Unaudited Condensed Consolidated Interim Financial Statements of

Echelon Financial Holdings Inc.

For nine months ended September 30, 2016 and 2015

ECHELON FINANCIAL HOLDINGS INC.
Consolidated Balance Sheets
(Unaudited, in thousands of Canadian dollars)

	Note	September 30, 2016	December 31, 2015
Assets			
Cash and short–term deposits	6	58,990	4,210
Accounts receivable		46,301	33,966
Investments	6	334,097	402,529
Due from insurance companies		1,462	1,821
Deferred policy acquisition costs		30,129	24,918
Income taxes recoverable		404	3,390
Prepaid expenses and other assets		2,513	2,671
Reinsurers' share – unearned premiums		8,434	8,178
– provision for unpaid claims	9	27,945	29,222
Property and equipment		985	577
Intangible assets	11	7,617	6,238
Deferred income taxes		5,360	5,221
Assets of the disposal group held for sale	19	394,103	348,316
Total assets		918,340	871,257
Liabilities			
Derivative Financial Instrument	7	215	—
Accounts payable and accrued liabilities		16,540	12,192
Payable to insurance companies		559	1,093
Unearned premiums		121,179	100,846
Unearned commission		2,244	1,964
Provision for unpaid claims	9	260,060	260,848
Liabilities of the disposal group held for sale	19	362,016	305,604
Total liabilities		762,813	682,547
Equity			
Share capital		70,014	69,653
Contributed surplus		381	436
Retained earnings		78,022	108,551
Accumulated other comprehensive income	16	2,920	6,060
Equity attributed to shareholders of the Company		151,337	184,700
Non-controlling interest	20	4,190	4,010
Total equity		155,527	188,710
Total liabilities and equity		918,340	871,257

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

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

		3 months ended September 30		9 months ended September 30	
		2016	**2015**	**2016**	**2015**
Revenue					
Gross written and assumed premiums		58,171	50,769	168,083	156,373
Less: Premiums ceded to reinsurers		(5,299)	(4,234)	(12,958)	(13,341)
Net written and assumed premiums		52,872	46,535	155,125	143,032
(Increase) in gross unearned premiums		(7,050)	677	(20,334)	(11,268)
Increase (decrease) in unearned premiums, reinsurers' share		630	(330)	256	799
Change in provision for unearned premiums		(6,420)	347	(20,078)	(10,469)
Net earned premiums		46,452	46,882	135,047	132,563
Investment income	6	4,487	(2,606)	13,348	6,336
Other income		—	—	—	748
Total revenue		50,939	44,276	148,395	139,647
Expenses					
Gross claims incurred		26,884	28,877	88,547	94,570
Less: claims recoveries from reinsurers		1,689	(606)	(3,429)	(8,426)
Net incurred claims		28,573	28,271	85,118	86,144
Gross acquisition costs		12,310	11,384	35,068	33,563
Less: acquisition cost recoveries from reinsurers		(1,495)	(1,304)	(4,203)	(3,591)
Net acquisition costs		10,815	10,080	30,865	29,972
Operating costs	14	8,477	7,111	25,530	20,090
Total expenses		47,865	45,462	141,513	136,206
Income before taxes and discount rate impact on claims		3,074	(1,186)	6,882	3,441
Impact of change in discount rate on claims[(1)]		(1,452)	—	(1,452)	(1,056)
Income before interest expense and income taxes		1,622	(1,186)	5,430	2,385
Interest expense	8	57	—	154	—
Income tax expense (recovery)	12	163	91	759	(1,071)
Net income (loss) on continued operations		1,402	(1,277)	4,517	3,456
Net income (loss) on discontinued operations	19	(2,232)	(2,455)	(31,615)	1,080
Net income (loss)		(830)	(3,732)	(27,098)	4,536
Attributed to:					
Shareholders of the Company - continued		1,235	(1,315)	4,008	3,626
Shareholders of the Company - discontinued		(2,201)	(2,325)	(31,494)	1,042
Non-controlling interest - continued	20	167	38	509	(170)
Non-controlling interest - discontinued		(31)	(130)	(121)	38
Net income (loss)		(830)	(3,732)	(27,098)	4,536
Other comprehensive income (loss), net of taxes that may be classified subsequently to net income					
Available-for-sale investments:					
Change in net unrealized gains (losses)		687	(4,034)	2,457	(1,126)
Reclassification of net realized (gains) to net income		(873)	(703)	(5,602)	(5,334)
Cumulative translation gain (loss)		(1)	1,444	(395)	1,266
Foreign exchange forward	7	(215)	—	4,099	—
Tax impact		51	1,061	74	1,402
Other comprehensive income (loss) on continued operations		(351)	(2,232)	633	(3,792)
Other comprehensive income (loss) on discontinued operations		(700)	2,084	(3,826)	730
Other comprehensive (loss)		(1,051)	(148)	(3,193)	(3,062)

