ECHELON FINANCIAL HOLDINGS INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS

For the twelve months ended December 31, 2017

TABLE OF CONTENTS

ECHELON FINANCIAL HOLDINGS INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION

AND RESULTS OF OPERATIONS

For the period ending December 31, 2017

Echelon Financial Holdings Inc. ("EFH" or "the Company") prepares its financial statements in accordance with International Financial Reporting Standards (IFRS), issued and effective as of December 31, 2017, as set out in the Handbook of the Chartered Professional Accountants (CPA Handbook).

The financial data for 2017, 2016 and 2015 in this discussion has been prepared in accordance with IFRS.

References to "EFH" or "the Company" in this Management's Discussion and Analysis of Financial Condition and Results of Operations refer to Echelon Financial Holdings Inc. on a consolidated basis, both now and in its predecessor forms.

The following discussion should be read in conjunction with EFH's audited consolidated financial statements and the related notes. The following commentary is current as of February 15, 2018. Additional information relating to EFH is available on SEDAR at www.sedar.com. Certain totals, subtotals and percentages may not reconcile due to rounding.

The Company uses both IFRS and certain non-IFRS measures to assess performance. Securities regulators require that companies caution readers about non-IFRS measures that do not have a standardized meaning under IFRS and are unlikely to be comparable to similar measures used by other companies. EFH analyzes performance based on underwriting income and underwriting ratios such as combined, expense and loss ratios, which are non-IFRS measures. Net operating income is defined as underwriting income plus interest and dividend income, net of tax. Underwriting income is defined as net earned premiums less net claims incurred, net acquisition expenses, general expenses and reversing any impact of change in discount rate and foreign exchange on claims and excludes impact of change in claims discount rates, foreign exchange on unpaid claims and investments, and non-recurring items. Net investment income consists of interest income, dividend income and premium financing charges, less interest expense, as per Note 6 of the Company's Financial Statements. Net operating income is adjusted to that attributable to shareholders for per share calculation.

The following discussion contains forward-looking information that involves risk and uncertainties based on current expectations. This information includes, but is not limited to, statements about the operations, business, financial condition, priorities, targets, ongoing objectives, strategies and outlook for the Company in 2017 and subsequent periods.

This information is based upon certain material factors or assumptions that were applied in drawing a conclusion or making a projection as reflected in the forward-looking information. By its nature, this information is subject to inherent risks and uncertainties that may be general or specific. A variety of material factors, many of which are beyond EFH's control, affect the operations, performance and results of the Company and its business and could cause actual results to differ materially from the expectations expressed in any of this forward-looking information (see "Risk Factors").

Forward-looking information is provided for the purpose of providing information about management's current expectations and plans relating to the future. Readers are cautioned that such information may not be appropriate for other purposes. Additional information about the risks and uncertainties about EFH's business is provided in its disclosure materials, including its annual information form, filed with the securities regulatory authorities in Canada, available at www.sedar.com. EFH does not expect to update any forward-looking information.

