Unaudited Condensed Consolidated Interim Financial Statements of

Echelon Financial Holdings Inc.

For six months ended June 30, 2017 and 2016

The external auditors have not reviewed these consolidated unaudited financial statements.

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

	Note	June 30, 2017	December 31, 2016
Assets			
Cash and short–term deposits	6	53,987	50,588
Accounts receivable		69,799	46,705
Loan receivable	7	18,238	—
Investments	6	342,154	336,535
Due from insurance companies		979	1,587
Deferred policy acquisition costs		36,708	30,689
Income taxes recoverable		—	867
Prepaid expenses and other assets		2,656	2,270
Reinsurers' share – unearned premiums		10,875	8,975
– provision for unpaid claims	10	28,108	27,023
Property and equipment		978	881
Intangible assets	12	8,785	8,197
Deferred income taxes		5,732	5,860
Assets of the disposal group held for sale	3	—	280,042
Total assets		578,999	800,219
Liabilities			
Income taxes payable		386	—
Derivative financial instruments	8	545	268
Accounts payable and accrued liabilities		21,283	17,332
Payable to insurance companies		2,741	450
Unearned premiums		148,672	120,184
Unearned commission		2,249	2,288
Provision for unpaid claims	10	254,287	255,129
Liabilities of the disposal group held for sale	3	—	263,194
Total liabilities		430,163	658,845
Equity			
Share capital		71,105	70,227
Contributed surplus		229	322
Retained earnings		75,582	71,935
Accumulated other comprehensive income	16	(1,859)	(5,070)
Equity attributed to shareholders of the Company		145,057	137,414
Non-controlling interest	19	3,779	3,960
Total equity		148,836	141,374
Total liabilities and equity		578,999	800,219

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, except per share amounts)

		3 months ended June 30		6 months ended June 30	
	Note	**2017**	**2016**	**2017**	**2016**
Revenue					
Gross written and assumed premiums		85,035	67,791	139,621	109,912
Less: Premiums ceded to reinsurers		(6,050)	(4,247)	(10,560)	(7,659)
Net written and assumed premiums		78,985	63,544	129,061	102,253
(Increase) in gross unearned premiums		(27,304)	(18,725)	(28,488)	(13,284)
Increase in unearned premiums, reinsurers' share		1,767	428	1,900	(374)
Change in provision for unearned premiums		(25,537)	(18,297)	(26,588)	(13,658)
Net earned premiums		53,448	45,247	102,473	88,595
Investment income	6	2,977	4,916	11,464	8,861
Total revenue		56,425	50,163	113,937	97,456
Expenses					
Gross claims incurred		33,856	31,667	64,302	61,663
Less: claims recoveries from reinsurers		(2,048)	(3,425)	(3,626)	(5,118)
Net incurred claims		31,808	28,242	60,676	56,545
Gross acquisition costs		13,475	11,666	27,073	22,758
Less: acquisition cost recoveries from reinsurers		(1,541)	(1,400)	(3,088)	(2,708)
Net acquisition costs		11,934	10,266	23,985	20,050
Operating costs	14	8,318	8,269	15,708	17,053
Total expenses		52,060	46,777	100,369	93,648
Income before interest expense and income taxes		4,365	3,386	13,568	3,808
Interest expense	9	84	53	155	97
Income tax expense	13	1,088	1,135	2,754	596
Net income on continued operations		3,193	2,198	10,659	3,115
Net (loss) on discontinued operations	18	—	(23,937)	(7,268)	(25,618)
Net income (loss)		3,193	(21,739)	3,391	(22,503)
Attributed to:					
Shareholders of the Company - continued operations		3,142	1,813	10,597	2,773
Shareholders of the Company - discontinued operations		—	(23,939)	(7,268)	(25,528)
Non-controlling interest - continued operations	19	51	385	62	342
Non-controlling interest - discontinued operations		—	2	—	(90)
Net income (loss)		3,193	(21,739)	3,391	(22,503)
Other comprehensive income (loss), net of taxes that may be classified subsequently to net income					
Available-for-sale investments:					
Change in net unrealized (losses)		(1,899)	3,188	(390)	1,770
Reclassification of net realized (gains) to net income		(31)	(2,396)	54	(4,729)
Cumulative translation gain (loss)		—	(172)	—	(394)
Foreign exchange forward	6	—	831	(4,314)	4,314
Tax impact		529	(277)	668	23
Other comprehensive (loss) on continued operations		(1,401)	1,174	(3,982)	984
Other comprehensive income (loss) income on discontinued operations		—	(2,331)	7,268	(3,126)
Other comprehensive (loss) income		(1,401)	(1,157)	3,286	(2,142)

