Hay Mutual Insurance Company

Financial Statements

For the year ended December 31, 2009

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Contents

MANAGEMENT REPORT

Management Statement on Responsibility for Financial Reporting

The financial statements are the responsibility of management and have been prepared in conformity with Canadian generally accepted accounting principles including the accounting requirements of the Financial Services Commission of Ontario. In the opinion of management, the financial statements fairly reflect the financial position, results of operations and cash flows of Hay Mutual Insurance Company within reasonable bounds of materiality.

Preparation of financial information is an integral part of management's broader responsibilities for the ongoing operations of the Company. Management maintains a system of internal accounting controls to ensure that transactions are accurately recorded on a timely basis, are properly approved and result in reliable financial information. The Board of Directors is responsible for approving the financial statements.

The Financial Services Commission of Ontario makes an annual examination and inquiry into the affairs of the Company as deemed necessary to ensure that the Company is in sound financial condition and that the interests of the policyholders are protected under the provisions of the Insurance Act of Ontario.

Auditors' Report

To the Policyholders of
Hay Mutual Insurance Company

We have audited the balance sheet of Hay Mutual Insurance Company as at December 31, 2009 and the statements of operations, comprehensive income (loss), unappropriated policyholders' surplus and accumulated other comprehensive loss, and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2009 and the results of its operations and cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

The prior year figures were audited by another firm of Chartered Accountants.

BDO Canada LLP

Chartered Accountants, Licensed Public Accountants

Strathroy, Ontario
January 15, 2010

Hay Mutual Insurance Company

Balance Sheet

December 31	2009	2008
Assets		
Cash	$ 170,581	$ 178,749
Investments (Note 2)	28,988,177	26,858,307
Accrued investment income	195,045	173,916
Receivables (Note 3)	1,458,701	1,314,474
Prepaid expenses	38,888	148,549
Unpaid claims and adjusting expenses recoverable from reinsurer (Note 4)	2,500,859	4,902,859
Current income taxes recoverable (Note 7)	-	156,856
Future income tax benefit	88,943	191,171
Deferred policy acquisition costs	363,253	344,754
Capital assets (Note 5)	1,977,023	2,047,618
	$ 35,781,470	$ 36,317,253
Liabilities and Policyholders' Surplus		
Unpaid claims and adjusting expenses (Note 4)	$ 4,922,732	$ 8,886,500
Unearned premiums (Note 6)	3,664,106	3,481,829
Due to reinsurer and other insurance companies	307,112	334,828
Accounts payable and accrued liabilities	1,088,631	127,860
Current income taxes payable (Note 7)	345,477	-
	10,328,058	12,831,017
Policyholders' surplus		
Unappropriated policyholders' surplus	26,154,760	25,023,052
Accumulated other comprehensive loss	(701,348)	(1,536,816)
	25,453,412	23,486,236
	$ 35,781,470	$ 36,317,253

On behalf of the Board:

_______________ Director

_______________ Director

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

Hay Mutual Insurance Company

Statement of Operations

For the year ended December 31	2009	2008
Gross premiums written	**$ 7,870,240**	$ 7,442,326
Deduct		
Reinsurance premiums	**1,656,130**	1,498,378
Increase in unearned premiums	**182,277**	116,296
Net premiums earned	**6,031,833**	5,827,652
Service charge revenue	**80,118**	70,230
Total underwriting revenue	**6,111,951**	5,897,882
Claims and expenses incurred		
Net claims and adjusting expenses (Note 4)	**2,547,483**	4,195,019
General	**1,565,220**	1,163,299
Commissions	**764,134**	735,804
Premium tax	**17,290**	21,382
	4,894,127	6,115,504
Underwriting income (loss) before premium refunds	**1,217,824**	(217,622)
Refund of premiums to policyholders	**1,000,000**	-
Underwriting income (loss) for the year	**217,824**	(217,622)
Net investment income	**1,228,201**	1,288,768
Gain on disposal of capital assets	**-**	120,705
Income before income taxes for the year	**1,446,025**	1,191,851
Income taxes (Note 7)		
Current income taxes	**291,317**	186,956
Future income taxes	**23,000**	26,000
	314,317	212,956
Net income for the year	**$ 1,131,708**	$ 978,895