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

Attributed to:					
Shareholders of the Company - continued operations		(347)	(2,198)	637	(3,788)
Shareholders of the Company - discontinued operations		(691)	2,084	(3,777)	730
Non-controlling interest - continued operation	20	(4)	(34)	(4)	(4)
Non-controlling interest - discontinued operation		(9)	—	(49)	—
Other comprehensive (loss)		(1,051)	(148)	(3,193)	(3,062)
Total comprehensive income (loss)		(1,881)	(3,880)	(30,291)	1,474
Attributed to:					
Shareholders of the Company - continued operations		888	(3,513)	4,645	(162)
Shareholders of the Company - discontinued operations		(2,892)	(241)	(35,271)	1,772
Non-controlling interest - continued operation	20	163	4	505	(174)
Non-controlling interest - discontinued operation		(40)	(130)	(170)	38
Total comprehensive income (loss)		(1,881)	(3,880)	(30,291)	1,474
Earnings per share attributable to shareholders of the Company	17				
Earnings per share continued operations - basic		$0.10	$(0.11)	$0.34	$0.31
Earnings per share - basic		$(0.08)	$(0.31)	$(2.34)	$0.40
Earnings per share continued operations - diluted		$0.10	$(0.11)	$0.33	$0.30
Earnings per share - diluted		$(0.08)	$(0.31)	$(2.34)	$0.39
Net income (loss)		(830)	(3,732)	(27,098)	4,536

[1] As the interest rate changes every year there is an impact to the incurred claims. Management believes it is beneficial to the user to see the impact of this change separately in order to understand the true movement in claims incurred.

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

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

	Share Capital	Contributed Surplus	Accumulated Other Comprehensive Income	Retained Earnings	Shareholders' Equity	Non-controlling Interest	Total Equity
Balance at January 1, 2016	69,653	436	6,060	108,551	184,700	4,010	188,710
Net income (loss)	—	—	—	(27,486)	(27,486)	388	(27,098)
Other comprehensive income (loss)	—	—	(3,140)	—	(3,140)	(53)	(3,193)
Total comprehensive income (loss)	—	—	(3,140)	(27,486)	(30,626)	335	(30,291)
Common shares repurchased	(292)	—	—	(384)	(676)	—	(676)
Dividends paid	—	—	—	(2,814)	(2,814)	—	(2,814)
Investment in subsidiary - Qudos	—	—	—	155	155	(155)	—
Common shares issued on stock options exercised	653		—		653	—	653
Stock compensation expense	—	(55)	—	—	(55)	—	(55)
Balance at September 30, 2016	70,014	381	2,920	78,022	151,337	4,190	155,527

	Share Capital	Contributed Surplus	Accumulated Other Comprehensive Income	Retained Earnings	Shareholders' Equity	Non-controlling interest	Total Equity
Balance at January 1, 2015	67,153	2,192	8,917	105,354	183,616	3,856	187,472
Net income (loss)	—	—	—	4,668	4,668	(132)	4,536
Other comprehensive income (loss)	—	—	(3,058)	—	(3,058)	(4)	(3,062)
Total comprehensive income (loss)	—	—	(3,058)	4,668	1,610	(136)	1,474
Common shares repurchased	(339)	—	—	(339)	(678)	—	(678)
Dividends paid	—	—	—	(3,880)	(3,880)	—	(3,880)
Investment in subsidiaries - ICPEI	—	—	—	—	—	250	250
- Qudos	—	—	—	(129)	(129)	129	—
Common shares issued on stock options exercised	1,949	—	—	—	1,949	—	1,949
Stock options expense	—	54	—	—	54	—	54
Balance at September 30, 2015	68,763	2,246	5,859	105,674	182,542	4,099	186,641

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

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

		September 30, 2016	September 30, 2015
Cash provided by (used in):			
Operating activities			
Net income		4,517	3,456
Adjusted for:			
Reinsurers' share of unearned premiums		(256)	(799)
Reinsurers' share of unpaid claims		1,277	(5,204)
Provision for unpaid claims		(788)	516
Unearned premiums		20,333	11,268
Deferred income taxes		(139)	(41)
Unearned commissions		280	158
Deferred policy acquisition costs		(5,211)	(2,491)
Amortization on property plant equipment and intangible assets		2,913	3,587
Amortization of premiums on bonds		1,438	1,568
Fair value change on FVTPL investments		(3,236)	9,452
Options expense		(55)	54
Currency translation		(395)	1,266
Foreign exchange forward		4,099	—
Prepaid expenses & other assets		158	(196)
		20,418	19,138
Cash flow from changes in			
Accounts receivable		(12,335)	10,362
Net realized (gains) losses		(569)	(5,370)
Income taxes (recoverable) payable		3,061	(7,499)
Due to insurance companies		(175)	797
Other liabilities		4,563	(918)
Cash (used in) continued operating activities		19,480	19,966
Financing activities			
Proceeds from issue of common shares for stock options		653	1,949
Common share dividends		(2,814)	(3,880)
Share repurchases		(676)	(678)
Additional investment in ICPEI by minority interest		—	250
Cash (used in) financing activities		(2,837)	(2,359)
Investing activities			
Purchases of property, equipment and intangible assets		(4,700)	(2,640)
Purchases of investments		(248,020)	(317,619)
Sale/maturity of investments		315,673	323,879
Cash provided by investing activities		62,953	3,620
Cash flow from discontinued operations	19	(8,111)	(18,874)
Increase in cash and short-term deposits		71,485	2,353
Cash and short-term deposits, beginning of period		23,373	27,326
Cash and short-term deposits, end of period		94,858	29,679
Supplementary information			
Operating activities			
Income taxes paid (recovered)		(1,712)	6,110