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

Attributed to:					
Shareholders of the Company - continued operations		(1,360)	1,179	(3,958)	984
Shareholders of the Company - discontinued operations		—	(2,301)	7,268	(3,086)
Non-controlling interest - continued operation	19	(41)	(10)	(24)	—
Non-controlling interest - discontinued operation		—	(25)	—	(40)
Other comprehensive (loss) income		(1,401)	(1,157)	3,286	(2,142)
Total comprehensive income (loss)		1,792	(22,896)	6,677	(24,645)
Attributed to:					
Shareholders of the Company - continued operations		1,782	2,992	6,639	3,757
Shareholders of the Company - discontinued operations		—	(26,240)	—	(28,614)
Non-controlling interest - continued operation	19	10	375	38	342
Non-controlling interest - discontinued operation		—	(23)	—	(130)
Total comprehensive income (loss)		1,792	(22,896)	6,677	(24,645)
Earnings per share attributable to shareholders of the Company	17				
Earnings per share continued operations - basic		$0.27	$0.15	$0.90	$0.24
(Loss) per share discontinued operations - basic		$0.00	$(2.04)	$(0.62)	$(2.18)
(Loss) earnings per share - basic		$0.27	$(1.89)	$0.28	$(1.94)
Earnings per share continued operations - diluted		$0.26	$0.15	$0.88	$0.23
(Loss) per share discontinued operations - diluted		$0.00	$(2.04)	$(0.62)	$(2.18)
(Loss) earnings per share - diluted		$0.26	$(1.89)	$0.28	$(1.94)
Net income (loss)		3,193	(21,739)	3,391	(22,503)

The accompanying notes are an integral part of these condensed 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, 2017	70,227	322	(5,070)	71,935	137,414	3,960	141,374
Net income	—	—	—	3,329	3,329	62	3,391
Other comprehensive income	—	—	3,310	—	3,310	(24)	3,286
Total comprehensive income	—	—	3,310	3,329	6,639	38	6,677
Transfer of currency translation adjustment	—	—	(99)	318	219	(219)	—
Common shares issued on stock options exercised	878	(107)	—		771	—	771
Stock compensation expense	—	14	—	—	14	—	14
Balance at June 30, 2017	71,105	229	(1,859)	75,582	145,057	3,779	148,836

	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	104,786	180,935	4,010	184,945
Net income (loss)	—	—	—	(22,750)	(22,750)	247	(22,503)
Other comprehensive income (loss)	—	—	(2,102)	—	(2,102)	(40)	(2,142)
Total comprehensive income (loss)	—	—	(2,102)	(22,750)	(24,852)	207	(24,645)
Common shares repurchased	(292)	—	—	(384)	(676)	—	(676)
Dividends paid	—	—	—	(2,814)	(2,814)	—	(2,814)
Investment in subsidiary - Qudos	—	—	—	270	270	(270)	—
Common shares issued on stock options exercised	648	—	—	—	648	—	648
Stock options expense	—	(70)	—	—	(70)	—	(70)
Balance at June 30, 2016	70,009	366	3,958	79,108	153,441	3,947	157,388

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)