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

Hay Mutual Insurance Company

Statement of Comprehensive Income (Loss)

For the year ended December 31	2009	2008
Net income for the year	**$ 1,131,708**	$ 978,895
Other comprehensive income (loss) for the year		
Change in unrealized gain (loss) on available-for-sale investments		
Debt securities	**(3,342)**	(9,909)
Equities	**1,036,315**	(1,629,341)
Income tax effect	**(197,505)**	311,621
	835,468	(1,327,629)
Comprehensive income (loss) for the year	**$ 1,967,176**	$ (348,734)

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

Hay Mutual Insurance Company

Statement of Unappropriated Policyholders' Surplus and Accumulated Other Comprehensive Loss

For the year ended December 31	2009	2008
Unappropriated Policyholders' Surplus		
Balance, beginning of year	**$ 25,023,052**	$ 24,044,157
Net income for the year	**1,131,708**	978,895
Balance, end of year	**$ 26,154,760**	$ 25,023,052
Accumulated Other Comprehensive Loss		
Balance, beginning of year	**$ (1,536,816)**	$ (209,187)
Other comprehensive income (loss) for the year	**835,468**	(1,327,629)
Balance, end of year	**$ (701,348)**	$ (1,536,816)

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

Hay Mutual Insurance Company
Statement of Cash Flows

For the year ended December 31	2009	2008
Cash provided by (used in)		
Operating activities		
Net income for the year	$ 1,131,708	$ 978,895
Adjustments to convert income to a cash basis:		
Amortization of capital assets	127,593	42,239
Amortization of premium on bonds	5,987	1,401
Gain on disposal of capital assets	-	(120,705)
Income tax effect of other comprehensive income	(197,505)	311,621
Increase in receivables	(144,227)	(12,708)
Decrease (increase) in prepaid expenses	109,661	(148,549)
Decrease (increase) in accrued investment income	(21,129)	15,912
Decrease (increase) in reinsurer's share of provision of unpaid claims	2,402,000	(1,047,535)
Decrease (increase) in income taxes payable/recoverable	502,333	(105,003)
Increase in deferred policy acquisition costs	(18,499)	(11,688)
Decrease (increase) in future income tax benefit	102,228	(87,978)
Decrease in accounts payable and accrued liabilities	960,771	(140,846)
Decrease in refund due to policyholders	-	(400,000)
Decrease in due to reinsurer and other insurance companies	(27,716)	(14,931)
Increase (decrease) in unpaid claims and adjusting expenses	(3,963,768)	1,752,276
Increase in unearned premiums	182,277	116,296
	1,151,714	1,128,697
Investing activities		
Proceeds on sale and maturity of investments	5,578,562	6,930,001
Purchase of investments	(6,681,446)	(6,874,031)
Purchase of capital assets	(56,998)	(1,440,730)
Proceeds on disposal of capital assets	-	201,050
	(1,159,882)	(1,183,710)
Decrease in cash during the year	(8,168)	(55,013)
Cash and equivalents, beginning of year	178,749	233,762
Cash and equivalents, end of year	$ 170,581	$ 178,749

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

Nature of Business

The Company is incorporated without share capital under the laws of Ontario as a mutual insurance company. The Company is subject to the Ontario Insurance Act and is licensed to write automobile, hail, property and liability insurance, in the province of Ontario.

The accounting policies of the Company conform with those generally accepted in Canada and comply with the requirements for filing with the Financial Services Commission of Ontario.

Revenue Recognition

Insurance premiums are included in income on a daily pro-rata basis over the life of the policies. Unearned premiums represent the portion of premiums written that relates to the unexpired term of the policies in force.

Investment income includes dividend income, interest income and gains (losses) on the sale of investments. Dividend income is recognized when declared and interest income is recognized using the effective yield method. Gains or losses on the sale of investments are recognized on the transaction date.