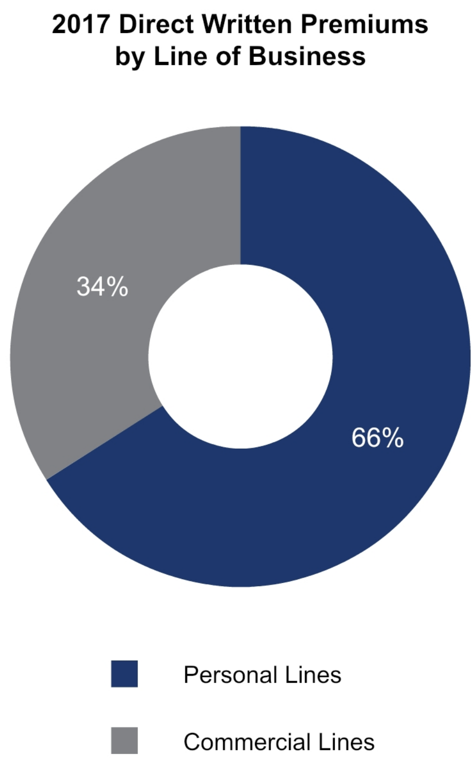
COMPANY OVERVIEW

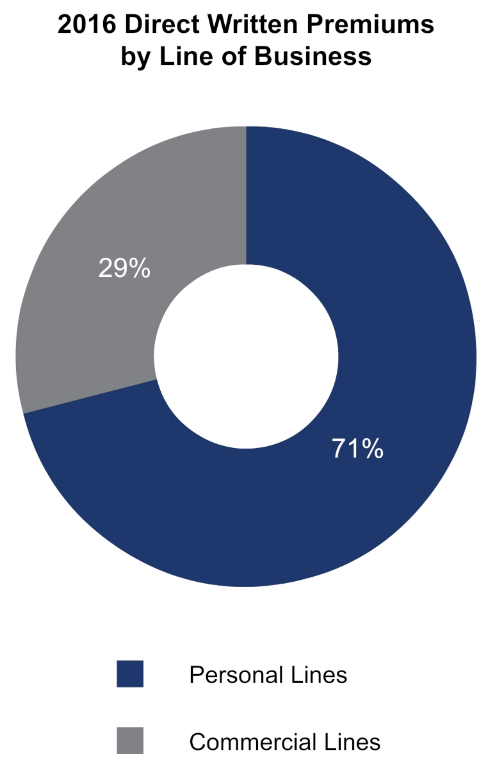
EFH operates in the property and casualty (“P&C”) insurance industry in Canada through Echelon Insurance ("Echelon"), a federally-regulated P&C insurance company and The Insurance Company of Prince Edward Island ("ICPEI"), a provincially regulated P&C insurance company. The Company underwrites automobile insurance and other specialty insurance products, with a focus on niche under-served markets. It has two lines of insurance business – Personal Lines and Commercial Lines. Personal Lines focuses on the underwriting of non-standard automobile insurance and insurance for motorcycles, antique and classic vehicles, trailers, motor-homes, recreational vehicles and personal property. Commercial Lines designs and underwrites Commercial Property, Commercial Automobile, Surety, Liability, and Specialty Programs.

On March 7, 2017, the Company completed the sale of its European operations. The European operation results are referred to as discontinued operations in this document.

EFH intends to grow its business profitably across Canada by offering a complete and diverse suite of products to its brokers, with an ability to transact efficiently through modern systems. EFH currently intends to use any excess capital in addition to capital generated from its operations to fund its growth.

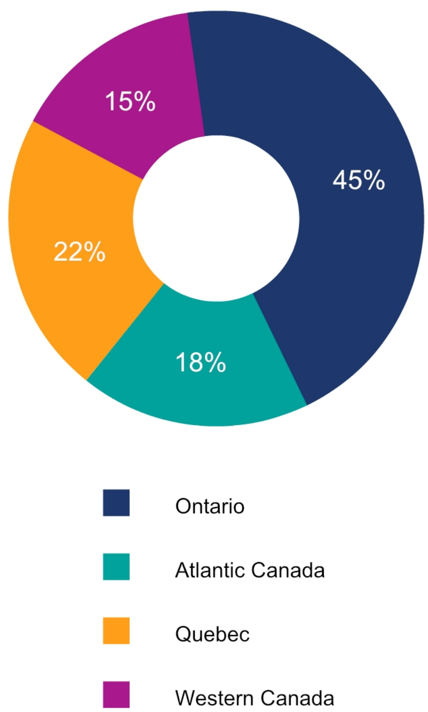
The breakdown of direct written premiums by category of business is shown below for 2017 and 2016 :



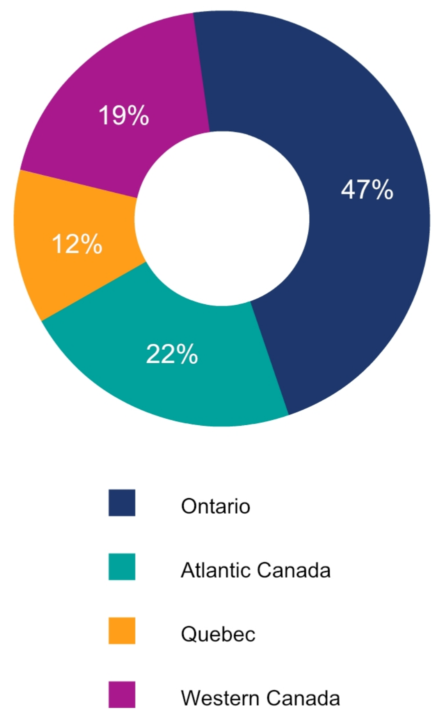


The breakdown of direct written premiums by region is shown below for 2017 and 2016:

2017 Direct Written Premiums by Region



2016 Direct Written Premiums by Region



On a Consolidated basis, 66% of EFH's direct written premiums in 2017 were attributable to premiums from Personal Lines policies while Commercial Lines accounted for 34%.