	June 30, 2017	June 30, 2016
Cash provided by (used in):		
Operating activities		
Net income from continuing operations	10,659	3,115
Net loss from discontinued operations	(7,268)	(25,618)
Adjusted for:		
Reinsurers' share of unearned premiums	(1,900)	376
Reinsurers' share of unpaid claims	(1,085)	(1,383)
Provision for unpaid claims	(842)	2,698
Unearned premiums	28,488	13,285
Deferred income taxes	128	(442)
Unearned commissions	(39)	169
Deferred policy acquisition costs	(6,019)	(3,770)
Amortization on property plant equipment and intangible assets	2,894	1,893
Amortization of premiums on bonds	813	961
Fair value change on FVTPL investments	(2,951)	(2,271)
Options expense	14	(70)
Currency translation	—	(394)
Foreign exchange forward	(4,314)	4,314
Prepaid expenses & other assets	(386)	1,318
	14,801	16,684
Cash flow from changes in		
Accounts receivable	(23,094)	(9,481)
Loan receivable	(18,238)	—
Net realized losses (gains)	958	278
Income taxes payable	1,926	1,235
Due to insurance companies	2,899	(43)
Other liabilities	4,228	2,137
Cash (used) provided by continuing operating activities	(5,861)	13,925
Cash (used) provided by discontinued operating activities	(137,935)	13,092
Cash (outflow) inflow from operating activities	(143,796)	27,017
Financing activities		
Proceeds from issue of common shares for stock options	771	648
Common share dividends	—	(2,814)
Share repurchases	—	(676)
Cash provided (used) by continuing financing activities	771	(2,842)
Cash inflow (outflow) from financing activities	771	(2,842)
Investing activities		
Purchases of property, equipment and intangible assets	(3,579)	(2,890)
Purchases of investments	(179,722)	(148,147)
Sale/maturity of investments	174,942	215,877
Proceeds received from the sale of subsidiary	5,117	—
Cash (used) provided by continuing investing activities	(3,242)	64,840
Cash provided (used) by discontinued investing activities	62,619	(13,746)
Cash inflow from investing activities	59,377	51,094

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

(Decrease) Increase in cash and short-term deposits	(83,648)	75,269
Cash and short-term deposits, beginning of period	137,635	23,373
Cash and short-term deposits, end of period	53,987	98,642
Supplementary information		
Operating activities		
Income taxes paid (recovered)	818	(78)

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

1 Nature of operations

Echelon Financial Holdings Inc. ("the Company") 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. 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").

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, 2016, which have been prepared in accordance with IFRS.

These consolidated financial statements have been authorized for issue by the Board of Directors on August 9, 2017.

3 Summary of significant accounting policies

The accounting policies adopted are consistent with those of the previous financial year end 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 probable to occur within one year. Assets and liabilities classified as held-for-sale are measured at the 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 17 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. The Company has decided to defer adoption to IFRS 17.

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 is currently evaluating the impact of IFRS 15 on its Consolidated Financial Statements and based on its preliminary workings, the impact will be minimal.

IFRS 16, Leases

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

IFRS 17, Insurance Contracts

In May 2017, the IASB published IFRS 17 which is effective January 1, 2021, with retrospective application. The standard replaces IFRS 4. The standard is comprehensive in scope and addresses recognition, measurement, presentation and disclosure for insurance contracts. The standard requires the entity to recognise a group of insurance contracts it issues from the earliest of the following: (a) the beginning of the coverage period of the group of contracts; (b) the date when the first payment from a policyholder in the group becomes due; and (c) for a group of onerous contracts, when the group becomes onerous. The measurement approach is based on the following building blocks: (i) a current, unbiased probability-weighted estimate of future cash flows expected to arise as the insurer fulfills the contract; (ii) the effect of the time value of money; (iii) a risk adjustment that measures the effects of uncertainty about the amount and timing of future cash flows; and (iv) a contractual service margin which represents the unearned profit in a contract (that is recognized in net earnings as the insurer fulfills its performance obligations under the contract). Estimates are required to be re-measured each reporting period. In addition, a simplified measurement approach is permitted for short-duration contracts in which the coverage period is approximately one year or less. The Company is currently evaluating the impacts of IFRS 17 on its consolidated financial statements.