Deferred Policy Acquisition Costs

Policy acquisition costs related to unearned premiums, comprising commissions, premium taxes and an allocation of other variable policy issue and underwriting expenses, are deferred and amortized to income over the period in which the premiums are earned. The method followed in determining the deferred acquisition costs limits the amount of the deferral to its realizable value by giving consideration to claims and expenses expected to be incurred as the premiums are earned.

Unpaid Claims and Adjusting Expenses

The provision for unpaid claims and adjusting expenses includes individual claim estimates for the full amount of all costs including investigation and the projected final settlements for losses, which occurred prior to the balance sheet date. In addition, a further provision is made in respect of incurred but not reported claims and development of losses on all outstanding claims. The provision does not take into consideration the time value of money. Estimates are subject to uncertainty, are selected from a wide range of possible outcomes and are adjusted up or down as additional information becomes known. All changes in estimates are recorded as incurred claims in the current period.

Future Income Taxes

The Company follows the liability method of accounting for income taxes. Under this method, future income tax assets and liabilities are recognized based on the expected future tax consequences of differences between the carrying amount of balance sheet items and their corresponding tax basis, using the enacted and substantively enacted income tax rates for the years in which the differences are expected to reverse. The difference occurs between amortization for accounting purposes and capital cost allowance for income tax purposes, and unpaid claims for tax and accounting purposes.

Reinsurance Ceded

Reinsurance premiums ceded and reinsurance recoveries on losses are recorded as reductions of the respective income and expense accounts. Unearned premiums on business ceded and estimates of amounts recoverable from the reinsurer on unpaid claims and adjusting expenses are recorded on the balance sheet. A contingent liability exists with respect to reinsurance ceded which may become a liability of the Company in the event that the reinsurer is unable to meet its obligation under the reinsurance contracts.

Capital Assets

Capital assets are recorded at cost less accumulated depreciation. Depreciation is provided using the straight-line method at rates reflecting the useful lives of the assets as follows:

Office building	20 years
Parking lot	13 years
Computer equipment	3 years
Furniture	10 years
Office equipment	5 years
Lawn equipment	5 years

Impairment of Long-Lived Assets

Long-lived assets are tested for recoverability whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. An impairment loss is recognized when their carrying value exceeds the total undiscounted cash flows expected from their use and eventual disposition. The amount of the impairment loss is determined as the excess of the carrying value of the asset over its fair value.

Financial Instruments

The Company classifies all its bonds and non-cashable term deposits as held-to-maturity, which are measured at amortized cost using the effective interest rate method. Common shares, pooled funds, Fire Mutuals Guarantee Fund, and short-term investments are classified as available-for-sale, which are measured at fair value, with unrealized gains and losses included in accumulated other comprehensive income until realized, at which time the cumulative gain or loss is transferred to investment income. If investments are permanently impaired, the accumulated unrealized loss is reported in net income. Receivables are classified as loans and receivables, which are measured at amortized cost. Accounts payable and accrued liabilities, and due to reinsurer and other insurance companies are classified as other financial liabilities, which are measured at amortized cost. Transaction costs are recognized immediately in income.

Use of Estimates

The preparation of financial statements in accordance with Canadian Generally Accepted Accounting Principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from management's best estimates as additional information becomes available in the future.

New Accounting Pronouncements

Recent accounting pronouncements that have been issued but are not yet effective, and have a potential impact for the Company, are as follows:

International financial reporting standards
The Canadian Accounting Standards Board confirmed in 2008 that the use of International Financial Reporting Standards (“IFRS”) by publicly accountable enterprises will be required in 2011 with comparative data for the prior year. IFRS uses a conceptual framework similar to Canadian GAAP, but there could be significant differences in recognition, measurement and disclosures that will need to be addressed.

In order to prepare for the conversion to IFRS, the Company has developed an IFRS Conversion Plan. The IFRS Conversion Plan is well underway with key IFRS standards analyzed and compared against the Company’s current Canadian GAAP policies. The key accounting policy alternatives have been identified including contract classification and first-time adoption of IFRS, however final decisions are pending. The impacts of these decisions are currently being assessed. Developments relating to existing standards and new standards are being monitored to assess the impact on the Conversion Plan. Our transition status is currently on track with our implementation schedule.