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

1 Nature of operations

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

The Company's wholly-owned subsidiaries are Echelon Insurance ("Echelon"), CIM Reinsurance Company Ltd. ("CIM Re") and CUISA Managing General Agency Corporation ("CUISA MGA"). The Company also owns 75% of The Insurance Company of Prince Edward Island ("ICPEI") and all of the preferred shares, in addition to 98.7% of the common shares of QIC Holdings ApS ("QIC"). QIC owns 100% of Qudos Insurance A/S ("Qudos") that is headquartered in Denmark and underwrites insurance products primarily in the United Kingdom, Ireland, and Denmark. The Company's ownership has increased to 98.7% from 97.5% at the beginning of the year due to capital injected to maintain its solvency ratio.

2 Basis of preparation

These condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) applicable to the preparation of interim financial statements, including IAS 34, Interim Financial Reporting. The condensed consolidated interim financial statements should be read in conjunction with the annual financial statements for the year ended December 31, 2015, which have been prepared in accordance with IFRS.

These consolidated financial statements have been authorized for issue by the Board of Directors, on November 2, 2016.

3 Summary of significant accounting policies

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

Discontinued Operations

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

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

Standards, amendments and interpretations not yet adopted or effective

IFRS 9, Financial Instruments

In July 2014 the IASB published the complete version of IFRS 9 which is effective for annual periods beginning on or after January 1, 2018, with retrospective application. The new standard includes requirements on the classification and measurement of financial assets and liabilities, an expected credit loss model that replaces the existing incurred loss impairment model and new hedge accounting guidance. The Company is currently evaluating the impacts of IFRS 9 on its consolidated financial statements, as well as the implementation options for insurers set out in the September 2016 amendment to *IFRS 4 Insurance Contracts* which allows eligible insurers to defer the adoption of IFRS 9 until the new insurance contracts standard is adopted, or 2021 at the latest.

IFRS 15, Revenue from contracts with customers

IFRS 15, Revenue from contracts with customers deals with revenue recognition and establishes principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. Revenue is recognized when a customer obtains control of a good or service and thus has the ability to direct the use and obtain the benefits from the good or service. The standard replaces IAS 18 'Revenue' and IAS 11 'Construction contracts' and related interpretations. The standard is effective for annual periods beginning on or after January 1, 2018. The Company has not yet assessed the impact of the standard or determined whether it will adopt the standard early.

IFRS 16, Leases

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

4 Critical accounting estimates and assumptions

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

In preparing these condensed consolidated interim financial statements, the significant judgements made by management in applying accounting policies and the key sources of estimation uncertainty were the same as those applied to the annual 2015 consolidated financial statements.

5 Seasonality

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

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

6 Investments

The following table provides a breakdown of the investment portfolio as at September 30, 2016, and December 31, 2015.

	Fair values	
Available-for-sale	**As at September 30, 2016**	**As at December 31, 2015**
Fixed income		
Canadian		
Federal	55,032	45,524
Provincial	43,690	55,976
Municipal	525	1,386
Corporate	139,838	171,789
	239,085	274,675
Fixed income lent through securities lending program		
Federal	15,618	14,231
Provincial	7,651	3,800
Municipal	857	—
Corporate	3,708	4,673
	27,834	22,704
Foreign fixed income		
Corporate	—	21,384
	—	21,384
Total fixed income	266,919	318,763
Commercial mortgages pooled funds	17,446	17,017
Money market pooled funds	209	403
Short-term fixed income and mortgage pooled funds	17,303	16,934
Total pooled funds	34,958	34,354
Common shares		
Canadian	275	2,656
U.S.	—	8,012
Total common shares	275	10,668
Total available-for-sale	302,152	363,785
Fair value through profit or loss		
Preferred shares	31,681	38,400
Preferred shares lent through securities lending program	264	344
Total preferred shares	31,945	38,744
Total investments	334,097	402,529
Cash and short-term deposits	58,990	4,210
Total investments including cash and short-term deposits	393,087	406,739

In accordance with the securities lending agreement, the amount of the collateral must be at least 105% of the fair value of the securities loaned. As at September 30, 2016, the Company had collateral of $29,821 (September 30, 2015 – $32,066) for the loaned securities or approximately 105% of the fair value of the loaned securities.