4 Critical accounting estimates and 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 thousands of Canadian dollars, except per share amounts)

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 2016 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.

6 Investments

The following table provides a breakdown of the investment portfolio as at June 30, 2017, and December 31, 2016.

	Fair values	
Available-for-sale	**As at June 30, 2017**	**As at December 31, 2016**
Fixed income		
Canadian		
Federal	52,979	67,826
Provincial	34,316	44,147
Municipal	509	519
Corporate	130,753	136,984
	218,557	249,476
Fixed income lent through securities lending program		
Federal	44,667	15,390
Provincial	9,620	998
Municipal	844	845
Corporate	5,614	1,885
	60,745	19,118
Total fixed income	279,302	268,594
Commercial mortgage pooled funds	—	17,423
Money market pooled funds	842	200
Short-term fixed income and mortgage pooled funds	19,302	17,229
Total pooled funds	20,144	34,852
Common shares		
Canadian	318	312
Total common shares	318	312
Total available-for-sale	299,764	303,758
Fair value through profit or loss		
Preferred shares	42,385	32,678
Preferred shares lent through securities lending program	5	99
Total preferred shares	42,390	32,777
Total investments	342,154	336,535
Cash and short-term deposits	53,987	50,588
Total investments including cash and short-term deposits	396,141	387,123

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 June 30, 2017, the Company had collateral of $67,715 (December 31, 2016 – $20,580) for the loaned securities or approximately 108% of the fair value of the loaned securities.

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

Fair value

The Company is responsible for determining the fair value of its investment portfolio by utilizing market-driven fair value measurements from active markets, where available, by considering other observable and unobservable inputs and by employing valuation techniques which make use of current market data. The technique employed has remained the same from December 31, 2016. The Company uses a fair-value hierarchy to categorize the inputs used in valuation techniques to measure fair value. A description of the inputs used in the valuation of financial instruments is as follows:

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

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

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

Level 3 – Inputs that are not based on observable market data. Management is required to use assumptions regarding unobservable inputs as there is little, if any, market activity in these investments or related observable inputs that can be corroborated at the measurement date. Unobservable inputs require management to make certain projections and assumptions about the information that would be used by market participants in pricing assets. To verify pricing, the Company assesses the 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 June 30, 2017, and December 31, 2016:

June 30, 2017				
	Level 1	**Level 2**	**Level 3**	**Total**
Fixed income	—	279,302	—	279,302
Money market pooled funds	—	842	—	842
Short-term fixed income and mortgage pooled funds	—	19,302	—	19,302
Equities	318	—	—	318
Preferred Shares	42,390	—	—	42,390
	42,708	299,446	—	342,154

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

December 31, 2016				
	Level 1	**Level 2**	**Level 3**	**Total**
Fixed income	—	268,594	—	268,594
Commercial mortgages pooled funds	—	17,423	—	17,423
Money market pooled funds	—	200	—	200
Short-term fixed income and mortgage pooled funds	—	17,229	—	17,229
Equities	312	—	—	312
Preferred Shares	32,777	—	—	32,777
	33,089	303,446	—	336,535

Investments in commercial mortgage pooled funds is valued using the Company's share of the net asset value of the commercial mortgage pooled fund as of June 30, 2017, and December 31, 2016.

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 six months ended June 30, 2017 or 2016.

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.

The Company has interests in unconsolidated structured entities, through investments in pooled funds, which are included in investments on the balance sheets. These entities are not controlled by the Company. The carrying value of pooled funds and maximum exposure to loss as of June 30, 2017 was $20,144 (December 31, 2016 – $34,852). Investments in pooled funds consist of units invested in underlying money market and mortgage securities managed by third-party managers. The pooled funds are perpetual private trusts created under trust agreements. Financing and support is only provided to the pooled funds through the purchase of units and is therefore limited to the investment made.