FOURTH QUARTER HIGHLIGHTS

- Net operating loss on continued operations of $0.51 per share compared to income of $0.40 per share in the fourth quarter of 2016.
- A combined operating ratio of 115% compared to 90% in the fourth quarter of 2016, primarily due to increased severity of claims compared to the prior year quarter, especially in Atlantic Auto.
- A 38% increase in direct written premiums over the same period in 2016 to $68.1 million as a result of organic growth in Personal Lines and growth in new Commercial Lines products launched in 2016.
- A pre-tax gain on invested assets of $3.6 million in the quarter compared to a pre-tax loss of $0.6 million in the prior year quarter, attributable to positive returns on the fixed income portfolio driven by spread compression in provincial and corporate bonds, in addition to strong returns in the preferred share and equity portfolios.
- Closing book value per share of $12.01, a decrease of 1% over the third quarter of 2017.

The following financial information compares three months ended December 31, 2017 results with the same period in 2016.

	3 months ended December 31		Change	
($ THOUSANDS except per share amounts)	**2017**	**2016**	**$**	**%**
Direct written and assumed premiums	68,050	49,403	18,647	38
Net written premiums	65,235	44,476	20,759	47
Net earned premiums	64,906	46,013	18,893	41
Net claims incurred	52,825	25,654	27,171	106
Net acquisition costs	15,173	10,680	4,493	42
Operating expenses	8,116	7,124	992	14
Underwriting (loss) income	(11,208)	2,555	(13,763)	(539)
Severance expense	(87)	(769)	682	89
Investment income	3,316	3,159	157	5
Impact of discount rate on claims	1,220	(1,370)	2,590	(189)
Net (loss) income before interest and income taxes	(6,759)	3,575	(10,334)	(289)
Interest expense	—	63	(63)	(100)
Income tax (recovery) expense	(1,933)	911	(2,844)	312
Net (loss) income	(4,826)	2,601	(7,427)	(286)
Net (loss) income attributable to shareholders	(4,966)	2,598	(7,564)	(291)
Net operating (loss) income attributable to shareholders	(6,252)	4,857	(11,109)	(229)
(Loss) Earnings per share				
Basic	($0.42)	$0.22	$(0.64)	(291)
Diluted	($0.42)	$0.22	$(0.64)	(291)
Net operating (loss) income per share – diluted [1]	($0.51)	$0.40	$(0.91)	(228)
Trailing twelve month return on equity (ROE) - continuing operations [2]	4.6%	4.2%		

[1] Net operating income is defined as underwriting income plus interest and dividend income, net of tax. Underwriting income excludes impact of change in claims discount rates, and non-recurring items. Net investment income consists of interest income, dividend income and premium financing charges, less interest expense, as per Note 6 of the Company's Consolidated Financial Statements. Net operating income is adjusted to that attributable to shareholders for per share calculation.

[2] ROE calculated on rolling twelve-month basis

Insurance Operations

Direct Written, Net Written and Net Earned Premiums

In the fourth quarter of 2017, direct written premiums increased by 38% while net earned premiums increased by 41% compared to the same period prior year. The increase in premium was driven by organic growth in Personal Lines and new Commercial Lines products launched in 2016.

Claims Incurred

For the quarter ended December 31, 2017, net claims expense increased by 106%, primarily due to increased severity of Personal Auto claims in the Atlantic provinces.

Net favourable development of prior year claims of $2.3 million was recorded in the fourth quarter of 2017 compared to net favourable development of $3.4 million in the same period in 2016. The favourable development primarily arose from the Commercial Lines segment and $1.2 million of the development related to a change in discount rate.

Acquisition Costs

Acquisition costs, which consist mainly of commissions, premium taxes and a portion of general expenses related to policy acquisitions, increased by 42%, in the quarter ended December 31, 2017, in line with the increase in net earned premiums.

Operating Expenses

Operating expenses increased by $1.0 million or 14%, to $8.1 million in the fourth quarter of 2017 compared to $7.1 million in the comparative quarter, driven by increased information technology and compensation expenses.