1. Change in Accounting Policy

On January 1, 2009, the Company adopted retroactively without restatement, changes to the Canadian Institute of Chartered Accountants (CICA) Handbook Section 1000, "Financial Statement Concepts", and CICA Handbook Section 3862, "Financial Instruments - Disclosures".

CICA Handbook Section 1000, "Financial Statement Concepts", has been amended to focus on the capitalization of costs that truly meet the definition of an asset and de-emphasizes the matching principle. The Company did not identify any significant changes from the existing standard, and therefore, the adoption of the amendments to this standard has not impacted the financial statements.

The Accounting Standards Board has amended CICA Handbook Section 3862, "Financial Instruments - Disclosures", by including enhanced disclosure requirements for fair value measurement of financial instruments and liquidity risks. The new required note disclosures have been included in Note 2. Prior period financial statements have not been restated for the updated disclosures.

2. Investments

The cost values, fair values and carrying values of investments as at December 31 were as follows:

	2009			2008		
	Cost Value	**Fair Value**	**Carrying Value**	Cost Value	Fair Value	Carrying Value
Available-for-sale:						
Fire Mutuals						
Guarantee Fund	**$ 19,627**	**$ 20,362**	**$ 20,362**	$ 18,947	$ 19,282	$ 19,282
Short-term investments	**1,001,829**	**1,001,829**	**1,001,829**	950,000	950,000	950,000
Fixed Income						
Pooled Fund	**6,241,370**	**6,211,651**	**6,211,651**	5,880,564	5,854,586	5,854,586
Canadian Equity						
Pooled Fund	**2,204,923**	**1,767,000**	**1,767,000**	2,217,847	1,362,210	1,362,210
Common shares	**2,534,284**	**2,131,534**	**2,131,534**	2,384,560	1,363,209	1,363,209
Membership in						
Credit Unions	**381**	**381**	**381**	381	381	381
	12,002,414	**11,132,757**	**11,132,757**	11,452,299	9,549,668	9,549,668
Held-to-maturity:						
Term deposits	**5,330,000**	**5,330,000**	**5,330,000**	4,780,000	4,780,000	4,780,000
Bonds and debentures						
Government of Canada	**250,658**	**261,110**	**250,658**	751,720	774,988	751,720
Canadian Provinces	**3,881,540**	**4,010,610**	**3,881,540**	4,255,935	4,423,914	4,255,935
Canadian Municipalities						
and Public Authorities	**4,121,222**	**4,180,945**	**4,121,222**	5,188,071	5,352,818	5,188,071
Corporate	**4,272,000**	**4,358,216**	**4,272,000**	2,332,913	2,284,565	2,332,913
	17,855,420	**18,140,881**	**17,855,420**	17,308,639	17,616,285	17,308,639
	$ 29,857,834	**$ 29,273,638**	**$ 28,988,177**	$ 28,760,938	$ 27,165,953	$ 26,858,307

The maximum exposure to credit risk would be the fair value as shown above.

2. Investments (continued)

The maturity profile of held-to-maturity investments, at carrying value, at December 31, 2009 was as follows:

Within	1 Year	2 to 3 Years	4 to 5 Years	Over 5 Years	Total
Term deposits	$ 1,400,000	$ 3,480,000	$ 450,000	$ -	$ 5,330,000
Bonds and debentures	2,880,577	3,932,235	2,820,255	2,892,353	12,525,420
	$ 4,280,577	$ 7,412,235	$ 3,270,255	$ 2,892,353	$ 17,855,420
Percent of total	24.0 %	41.5 %	18.3 %	16.2 %	100.0 %

The estimated fair values of the short-term investments and term deposits, bonds and debentures, and pooled funds are based on quoted market values. The estimated fair values of equities are determined using last bid prices. The Company has reviewed the values of the above investments and has determined that there are no impairments other than temporary due to the current economic downturn.

All investments are denominated in Canadian dollars. Interest income, dividends received, and gains or losses on disposal of investments are included in net investment income.

Term deposits
These are comprised of guaranteed investment certificates with effective interest rates of 1.75% to 5.0% (2008 - 1.75% to 5.0%). Interest is receivable on a semi-annual basis or annual basis.