Fair value

The Company is responsible for determining the fair value of its investment portfolio by utilizing market-driven fair value measurements from active markets, where available, by considering other observable and unobservable inputs and by employing valuation techniques which make use of current market data. The

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

Company uses a fair-value hierarchy to categorize the inputs used in valuation techniques to measure fair value. A description of the inputs used in the valuation of financial instruments is as follows:

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

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

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

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

The following table provides the classification of the Company's investments within the fair value hierarchy, as outlined above, as at September 30, 2016, and December 31, 2015:

September 30, 2016				
	Level 1	**Level 2**	**Level 3**	**Total**
Fixed income	—	266,919	—	266,919
Commercial mortgages pooled funds	—	17,446	—	17,446
Money market pooled funds	—	209	—	209
Short-term fixed income and mortgage pooled funds	—	17,303	—	17,303
Equities	275	—	—	275
Preferred Shares	31,945	—	—	31,945
	32,220	301,877	—	334,097

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

December 31, 2015				
	Level 1	**Level 2**	**Level 3**	**Total**
Fixed income	—	318,763	—	318,763
Commercial mortgages pooled funds	—	17,017	—	17,017
Money market pooled funds	—	403	—	403
Short-term fixed income and mortgage pooled funds	—	16,934	—	16,934
Equities	10,668	—	—	10,668
Preferred Shares	38,744	—	—	38,744
	49,412	353,117	—	402,529

The fair value of the Company's investments, determined with the use of unobservable market information as inputs, is $nil (December 31, 2015 – $nil) of the total investment portfolio. All investments in a commercial mortgages pooled fund with a fair value of $17,446 are in level 2.

A reconciliation of Level 3 investments for the years ended September 30, 2016, and December 31, 2015, with the use of significant unobservable inputs from January 1 to September 30, is as follows:

	September 30, 2016	**December 31, 2015**
Balance at beginning of period	—	2,173
Addition during the year	—	—
Disposal / Reclassification during the year	—	(2,173)
Net unrealized gains included in other comprehensive income	—	—
Balance at end of period	—	—

Investment in commercial mortgages pooled funds is valued using the Company's share of the net asset value of the commercial mortgage pooled fund as of September 30, 2016, and December 31, 2015.

The Company's policy is to recognize transfers into and transfers out of fair value hierarchy levels as of the date of the event or change in circumstances that caused the transfer. There were no transfers during the nine months ended September 30, 2016 or 2015. There were no transfers from Level 2 to Level 1, or vice versa in the period.

The fair values of cash and short-term deposits, account receivables and financial liabilities, other than the provision for unpaid claims, approximate their carrying values due to their short-term nature.

Impaired assets and provisions for losses

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

No impairments on AFS investments were recognized for the period ended September 30, 2016 (September 30, 2015 – $nil). A remaining gross unrealized loss of $550 on AFS investments held as at September 30, 2016 (September 30, 2015 – $3,437) is recorded, net of tax, in the amount of $400 (September 30, 2015 – $2,859) in Accumulated Other Comprehensive Income.

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

Investment income

The table below provides additional details on net investment income:

	3 months ended September 30		9 months ended September 30	
	2016	**2015**	**2016**	**2015**
Interest income	2,485	3,178	8,347	9,449
Dividend income	378	582	1,397	1,929
Net realized gains (losses)	847	724	569	5,370
Fair value change on FVTPL investments	965	(5,598)	3,236	(9,452)
Realized and unrealized foreign exchange gains (losses)	21	(1,237)	480	(138)
Investment expenses	(209)	(255)	(681)	(822)
Investment income	4,487	(2,606)	13,348	6,336

7 Derivative Financial Instrument

On January 21, 2016, the Company entered into a three month foreign exchange forward contract to manage the foreign currency risk on its investment in its European subsidiary, Qudos. The Company agreed to buy $47.8 million (CAD) and sell €30 million (EUR). The fair value of the forward was $3.5 million as at March 31, 2016. The contract was an effective hedge and there was no ineffectiveness. The contract matured on April 22, 2016, with a realized value of $4.3 million.

On August 8, 2016, the Company entered into a three month foreign exchange forward contract to manage the foreign currency risk on its sales proceeds from its European subsidiary, Qudos. The contract value is $23 million (CAD). The fair value of the forward was a loss of $0.2 million as at September 30, 2016.

8 Line of credit

The Company has a $10 million two-year secured revolving term credit facility effective June 30, 2015, maturing on July 1, 2017. This credit facility may be drawn at the prime rate plus a margin or as bankers' acceptances rate plus a margin. This facility was undrawn as at September 30, 2016. As part of the covenants of the loans under the credit facilities, the Company is required to maintain certain ratios and limits. All financial limits and ratios have been met as at September 30, 2016.