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

No impairments on AFS investments were recognized for the period ended June 30, 2017 and 2016. Gross unrealized loss of $1,755 on AFS investments at June 30, 2017 (December 31, 2016 – $1,691) is recorded, net of tax, in the amount of $1,275 (December 31, 2016 – $1,231) 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 June 30		6 months ended June 30	
	2017	**2016**	**2017**	**2016**
Interest income	2,244	2,710	4,346	5,862
Dividend income	397	555	767	1,019
Net realized (losses) gains	(27)	(2,292)	(958)	(278)
Fair value change on FVTPL investments	201	4,174	2,951	2,271
Realized and unrealized foreign exchange gains	347	(8)	4,727	459
Investment expenses	(185)	(223)	(369)	(472)
Investment income	2,977	4,916	11,464	8,861

7 Loan receivable

On March 7, 2017, the Company entered into a loan agreement with New Nordic Odin Guernsey Limited to lend the principal amount of 91.5 million Danish Krone (DKK) payable on December 31, 2017.

The loan bears interest on the principal amount outstanding at the rate of six percent (6%) per annum that commenced on July 6, 2017 and is payable monthly.

8 Derivative financial instruments

The details of the outstanding contracts for hedging the sales proceeds of the European subsidiary are as follows:

Contract Party	Deal Date	Value Date	FX Contract Purchase Amount CAD$	FX Contract Sale Amount DKK	Contract Rate	Rate as at June 30, 2017	Net Settlement Amount at June 30, 2017
RBC Royal Bank	8-Dec-16	6-Jul-17	12.0M	63.4M	5.2850	5.0210	(0.6) M
RBC Royal Bank	16-May-17	6-Jul-17	5.7M	28.1M	4.9450	5.0210	0.1 M

9 Line of credit

The Company had a $10.0 million two-year secured revolving term credit facility effective June 30, 2015, which matured on July 1, 2017. The facility expired and will not be renewed.

For the year ended June 30, 2017, the Company has expensed $0.2 million on the income statement, below income before interest expense and income tax, related to the maintenance of the credit facility (June 30, 2016 – $0.1 million).

10 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.

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

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:

Entity	June 30, 2017	December 31, 2016
Echelon Insurance	1.90%	1.90%
ICPEI	1.85%	1.75%

The Company recorded a $11,126 reduction to the net provision for unpaid claims relating to redundancies in prior years' estimates (June 30, 2016 – $9,342).

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 $19,426 as at June 30, 2017 (December 31, 2016 – $21,388).

Claims development

Provision for unpaid claims analysis	June 30, 2017	June 30, 2016
Unpaid claims, beginning of year, net	228,106	231,626
Favourable prior year claims development	(11,126)	(9,342)
Provision for claims occurring in current period	71,802	65,887
Paid on claims occurring during		
Current year	(25,422)	(20,416)
Prior year	(37,181)	(34,814)
Unpaid claims, end of period, net	226,179	232,941
Reinsurers' share	28,108	30,605
Gross unpaid claims	254,287	263,546

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.

11 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.

Following the sale of its European operations completed in the first quarter of 2017 (see note 18) the company's Insurance risk is lower compared to the year end.

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 June 30, 2017, and December 31, 2016, 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 June 30, 2017			
200 basis point rise	263,462	(6)%	(11,563)
100 basis point rise	271,382	(3)%	(5,782)
No change	279,302	—	—
100 basis point decline	287,222	3%	5,781
200 basis point decline	295,142	6%	11,561

Change in interest rates	Fair value of fixed income	Hypothetical change on fair value	Effect on OCI net of tax
As at December 31, 2016			
200 basis point rise	252,340	(6)%	(11,865)
100 basis point rise	260,468	(3)%	(5,932)
No change	268,594	—	—
100 basis point decline	276,722	3%	5,931
200 basis point decline	284,850	6%	11,863