Underwriting Income

Underwriting loss of $11.2 million was recorded in the fourth quarter of 2017 compared to an underwriting income of $2.6 million in the same period in 2016 due to weak Personal Lines results in the quarter.

Investment Income

Investment income was $3.3 million comparable to $3.2 million in the fourth quarter of 2016.

Net Income before Income Taxes

For the quarter ended December 31, 2017, net loss before taxes was $6.8 million compared to income of $3.6 million in the fourth quarter of 2016 primarily due to a decrease in underwriting income.

Income Taxes

For the quarter ended December 31, 2017, the provision for income taxes reflects a recovery of $1.9 million compared to an expense of $0.9 million for the same period last year.

SEGMENTED FINANCIAL INFORMATION (Continued Operations)

The segmented results below exclude corporate expenses.

TOTAL OPERATIONS

	3 months ended December 31				Twelve months ended December 31			
($THOUSANDS)	**2017**	**2016**	**$ Change**	**% Change**	**2017**	**2016**	**$ Change**	**% Change**
Direct written premiums	68,050	49,403	18,647	38	285,718	217,486	68,232	31
Net earned premiums	64,906	46,013	18,893	41	227,396	181,060	46,336	26
Net claims:								
Current year claims	55,106	29,096	26,010	89	182,559	128,015	54,544	43
Current year loss ratio	84.9%	63.2%			80.3%	70.7%		
Favourable prior year claims development	2,281	3,442	(1,161)	(34)	25,745	17,243	8,502	49
Total net claims	52,825	25,654	27,171	106	156,814	110,772	46,042	42
Loss ratio	81.4%	55.8%			69.0%	61.2%		
Expense ratio	33.8%	34.5%			33.3%	35.0%		
Combined ratio	115.2%	90.3%			102.3%	96.2%		
Underwriting income (loss)	(9,844)	4,326	(14,170)	(328)	(5,183)	6,814	(11,997)	(176)

PERSONAL LINES

	3 months ended December 31				Twelve months ended December 31			
($THOUSANDS)	**2017**	**2016**	**$ Change**	**% Change**	**2017**	**2016**	**$ Change**	**% Change**
Direct written premiums	42,638	31,171	11,467	37	189,454	154,992	34,462	22
Net earned premiums	45,865	35,285	10,580	30	165,893	139,616	26,277	19
Net claims:								
Current year claims	43,527	26,059	17,468	67	144,467	106,017	38,450	36
Current year loss ratio	94.9%	73.9%			87.1%	76.0%		
(Unfavourable) favourable prior year claims development	(175)	(1,560)	1,385	89	19,582	8,194	11,388	139
Total net claims	43,702	27,619	16,083	58	124,885	97,823	27,062	28
Loss ratio	95.3%	78.3%			75.3%	70.1%		
Expense ratio	31.5%	31.8%			30.2%	32.2%		
Combined ratio	126.8%	110.1%			105.5%	102.3%		
Underwriting income (loss)	(12,265)	(3,530)	(8,735)	247	(9,186)	(3,177)	(6,009)	(189)

Fourth quarter 2017

Personal Lines recorded an underwriting loss of $12.3 million compared to an underwriting loss of $3.5 million in the same period last year. Direct written premiums increased by 37% in the quarter due to organic growth in personal auto in Ontario and Quebec.

This segment's combined ratio increased to 127% in the quarter as a result of the following factors:

1. Increased severity of claims in Atlantic Auto, in addition to increased frequency in Ontario Auto.
2. Weak results in Ontario recreational vehicles.
3. This was partially offset by reduced adverse development compared to the prior quarter.

Year-to-date 2017

Personal Lines reported an underwriting loss of $9.2 million compared to an underwriting loss of $3.2 million in the same period last year. Direct written premiums increased by 22% for the year, primarily due to organic growth in Personal Auto across Canada, but especially in Ontario and Quebec.

This segment's combined ratio increased to 106% for the year as a result of the following factors:

1. Increased severity of claims in Atlantic auto and Ontario motorcycle compared to prior year.
2. $2.0 million impact from BC wildfire losses on Personal Property.
3. These factors were partially offset by improved results in Ontario Auto.