For the quarter ending September 30, 2016, the Company has expensed $0.2 million related to the maintenance of the credit.

9 Provision for unpaid claims

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

The Company determines the discount rate based on the expected return on its investment portfolio of assets with appropriate assumptions for interest rates relating to reinvestment of maturing investments. The Company discounts its best estimate as follows for each entity, which is for all lines of business within reporting entity:

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

Entity	September 30, 2016	December 31, 2015
Echelon Insurance	2.24%	2.44%
ICPEI	1.63%	1.63%

The Company recorded a $13,801 reduction to the net provision for unpaid claims relating to redundancies in prior years' estimates (September 30, 2015 – $11,988).

To recognize the uncertainty in establishing these best estimates, to allow for possible deterioration in experience, and to provide greater comfort that the actuarial liabilities are adequate to pay future claims, the Company includes provisions for adverse deviations (PFADs) in some assumptions relating to claims development, reinsurance recoveries and future investment income. The PFADs selected are in the mid-range of those recommended by the Canadian Institute of Actuaries. The aggregate impact of the provision for adverse deviation is to increase the provision for unpaid claims on a net basis by $19,558 as at September 30, 2016 (December 31, 2015 – $21,818).

Claims development

Provision for unpaid claims analysis	September 30, 2016	September 30, 2015
Unpaid claims, beginning of year, net	231,626	251,740
Favourable prior year claims development	13,801	11,988
Provision for claims occurring in current period	72,769	75,212
Paid on claims occurring during		
Current year	(38,603)	(34,027)
Prior year	(47,478)	(60,294)
Unpaid claims, end of period, net	232,115	244,619
Reinsurers' share	27,945	28,963
Gross unpaid claims	260,060	273,582

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

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

10 Risk management

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

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

The Company has written principles for overall risk management, as well as written policies covering specific areas such as underwriting, reinsurance, foreign exchange risk, interest rate risk, credit risk, use of derivative financial instruments and non–derivative financial instruments and investment of excess liquidity.

Insurance risk

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

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

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

Interest rate risk

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

The sensitivity analysis for interest rate risk as set out in the table below illustrates the impact of changes in interest rates on OCI relating to the fixed income investment portfolio as at September 30, 2016, and December 31, 2015, based on parallel 200 basis point shifts in interest rates up and down in 100 basis point increments.

Change in interest rates	Fair value of fixed income	Hypothetical change on fair value	Effect on OCI net of tax
As at September 30, 2016			
200 basis point rise	251,541	(6)%	(11,226)
100 basis point rise	259,230	(3)%	(5,613)
No change	266,919	—	—
100 basis point decline	274,607	3%	5,612
200 basis point decline	282,296	6%	11,225

Change in interest rates	Fair value of fixed income	Hypothetical change on fair value	Effect on OCI net of tax
As at December 31, 2015			
200 basis point rise	300,095	(6)%	(13,628)
100 basis point rise	309,430	(3)%	(6,814)
No change	318,763	—	—
100 basis point decline	328,099	3%	6,814
200 basis point decline	337,433	6%	13,628

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

Liquidity risk

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

The maturity profile of bonds as at September 30, 2016, and December 31, 2015, are as follows:

September 30, 2016	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Bonds	20,898	85,921	91,024	69,076	266,919
Percentage of total	8%	32%	34%	26%	100%

December 31, 2015	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Bonds	34,163	88,757	97,216	98,627	318,763
Percentage of total	11%	28%	30%	31%	100%

The following tables summarize the expected timing of cash flows arising from insurance obligations, on an undiscounted basis, as at September 30, 2016, and December 31, 2015:

September 30, 2016	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Actuarial liabilities (undiscounted)	84,489	90,970	48,129	27,154	250,742
Less: Reinsurance recoverable (undiscounted)	11,440	9,377	4,339	2,453	27,609
Net actuarial liabilities	73,049	81,593	43,790	24,701	223,133

December 31, 2015	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Actuarial liabilities (undiscounted)	84,690	91,529	48,349	27,265	251,833
Less: Reinsurance recoverable (undiscounted)	11,421	9,836	4,572	2,534	28,363
Net actuarial liabilities	73,269	81,693	43,777	24,731	223,470

All other financial liabilities are for duration of one year or less. The contractual maturities for lease commitments are listed in note 15.

Equity price risk

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

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

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

The table below summarizes the potential impact of a 10% change in the value of the equity securities (common and preferred shares) on net income and OCI for the nine months ended September 30, 2016, and the year ended December 31, 2015. Certain shortcomings are inherent in the method of analysis presented, as the analysis is based on the assumption that all equity holdings increased/decreased by 10% with all other variables held constant.