Bonds and debentures
The effective interest rate for the Company's bond portfolio at December 31, 2009 is 4.24% (2008 - 5.11%) based on cost value.

2. Investments (continued)

In compliance with CICA Handbook Section 3862, "Financial Instruments - Disclosures", the Company has categorized its assets and liabilities that are carried at fair value, based on the priority of the inputs to the valuation techniques used to measure fair value, into a three level fair value hierarchy. Financial assets and liabilities measured at fair value are categorized as follows:

Level 1: Fair value is based on unadjusted quoted prices for identical assets or liabilities in an active market.

Level 2: Fair value is based on quoted prices for similar assets or liabilities in active markets, valuation that is based on significant observable inputs or inputs that are derived principally for or corroborated with observable market data through correlation or other means.

Level 3: Fair value is based on valuation techniques that require one or more significant unobservable inputs or the use of broker quotes. These unobservable inputs reflect the Company's assumptions about the assumptions market participants would use in pricing the assets or liabilities.

	Level 1	Level 2	Level 3	Total
Fire Mutuals Guarantee Fund	$ -	$ 20,362	$ -	$ 20,362
Short-term investments	-	1,001,829	-	1,001,829
Fixed income pooled fund	-	6,211,651	-	6,211,651
Canadian equity pooled fund	-	1,767,000	-	1,767,000
Common shares	2,131,534	-	-	2,131,534
Membership in Credit Unions	-	381	-	381
Total assets measured at fair value	$ 2,131,534	$ 9,001,223	$ -	$11,132,757

3. Receivables

Included in receivables is an amount of $253,463 (2008 - $291,921) due from Facility Association and $1,953 (2008 - $487) payable to Facility Risk Sharing. The Company is contingently liable for any future requests to pay additional amounts to the Facility.

4. Unpaid Claims and Adjusting Expenses

The establishment of the provision for unpaid claims and adjusting expenses relies on the judgment and opinions of a number of individuals, on historical precedence and experience, on legal opinions, on economic, local and regulatory bodies, and on trends and future developments. The process of determining the provision by its nature involves risks, that the final results may vary substantially from the best estimate. The variance may arise when events affecting the final settled value of claims are not known at the time the unpaid claim liability is established. Below are the details of the provision for unpaid claims and adjusting expenses by type of insurance:

	2009		2008	
	Gross	**Recoverable**	Gross	Recoverable
Property	**$ 255,217**	**$ (137,527)**	$ 1,446,297	$ 439,973
Liability	**1,175,652**	**572,250**	3,539,765	2,341,371
Automobile	**3,491,863**	**2,066,136**	3,900,438	2,121,515
	$ 4,922,732	**$ 2,500,859**	$ 8,886,500	$ 4,902,859

Net claims and adjusting expenses consist of:

	2009	2008
Gross claims incurred	**$ 3,568,735**	$ 4,506,771
Gross adjusting expense	**494,915**	583,752
	4,063,650	5,090,523
Reinsurance recoveries		
Claims	**(1,354,204)**	(733,500)
Adjusting	**(161,963)**	(162,004)
	$ 2,547,483	$ 4,195,019

5. Capital Assets

	2009		2008	
	Cost	**Accumulated Amortization**	Cost	Accumulated Amortization
Office building	**$ 1,359,423**	**$ 84,819**	$ 1,347,814	$ 16,848
Building lot	**127,170**	**-**	125,332	-
Farmland	**226,668**	**-**	226,668	-
Parking lot	**98,670**	**9,867**	98,670	1,973
Computer equipment	**96,692**	**36,094**	66,312	7,448
Furniture	**283,082**	**95,491**	282,787	73,696
Office equipment	**2,141**	**214**	9,194	9,194
Lawn equipment	**10,735**	**1,073**	-	-
	$ 2,204,581	**$ 227,558**	$ 2,156,777	$ 109,159
Net book value		**$ 1,977,023**		$ 2,047,618

6. Unearned Premiums

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, investment income and expected profit in relation to unearned premiums. There was no premium deficiency at December 31, 2009 (2008 - $nil).