COMMERCIAL LINES

	3 months ended December 31				Twelve months ended December 31			
($THOUSANDS)	**2017**	**2016**	**$ Change**	**% Change**	**2017**	**2016**	**$ Change**	**% Change**
Direct written premiums	25,412	18,232	7,180	39	96,264	62,494	33,770	54
Net earned premiums	19,041	10,728	8,313	77	61,503	41,444	20,059	48
Net claims:								
Current year claims	11,579	3,037	8,542	281	38,092	21,998	16,094	73
Current year loss ratio	60.8%	28.3%			61.9%	53.1%		
Favourable prior year claims development	2,456	5,002	(2,546)	(51)	6,163	9,049	(2,886)	(32)
Total net claims	9,123	(1,965)	11,088	564	31,929	12,949	18,980	147
Loss ratio	47.9%	(18.3)%			51.9%	31.2%		
Expense ratio	39.4%	45.2%			41.6%	44.7%		
Combined ratio	87.3%	26.9%			93.5%	75.9%		
Underwriting income (loss)	2,421	7,856	(5,435)	(69)	4,003	9,991	(5,988)	(60)

Fourth quarter 2017

Commercial Lines recorded an underwriting income of $2.4 million compared to $7.9 million in the same period last year. Direct written premiums increased by 39% in the quarter primarily due to the launch of Commercial Auto and Surety in 2016.

This segment's combined ratio increased to 87% in the quarter from an exceptional 27% in prior year quarter as a result of the following factors:

1. Higher frequency of losses on the warranty book compared to the same period last year.
2. Improved expense ratio due to start up costs incurred in the prior year quarter primarily on the launch of new products.
3. Reduced redundancies on prior year claims of $2.5 million compared to $5.0 million in the same period last year.

Year-to-date 2017

Commercial Lines recorded an underwriting income of $4.0 million compared to $10.0 million in the same period last year. Direct written premiums increased by 54% for the year, primarily due to the launch of Commercial Auto and Surety in 2016.

This segment's combined ratio increased to 94% for the year from an exceptional level of 76% in the prior year as a result of the following factors:

1. Weaker results in Commercial Auto due to increased severity of claims.

1\. Higher frequency of losses on the warranty book compared to the same period last year.

2\. Reduced redundancies on prior year claims of $6.2 million compared to $9.0 million in the same period last year.

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. The Company has received an aggregate of $16.7 million to date on closing and from the partial repayment of the loan, and is scheduled to receive an additional $6.6 million prior to March 31, 2018, which it has recognized as a loan receivable on its balance sheet. Interest payments on the loan are current.

SUMMARY OF QUARTERLY RESULTS

A summary of the Company's last eight quarters (after all corporate expenses) is as follows:

	2017				2016			
($ THOUSANDS except per share amounts)	**Q4**	**Q3**	**Q2**	**Q1**	**Q4**	**Q3**	**Q2**	**Q1**
Direct written and assumed premiums	68,050	78,047	85,035	54,586	49,403	58,171	67,791	42,121
Net earned premiums and other revenue	64,906	60,017	53,448	49,025	46,013	46,452	45,247	43,348
Underwriting income (loss)	(11,208)	(3,428)	1,477	716	2,555	(429)	(485)	(2,055)
Income before interest expense and income taxes	(6,759)	936	4,365	9,203	3,575	1,622	3,402	406
Net income	(4,826)	810	3,193	7,466	2,602	1,402	2,214	901
Net operating income	(6,252)	1,211	3,338	2,316	4,857	1,580	2,892	1,025
Earnings (loss) per adjusted share								
(a) Basic	($0.42)	$0.07	$0.27	$0.63	$0.22	$0.10	$0.15	$0.08
(b) Diluted	($0.42)	$0.07	$0.26	$0.62	$0.22	$0.10	$0.15	$0.08
Net operating income per share - diluted	($0.51)	$0.10	$0.28	$0.19	$0.40	$0.13	$0.24	$0.09
Selected financial ratios								
Loss ratio	81.4%	72.2%	59.5%	58.9%	55.8%	61.5%	62.4%	65.3%
Expense ratio	35.8%	33.5%	37.7%	39.6%	38.6%	39.4%	38.7%	39.4%
Combined ratio	117.2%	105.7%	97.2%	98.5%	94.4%	100.9%	101.1%	104.7%
Book value per share	$12.01	$12.14	$12.25	$12.10	$11.70	$12.90	$13.08	$15.16

The quarterly results reflect the seasonality of the Company's business. While net earned premiums are relatively stable from quarter to quarter, underwriting results may vary significantly by quarter as they are affected by seasonality, as described in Note 5 of the Financial Statements.