Change in equity holdings	**Effect on net income (loss) net of tax**		**Effect on OCI net of tax**	
	September 30, 2016	**December 31, 2015**	**September 30, 2016**	**December 31, 2015**
10% rise	2,332	2,828	20	779
10% decline	(2,332)	(2,828)	(20)	(779)

Credit risk

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

The Company is exposed to risk from reinsurers' inability to cover balances. 98.8% of the Company's reinsurance balances are from registered reinsurers. The Company holds sufficient collateral to cover the 1.2% of reinsurance balances from unregistered reinsurers.

The following table sets forth the Company's fixed income securities portfolio by credit quality as at September 30, 2016, and December 31, 2015.

Fixed income portfolio

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

	As at September 30, 2016		**As at December 31, 2015**	
	Fair value	**Fair value**	**Fair value**	**Fair value**
AAA	96,155	36%	89,413	28%
AA	65,142	24%	74,209	24%
A	65,070	25%	69,918	22%
BBB	40,552	15%	51,718	16%
BB	—	—%	13,808	4%
B	—	—%	9,187	3%
CCC	—	—%	537	0%
Unrated	—	—%	9,973	3%
Total	266,919	100%	318,763	100%

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

Preferred share portfolio

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

	As at September 30, 2016		As at December 31, 2015	
	Fair value	Fair value	Fair value	Fair value
P2	31,524	99%	30,702	79%
P3	421	1%	8,042	21%
Total	31,945	100%	38,744	100%

11 Intangible assets

	Opening cost	Purchases	Sales	End of period cost	Accumulated amortization	Net
Software						
September 30, 2016	23,014	3,973	—	26,987	19,770	7,217
December 31, 2015	19,430	3,584	—	23,014	17,176	5,838
Goodwill						
September 30, 2016	400	—	—	400	—	400
December 31, 2015	400	—	—	400	—	400
Total intangible assets						
September 30, 2016	23,414	3,973	—	27,387	19,770	7,617
December 31, 2015	19,830	3,584	—	23,414	17,176	6,238

12 Income taxes

The income tax (recovery) is as follows:

	3 months ended September 30		9 months ended September 30	
	2016	**2015**	**2016**	**2015**
Current	31	224	898	(1,041)
Deferred	132	(133)	(139)	(30)
	163	91	759	(1,071)

The effective income tax rates are different from the combined federal and provincial income tax rates.

The consolidated statements of income and comprehensive income contain items that are non-taxable or non-deductible for income tax purposes, which cause the income tax expense to differ from what it would have been if based on statutory rates.

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

The difference is broken down as follows:

	3 months ended September 30		9 months ended September 30	
	2016	**2015**	**2016**	**2015**
Income tax expense calculated at statutory rates	27.0 %	27.0 %	27.0 %	27.0 %
Increase (decrease) in income tax rates resulting from:				
Non-taxable dividend income	(30.1)%	14.9 %	(7.0)%	(12.9)%
Non-taxable (income) loss	22.0 %	(47.1)%	(9.9)%	(22.5)%
Non-deductible expenses	1.6 %	(34.5)%	5.9 %	12.1 %
Tax benefit of losses not previously recognized	4.4 %	2.3 %	(11.8)%	(21.4)%
Tax benefit of losses not recognized	(39.8)%	— %	0.0 %	— %
Statutory rate differences	0.3 %	(2.8)%	1.0 %	(1.2)%
Non-taxable portion of capital gains	(35.4)%	2.7 %	(11.8)%	(8.3)%
Other	60.5 %	28.5 %	21.0 %	(2.5)%
Effective income tax rate	10.5 %	(9.0)%	14.4 %	(29.7)%

13 Related party transactions

The Co-operators Group Limited and Co-operators General Insurance Company (collectively Co-operators), significant shareholders of the Company, provide services to the Company, including but not limited to product distribution and investment management services under arms length contracts. Direct written premiums derived from Co-operators' agents were $3,412 (September 30, 2015 – $4,566); commissions paid were $391 (September 30, 2015 – $527) and investment management fees were $190 (September 30, 2015 – $197).

14 Operating Costs by nature

The table below presents operating costs by major category:

	Three Months Ended September 30		Nine Months Ended September 30, 2015	
	2016	**2015**	**2016**	**2015**
Salaries and benefits	3,544	3,209	11,371	10,621
Systems costs	1,839	1,376	5,529	4,791
Professional fees	756	472	1,362	914
Occupancy	385	320	959	1,042
Severance	984	—	3,497	—
Other expenses	969	1,734	2,812	2,722
	8,477	7,111	25,530	20,090

Corporate expenses include $0.4 million (2015 - $1.0 million) relating to positive development on prior year claims reserves of ICPEI, that in accordance with terms of the share purchase agreement are payable to SGI Canada on January 1, 2019, up to a maximum of the lesser of $1.5 million or 75% of the surplus. The indemnification liability is offset by positive development of the reserve in ICPEI. In the event that prior period losses are greater than the reserves held at June 30, 2014, SGI Canada will be required to pay the Company the difference on January 1, 2019, to a maximum of the lesser of $1.5 million or 75% of the deficiency.