7. Income Taxes

The Company is responsible for income taxes on the portion of its premiums that relate to non-farm business. During 2009, 57.94% (2008 - 57.62%) of its revenue was generated from non-farm activities and is taxable. The following table reconciles the statutory federal and provincial income taxes to the effective income tax on income before income taxes.

	2009	2008
Income taxes at combined statutory rates	**$ 640,800**	$ 399,270
Exemption for insurers of farmers and fishermen	**(258,729)**	(169,211)
Non-deductible items and other items	**(67,754)**	(17,103)
	$ 314,317	$ 212,956
Represented by		
Current income taxes	**$ 291,317**	$ 186,956
Future income taxes	**23,000**	26,000
	$ 314,317	$ 212,956

8. Reinsurance Ceded

The Company follows a policy of underwriting and reinsuring contracts of insurance which limit the liability of the Company to a maximum amount on any one claim as follows:

Property - First $175,000 + 10% of the excess loss to a maximum of $1,000,000.
Liability - First $125,000 + 10% of the excess loss to a maximum of $1,000,000.
Automobile - First $125,000 + 10% of the excess loss to a maximum of $1,000,000.

The Company also carries reinsurance, which limits the Company's liability to the first $500,000 plus 5% of any additional amount to protect itself against certain catastrophic losses. The Company's stop loss reinsurance contract is dependent on the amount of certain classes of losses in any given year in relation to premium income.

9. Reinsurance Assumed

In addition to the above reinsurance programs, the Company has assumed units of reinsurance through the Farm Mutual Reinsurance Plan Inc. on their Catastrophe Treaty, Manitoba Crop Insurance and Agricorp Crop Insurance Programs. The units on the Catastrophe Treaty present a maximum exposure to the Company's surplus of $250,000 per catastrophe. The Manitoba Crop Insurance and Agricorp Crop Insurance units present a maximum exposure to the Company's surplus of $100,000 per annum each.

10. Pension Plan

The Company makes contributions on behalf of its employees to the Ontario Mutual Insurance Association (OMIA) Pension Plan, which is a multi-mutual employer plan. Staff members have the option to participate in either a money purchase plan or a defined benefit plan. Agents only participate in the money purchase plan.

The defined benefit plan specifies the amount of the retirement benefit to be received by the employees, based on length of service and final average earnings.

An actuarial valuation of the Pension Plan as of December 31, 2006 showed a deficit of $23,771 which was paid in a lump sum payment during 2007. The next actuarial valuation will be as of December 31, 2009.

The amount contributed to the plan for 2009 was $63,201 (2008 - $56,164) for current service. These payments are included as expenditures in the statement of operations.

11. Rate Regulations

The Company is subject to rate regulation in the automobile business that it writes. Before automobile insurance rates can be changed a rate filing is prepared, as a combined filing for most Ontario Farm Mutuals, by the Farm Mutual Reinsurance Plan Inc. The rate filing must include actuarial justification for the rate increases or decreases. All rate filings are approved or denied by the Financial Services Commission of Ontario.

The Company is also required by regulation to assume a share of automobile insurance underwritten through the Facility Association, the liability for which has been reflected in the financial statement.

The Company's gross written automobile insurance premiums are $3,371,932 (2008 - $3,057,546), which are subject to rate regulation.

12. Statement of Cash Flows

	2009	2008
Income taxes paid in the year	**$ 75,300**	$ 213,600

13. Contingent Liabilities and Guarantees

Pursuant to an agreement effective January 1, 1976, 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. ("The Plan"), which is a general reinsurer that shares in the insurance risks originally accepted by member insurance companies. As a member of the Plan, the Company may be required to contribute additional capital to the Plan should the Plan's capital fall below a prescribed minimum. The additional capital would be provided by purchasing subordinated debt obligations issued by the Plan.

The Company is contingently liable under a letter of credit issued to a municipality amounting to $71,000 in regard to completing the new facility according to the Site Plan agreement.

