,574
Property and equipment	7,227	887	8,114
Intangible assets	1,424	---	1,424
Other assets	396	97	493
	$ 214,929	$ 32,200	$ 247,129
Liabilities			
Expenses due and accrued	$ 2,272	$ 541	$ 2,813
Due to other insurers	1,690	3	1,693
Due to brokers	3,410	78	3,488
Income taxes payable	642	---	642
Provision for unpaid claims	86,022	7,645	93,667
Unearned reinsurance commissions	48	---	48
Unearned premiums	50,875	5,535	56,410
	144,959	13,802	158,761
Surplus for the protection of policyholders			
Policyholders' equity	64,096	18,398	82,494
Accumulated other comprehensive income	5,874	---	5,874
	69,690	18,398	88,368
	$ 214,929	$ 32,200	$ 247,129

(In thousands of dollars)

18. Subsequent event – formation of Heartland Farm Mutual Inc. (continued):

The following is the summarized pro forma information from the statement of income and comprehensive income of the amalgamated company, as if the amalgamation had been completed at the beginning of the year, on January 1, 2015:

	North Waterloo Farmers Mutual Insurance Company	Oxford Mutual Insurance Company	Heartland Farm Mutual Inc.
Gross written premiums	$ 100,656	$ 11,599	$ 112,225
Net income	7,081	572	7,653
Total comprehensive income	8,992	572	9,564