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

15 Lease commitments

The Company is committed under lease agreements for office premises and computer equipment with minimum lease payments of $11,178 as follows:

Lease commitments	
2016	385
2017	1,382
2018	1,368
2019	1,287
2020	1,198
2021 and thereafter	5,558
	11,178

16 Accumulated other comprehensive income

A breakdown of the accumulated other comprehensive income is shown below.

	As at September 30, 2016	As at December 31, 2015
Gross unrealized gains	3,169	4,208
Foreign currency translation adjustments	(4,998)	2,151
Foreign exchange forward	4,099	—
Tax impact	650	(299)
Ending balance	2,920	6,060

17 Earnings per share

	3 months ended September 30		9 months ended September 30	
	2016	**2015**	**2016**	**2015**
Basic earnings per share on continuing operations:				
Net income (loss) available to shareholders	1,235	(1,315)	4,008	3,626
Average number of common shares	11,734	11,739	11,732	11,675
Basic earnings per share on continuing operations	$0.10	$(0.11)	$0.34	$0.31
Diluted earnings per share:				
Average number of common shares	11,734	11,739	11,732	11,675
Average number of dilutive common shares under employee stock compensation plan	255	295	263	305
Average number of diluted common shares	11,989	12,034	11,995	11,980
Diluted earnings per share on continuing operations	$0.10	$(0.11)	$0.33	$0.30

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

	3 months ended September 30		9 months ended September 30	
	2016	**2015**	**2016**	**2015**
Basic earnings per share:				
Net income available to shareholders	(966)	(3,640)	(27,486)	4,668
Average number of common shares	11,734	11,739	11,732	11,675
Basic earnings (loss) per share	$(0.08)	$(0.31)	$(2.34)	$0.40
Diluted earnings per share:				
Average number of common shares	11,734	11,739	11,732	11,675
Average number of dilutive common shares under employee stock compensation plan	255	295	263	305
Average number of diluted common shares	11,989	12,034	11,995	11,980
Diluted earnings (loss) per share	$(0.08)	$(0.31)	$(2.34)	$0.39

18 Subsequent event

On October 11, 2016 the foreign exchange forward contract for $23 million CAD matured. On maturity there was a realized loss of $0.4 million.

A new three month foreign exchange forward contract for $18 million CAD was entered to manage the foreign currency risk on its sales proceeds from its European subsidiary, Qudos. This contract will expire on December 12, 2016.

19 Held for sale classification and discontinued operations

During the second quarter of 2016, a decision was made to sell the European operations and all net assets were recorded as Held for Sale and recorded at the lower of the fair value less cost to sell and the carrying value. This reclassification for the discontinued operations resulted in a $21 million impairment being recorded against the unearned premiums included within the liabilities of the disposable group held for sale. An additional $1 million of transaction costs was recorded to reflect the costs to dispose the operations.

Assets and liabilities of the disposal group held for sale

The assets and liabilities of the disposal group classified as held for sale included in the consolidated balance sheet as at September 30, 2016 was as follows:

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

	As at September 30, 2016	As at December 31, 2015
Assets of the disposal group held for sale		
Cash and short-term deposits	35,868	19,163
Investments	126,902	110,570
Reinsurers' share of unearned premiums	77,327	81,775
Reinsurers' share of unpaid claims	93,013	60,936
All other Assets	60,993	75,872
Total assets of disposal group held for sale	394,103	348,316
Liabilities of the disposal group held for sale		
Accounts payable and accrued liabilities	10,177	22,074
Unearned premiums	127,296	107,435
Provision for unpaid claims	185,382	136,366
All other Liabilities	39,161	39,729
Total liabilities of disposal group held for sale	362,016	305,604

Net income (loss) from discontinued operations

The components of the net income (loss) from discontinued operations included in the consolidated statements of income and comprehensive income are as follows:

	3 months ended September 30		9 months ended September 30	
	2016	**2015**	**2016**	**2015**
Revenue				
Gross written and assumed premiums	71,520	80,395	204,984	203,436
Net written premium	36,730	48,228	99,844	129,442
(Increase) decrease in provision for unearned premium	(3,438)	(10,924)	9,265	(32,597)
Net earned premiums	33,292	37,304	109,109	96,845
Investment income	577	(157)	2,171	763
Total revenue	33,869	37,147	111,280	97,608
Expenses				
Net incurred claims	22,922	23,730	79,698	54,944
Impact of change in discount rate on claims	—	441	—	616
Net acquisition costs	11,964	14,373	37,839	35,887
Operating costs	1,577	1,552	5,806	5,131
Total expenses	36,463	40,096	123,343	96,578
Income (loss) before income taxes	(2,594)	(2,949)	(12,063)	1,030
Income tax (recovery) expense	(362)	(494)	(2,448)	(50)
Net income (loss) on discontinued operations	(2,232)	(2,455)	(9,615)	1,080
Impairment of the net assets of disposal group held for sale	—	—	(22,000)	—
Net income (loss) on discontinued operations	(2,232)	(2,455)	(31,615)	1,080