(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 June 30, 2017, and December 31, 2016, are as follows:

June 30, 2017	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Bonds	25,209	94,146	95,790	64,157	279,302
Percentage of total	9%	34%	34%	23%	100%

December 31, 2016	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Bonds	18,190	76,090	100,469	73,845	268,594
Percentage of total	7%	28%	37%	28%	100%

The following tables summarize the expected timing of cash flows arising from insurance obligations, on an undiscounted basis, as at June 30, 2017, and December 31, 2016:

June 30, 2017	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Actuarial liabilities (undiscounted)	75,792	78,999	40,843	22,647	218,281
Less: Reinsurance recoverable (undiscounted)	7,699	7,450	3,242	4,559	22,950
Net actuarial liabilities	68,093	71,549	37,601	18,088	195,331

December 31, 2016	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Actuarial liabilities (undiscounted)	86,700	87,875	43,864	24,008	242,447
Less: Reinsurance recoverable (undiscounted)	9,251	8,928	3,608	4,660	26,447
Net actuarial liabilities	77,449	78,947	40,256	19,348	216,000

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 six months ended June 30, 2017, and the year ended December 31, 2016. 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**	
	June 30, 2017	**December 31, 2016**	**June 30, 2017**	**December 31, 2016**
10% rise	3,094	2,393	23	23
10% decline	(3,094)	(2,393)	(23)	(23)

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. 99.8% of the Company's reinsurance balances are from registered reinsurers. The Company holds sufficient collateral to cover the 0.2% of reinsurance balances from unregistered reinsurers.

The following table sets forth the Company's fixed income securities portfolio by credit quality as at June 30, 2017, and December 31, 2016.

Fixed income portfolio

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

	As at June 30, 2017		**As at December 31, 2016**	
	Fair value	**Fair value**	**Fair value**	**Fair value**
AAA	121,426	43%	107,267	40%
AA	47,372	17%	52,728	20%
A	74,128	27%	67,360	25%
BBB	36,376	13%	41,239	15%
Total	279,302	100%	268,594	100%

Preferred share portfolio

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

	As at June 30, 2017		**As at December 31, 2016**	
	Fair value	Fair value	Fair value	Fair value
P2	36,050	85%	29,600	90%
P3	6,340	15%	3,177	10%
Total	42,390	100%	32,777	100%

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

12 Intangible assets

	Opening cost	Purchases	Sales	End of period cost	Accumulated amortization	Net
Software						
June 30, 2017	28,712	3,024	—	31,736	23,351	8,385
December 31, 2016	23,014	5,698	—	28,712	20,915	7,797
Goodwill						
June 30, 2017	400	—	—	400	—	400
December 31, 2016	400	—	—	400	—	400
Total intangible assets						
June 30, 2017	29,112	3,024	—	32,136	23,351	8,785
December 31, 2016	23,414	5,698	—	29,112	20,915	8,197

13 Income taxes

The income tax is as follows:

	3 months ended June 30		6 months ended June 30	
	2017	**2016**	**2017**	**2016**
Current	1,150	918	2,626	867
Deferred	(62)	217	128	(271)
	1,088	1,135	2,754	596

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

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

The difference is broken down as follows:

	3 months ended June 30		6 months ended June 30	
	2017	**2016**	**2017**	**2016**
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	(2.5)%	4.5 %	(1.5)%	2.7 %
Non-taxable (income) loss	— %	(9.0)%	— %	(23.2)%
Non-deductible expenses	(0.5)%	4.1 %	0.1 %	7.7 %
Tax benefit of losses not previously recognized	1.5 %	(0.8)%	(4.9)%	(1.9)%
Statutory rate differences	0.3 %	2.0 %	0.1 %	1.3 %
Non-taxable portion of capital gains	— %	(0.8)%	— %	(1.9)%
Other	(0.4)%	0.1 %	(0.2)%	4.2 %
Effective income tax rate	25.4 %	27.1 %	20.6 %	15.9 %