14. Capital Management

The Company's objectives with respect to capital management are to maintain a capital base that is structured to exceed regulatory requirements and to best utilize capital allocations. Reinsurance is utilized to protect capital from catastrophic losses as the frequency and severity of these losses are inherently unpredictable. To limit their potential impact, catastrophe coverage limits the Company's exposure to $500,000 plus 5% of the remaining loss. The $500,000 net retained amount represents approximately 2% of the Company's capital. For the purpose of capital management, the Company has defined capital as policyholders' surplus excluding accumulated other comprehensive income.

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

In an actuarial study done, the Net Risk Ratio was shown to have a high correlation to the MCT. As a result of these findings, the Company uses Net Risk Ratio to monitor capital adequacy. Net Risk Ratio is calculated as premiums written less premiums ceded, divided by surplus.

15. Financial Instrument Risk Management

Fair Value
The fair value of cash, receivables, accrued investment income, unpaid claims and adjusting expenses recoverable from reinsurer, deferred policy acquisition costs, accounts payable and accrued liabilities, due to reinsurer and other insurance companies and unearned premiums approximate their carrying values due to their short-term maturity.

The fair value of temporary investments and of bonds and shares included in Note 2, Investments is based on quoted market prices (last bid prices).

The provision for unpaid claims and adjusting expenses and related unpaid claims and adjusting expenses recoverable from reinsurer will be settled over an extended period of time. Their estimated fair values, which would represent the discounted future net cash outflows required to meet these obligations, has not been determined. It would not be cost effective to determine the fair value.

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

The Company’s investment policy puts limits on the bond portfolio including portfolio composition limits, issuer type limits, bond quality limits, aggregate issuer limits, corporate sector limits and general guidelines for geographic exposure. The bond portfolio remains very high quality with 100% of the bonds rated A or better. All fixed income portfolios are measured for performance on a quarterly basis and monitored by management on a monthly basis.

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

Receivables are short-term in nature and are not subject to material credit risk.

The maximum exposure to credit risk and concentration of this risk is outlined in Note 2.

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

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

The Company's investment policy operates within the guidelines of the Insurance Act. An investment policy is in place and its application is monitored by the Investment Committee and the Board of Directors. Diversification techniques are utilized to minimize risk. The policy limits the investment in any one corporate issuer to a maximum of 10% of the Company's total assets.

15. Financial Instrument Risk Management (continued)

Currency Risk
The Company's investments are not exposed to currency risk as they do not have any foreign holdings.

Interest Rate Risk
Interest rate risk is the potential for financial loss caused by changes in market interest rates. This risk arises when a Company's asset cash flows do not coincide with the cash flows arising from the liabilities, as this may result in the need to either sell assets to meet policy payments and expenses or reinvest excess asset cash flows under unfavourable interest environments.

The Company is exposed to this risk through its interest bearing investments (Term deposits, Pooled fund, Bonds).

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

The objective and policies and procedures for managing interest rate risk is to diversify the bond portfolio in such a way that the bonds are a portfolio laddered over 9 years. This protects the Company from fluctuations in the interest rate.

At December 31, 2009, a 1% move in interest rates, with all other variables held constant, could impact the market value of bonds by $538,836 (2008 - $757,059).

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

15. Financial Instrument Risk Management (continued)

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

The Company's portfolio includes Canadian stocks with fair values that move with the Toronto Stock Exchange Composite Index. A 10% movement in the stock markets with all other variables held constant would have an estimated affect on the fair values of the Company's Canadian common stocks of $389,853 (2008 - $272,542). For stocks that the Company did not sell during the period, the change would be recognized in the asset value and in Other Comprehensive Income. For stocks that the Company did sell during the period, the change during the period and changes prior to the period would be recognized as net realized gains or losses in income during the period.

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

<u>Liquidity Risk</u>
Liquidity risk is the risk that the Company will not be able to meet all cash outflow obligations as they come due. The Company mitigates this risk by monitoring cash activities and expected outflows. The Company's current liabilities arise as claims are made. The Company does not have material liabilities that can be called unexpectedly at the demand of a lender or client. The Company has no material commitments for capital expenditures and there is no need for such expenditures in the normal course of business. Claim payments are funded by current operating cash flows including investment income.

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