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

Cash flow from discontinued operations

The details of the cash flow of the discontinued operations included in the consolidated statement of cash flows was as follows:

	September 30, 2016	September 30, 2015
Discontinued cash provided by (used in):		
Net (loss) income	(31,615)	1,080
Operating activities	38,858	3,322
Financing activities	—	—
Investing activities	(15,354)	(23,276)
Cash flow from discontinued operations	**(8,111)**	**(18,874)**

20 Non-controlling interest

The Company has non-controlling interests attributable to the subsidiary of ICPEI, please refer to Note 1.

	3 months ended September 30		9 months ended September 30	
	2016	2015	2016	2015
Revenue				
Gross written and assumed premiums	2,041	1,855	5,728	5,301
Net earned premiums	1,708	1,708	4,885	4,837
Investment income	106	(92)	248	(58)
Total revenue	1,814	1,616	5,133	4,779
Expenses				
Net incurred claims	895	917	2,506	3,330
Net acquisition costs	386	389	1,117	1,113
Operating costs	290	265	796	624
Total expenses	1,571	1,571	4,419	5,067
Income (loss) before income taxes	243	45	714	(288)
Income tax expense (recovery)	76	7	205	(118)
Net income (loss) attributable to NCI	167	38	509	(170)
OCI attributable to NCI	(4)	(34)	(4)	(4)
Comprehensive income attributable to NCI	163	4	505	(174)

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

	As at September 30, 2016	As at December 31, 2015
Assets		
Cash and investments	9,419	8,337
Other assets	4,599	4,417
Total assets	14,018	12,754
Liabilities		
Unearned premium	3,871	3,428
Unpaid claims	5,715	5,682
Other liabilities	645	362
Total liabilities	10,231	9,472
Equity		
Share capital	—	—
AOCI	5	9
Retained earnings	3,782	3,273
Total equity	3,787	3,282
Total liabilities and equity	14,018	12,754

	As at September 30, 2016	As at December 31, 2015
	ICPEI	**ICPEI**
Cash flow from operating activities	1,073	(581)
Cash flow from investing activities	(173)	(201)
Cash flow from financing activities	—	250
Net increase (decrease) in cash and short-term deposits	900	(532)

21 Segmented information

The Company operates through two segments: Personal Lines and Commercial Lines businesses. Through its Personal Lines segment, the Company is engaged primarily in the underwriting of high premium, non-standard automobile insurance.

Through its Commercial Lines, the Company designs and underwrites specialized non-auto insurance programs, such as higher premium property, primary and excess liability, legal expense, creditor insurance, warranty coverage, surety and commercial auto.

The European operations are considered to be discontinued and not disclosed.

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

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

	3 months ended September 30		9 months ended September 30	
	2016	**2015**	**2016**	**2015**
Revenue				
Earned premiums				
– Personal Lines	36,357	33,935	104,331	101,065
– Commercial Lines	10,095	12,947	30,716	31,498
Total earned premium	46,452	46,882	135,047	132,563
Net claims Incurred				
– Personal Lines	24,514	21,553	70,204	69,838
– Commercial Lines	4,059	6,718	14,914	16,306
Total net claims incurred	28,573	28,271	85,118	86,144
Net expenses				
– Personal Lines	11,664	10,526	33,774	31,221
– Commercial Lines	4,741	4,236	13,667	12,501
Total	16,405	14,762	47,441	43,722
Corporate Expenses	1,903	2,429	5,457	6,340
Total net expenses	18,308	17,191	52,898	50,062
Income (loss) before income taxes				
– Personal Lines	179	1,856	353	6
– Commercial Lines	1,295	1,993	2,135	2,691
Total Canada	1,474	3,849	2,488	2,697
Corporate and other	(1,903)	(2,429)	(5,457)	(6,340)
Underwriting income (loss)	(429)	1,420	(2,969)	(3,643)
Impact of change in net claims discount rate[1]	(1,452)	—	(1,452)	(1,056)
Other income	—	—	—	748
Severance expense	(984)	—	(3,497)	—
Investment income	4,487	(2,606)	13,348	6,336
Total income before income taxes	1,622	(1,186)	5,430	2,385

[1] As the interest rate changes every year, there is an impact to the incurred claims. Management believes it is beneficial to the user to see the impact of this change separately in order to understand the true movement in claims incurred.

Segmented long-term assets

	As at September 30, 2016	As at December 31, 2015
Personal Lines	7,032	6,240
Commercial Lines	1,518	575
Total segmented long-term assets	8,550	6,815