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

14 Operating Costs by nature

The table below presents operating costs by major category:

	3 months ended June 30		6 months ended June 30	
	2017	**2016**	**2017**	**2016**
Salaries and benefits	4,443	3,408	8,519	7,828
Systems costs	2,327	1,992	4,451	3,689
Professional fees	639	312	1,455	606
Occupancy	437	265	826	575
Severance	89	1,028	89	2,512
Other expenses	383	1,264	368	1,843
	8,318	8,269	15,708	17,053

15 Lease commitments

The Company is committed under lease agreements for office premises and computer equipment with minimum lease payments of $11,656 as follows:

Lease commitments	
2017	890
2018	1,759
2019	1,671
2020	1,395
2021	1,411
2022 and thereafter	4,530
	11,656

16 Accumulated other comprehensive income

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

	As at June 30, 2017	As at December 31, 2016
Gross unrealized losses	(2,468)	(459)
Foreign currency translation adjustments	499	(10,776)
Foreign exchange forward	—	4,314
Tax impact	110	1,851
Ending balance	(1,859)	(5,070)

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

17 Earnings per share

	3 months ended June 30		6 months ended June 30	
	2017	**2016**	**2017**	**2016**
Basic earnings per share on continued operations:				
Net income available to shareholders	3,142	1,813	10,597	2,773
Average number of common shares	11,829	11,723	11,794	11,731
Basic earnings per share on continued operations	$0.27	$0.15	$0.90	$0.24
Diluted earnings per share:				
Average number of common shares	11,829	11,723	11,794	11,731
Average number of dilutive common shares under employee stock compensation plan	201	262	219	267
Average number of diluted common shares	12,030	11,985	12,013	11,998
Diluted earnings per share on continued operations	$0.26	$0.15	$0.88	$0.23

	3 months ended June 30		6 months ended June 30	
	2017	**2016**	**2017**	**2016**
Basic earnings per share on discontinued operations:				
Net income available to shareholders	—	(23,939)	(7,268)	(25,528)
Average number of common shares	11,829	11,723	11,794	11,731
Basic earnings per share on discontinued operations	$0.00	$(2.04)	$(0.62)	$(2.18)
Diluted earnings per share:				
Average number of common shares	11,829	11,723	11,794	11,731
Average number of dilutive common shares under employee stock compensation plan	201	262	219	267
Average number of diluted common shares	12,030	11,985	12,013	11,998
Diluted earnings per share on discontinued operations	$0.00	$(2.04)	$(0.62)	$(2.18)

	3 months ended June 30		6 months ended June 30	
	2016	**2015**	**2017**	**2016**
Basic earnings per share:				
Net income available to shareholders	3,142	(22,126)	3,329	(22,755)
Average number of common shares	11,829	11,723	11,794	11,731
Basic earnings (loss) per share	$0.27	$(1.89)	$0.28	$(1.94)
Diluted earnings per share:				
Average number of common shares	11,829	11,723	11,794	11,731
Average number of dilutive common shares under employee stock compensation plan	201	262	219	267
Average number of diluted common shares	12,030	11,985	12,013	11,998
Diluted earnings (loss) per share	$0.26	$(1.89)	$0.28	$(1.94)

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

18 Discontinued operations

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

	3 months ended June 30		6 months ended June 30	
	2017	**2016**	**2017**	**2016**
Revenue				
Gross written and assumed premiums	—	81,185	15,896	133,464
Net written premium	—	38,729	12,784	63,114
Decrease in provision for unearned premium	—	1,039	6,173	17,214
Net earned premiums	—	39,768	18,957	80,328
Investment (loss) income	—	354	(10,562)	1,594
Total revenue	—	40,122	8,395	81,922
Expenses				
Net incurred claims	—	27,619	10,392	56,776
Net acquisition costs	—	13,521	6,254	26,621
Operating costs	—	1,817	1,067	4,229
Total expenses	—	42,957	17,713	87,626
(Loss) before income taxes	—	(2,835)	(9,318)	(5,704)
Income tax (recovery)	—	(898)	(2,050)	(2,086)
Net (loss) on discontinued operations	—	(1,937)	(7,268)	(3,618)
Impairment of the net assets of disposal group held for sale	—	(22,000)	—	(22,000)
Net (loss) income on discontinued operations	—	(23,937)	(7,268)	(25,618)
Other comprehensive income (loss) on discontinued operations	—	(2,331)	7,268	(3,126)
Comprehensive (loss) on discontinued operations	—	(26,268)	—	(28,744)

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

19 Non-controlling interest

The Company has non-controlling interests attributable to the subsidiary of ICPEI, please refer to Note 1. The following tables summarize the comprehensive income attributable to the non-controlling shareholders for year ending June 30:

	3 months ended June 30		6 months ended June 30	
	2017	**2016**	**2017**	**2016**
Revenue				
Gross written and assumed premiums	2,459	2,226	4,100	3,687
Net earned premiums	1,766	1,640	3,396	3,177
Investment income	73	134	204	142
Total revenue	1,839	1,774	3,600	3,319
Expenses				
Net incurred claims	1,131	613	2,249	1,611
Net acquisition costs	411	377	839	731
Operating costs	229	251	435	505
Total expenses	1,771	1,241	3,523	2,847
Income (loss) before income taxes	68	533	77	472
Income tax	17	148	15	130
Net income (loss) attributable to NCI	51	385	62	342
Other comprehensive income attributable to NCI	(41)	(10)	(24)	—
Comprehensive income (loss) attributable to NCI	10	375	38	342

The following tables are the net assets of the non-controlling shareholders as June 30, 2017 and December 31, 2016:

	As at June 30, 2017	**As at December 31, 2016**
Assets		
Cash and investments	9,371	9,421
Other assets	4,936	4,376
Total assets	14,307	13,797
Liabilities		
Unearned premium	4,063	3,699
Unpaid claims	6,044	5,709
Other liabilities	421	648
Total liabilities	10,528	10,056
Equity		
Share capital	—	—
AOCI	(68)	(44)
Retained earnings	3,847	3,785
Total equity	3,779	3,741
Total liabilities and equity	14,307	13,797

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

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

	As at June 30, 2017	As at December 31, 2016
Cash flow from operating activities	(63)	1,138
Cash flow from investing activities	(614)	(232)
Cash flow from financing activities		—
Net increase (decrease) in cash and short-term deposits	(677)	906

20 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 and warranty coverage.

The European operations are discontinued. Please refer to note 18.

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 June 30		6 months ended June 30	
	2017	**2016**	**2017**	**2016**
Revenue				
Earned premiums				
– Personal Lines	39,317	34,614	76,311	67,974
– Commercial Lines	14,131	10,633	26,162	20,621
Total earned premium	53,448	45,247	102,473	88,595
Net claims incurred				
– Personal Lines	25,876	23,758	48,984	45,690
– Commercial Lines	5,932	4,484	11,692	10,855
Total net claims incurred	31,808	28,242	60,676	56,545
Net expenses				
– Personal Lines	12,091	11,425	24,087	22,110
– Commercial Lines	6,080	4,563	11,351	8,927
Total	18,171	15,988	35,438	31,037
Corporate Expenses	1,992	1,519	4,166	3,554
Total net expenses	20,163	17,507	39,604	34,591
Income before income taxes				
– Personal Lines	1,350	(569)	3,240	174
– Commercial Lines	2,119	1,586	3,119	839
Total	3,469	1,017	6,359	1,013
Corporate and other	(1,992)	(1,519)	(4,166)	(3,554)
Underwriting income (loss)	1,477	(502)	2,193	(2,541)
Severance expense	(89)	(1,028)	(89)	(2,512)
Investment income	2,977	4,916	11,464	8,861
Total income before interest and income taxes	4,365	3,386	13,568	3,808