Net Operating Income

	Q4 2017	2017	2016	2015	2014	2013
($ THOUSANDS except per share amounts)						
Net investment income	2,821	10,416	11,502	14,050	13,650	13,349
Underwriting income (loss)	(11,208)	(12,443)	(414)	(447)	8,106	(2,980)
Add: CAT losses	—	2,604	3,334	—	—	—
Pre-tax operating income	(8,387)	577	14,422	13,603	21,756	10,369
Income tax	2,275	190	(3,556)	(3,673)	(5,874)	(2,800)
Net operating income	(6,112)	767	10,866	9,930	15,882	7,569
Minority interest	(140)	(154)	(512)	(8)	(129)	—
Net operating income attributable to shareholders	(6,252)	613	10,354	9,922	15,753	7,569
Net operating income per share - diluted	$(0.51)	$0.05	$0.86	$0.83	$1.31	$0.63

2017 FINANCIAL OVERVIEW

Revenue

Revenue reflected in the consolidated financial statements includes net earned premiums, investment income, realized gains and losses on the sale of investments, and other revenue.

($ THOUSANDS)	Q4 2017	2017	2016
Gross premiums written	68,050	285,718	217,486
Net premiums written	65,235	266,807	199,601
Net earned premiums	64,906	227,396	181,060
Net interest and dividends	2,821	10,416	11,502
Realized and unrealized gains on investments	483	2,151	4,150
Foreign exchange gains	12	4,629	855
Total revenue	68,222	244,592	197,567

The Company's main source of revenue was earned premiums from the sale of insurance policies. Gross written premiums totaled $285.7 million, an increase of 31% compared to $217.5 million last year. The increase in gross premiums was primarily due to organic growth in Personal Auto and increased volumes from the newly launched products in 2016.

Personal Lines recorded $189.5 million of premiums in 2017 compared to $155.0 million in 2016, an increase of 22%. Commercial Lines recorded $96.3 million of premiums in 2017 compared to $62.5 million in 2016, an increase of 54%.

Net earned premiums increased $46.3 million, or 26% in 2017, to $227.4 million from $181.1 million in 2016.

Investment income constituted approximately 7% of EFH's total revenue in 2017. Market fluctuations in interest rates and equity markets affect EFH's returns on the market value of fixed income, preferred shares, equity markets and short-term investments. Net realized and unrealized gains including foreign exchange gains on invested assets totaled $6.8 million compared to net realized and unrealized gain of $5.0 million last year.

Expenses

EFH's expenses consist of incurred claims, acquisition costs and operating expenses.

($ THOUSANDS)	Q4 2017	2017	2016
Incurred claims[1]	52,825	156,814	110,772
Acquisition expense	15,173	51,994	41,545
Operating expense [2]	8,116	31,031	29,157
	76,114	239,839	181,474

Selected Underwriting Ratios	Q4 2017	2017	2016
Incurred claims ratio[1]	81.4%	69.0%	61.2%
Acquisition expense ratio	23.4%	22.9%	22.9%
Operating expense ratio	12.4%	13.6%	16.1%
Combined ratio[1]	117.2%	105.5%	100.2%

[1] Before impact of change in discount rate decreasing unpaid claims by $3.3 million in 2017 and increasing unpaid claims by $2.8 million in 2016.

[2] Operating expenses do not include severance costs of $0.3 million in 2017, $4.3 million in 2016.

Incurred claims, also referred to as losses, are the amounts payable under insurance policies relating to insured events. Loss adjustment expenses, also referred to as claims expenses, are the expenses of settling claims, including allocated (i.e. external) loss adjustment expenses and unallocated (i.e. internal) loss adjustment expenses (together, LAE). Achieving profitable results depends on EFH's ability to manage future claims and other costs through innovative product design, strict underwriting criteria and efficient claims management.

Acquisition costs consist mainly of commissions and premium taxes which are directly related to the acquisition of premiums. Commissions are the amounts paid to producers for selling insurance policies. The amount of commission is generally a percentage of the premium of the insurance policy sold or renewed. Contingent commissions are paid to brokers and Managing General Agents (MGAs) on an annual basis if they meet certain targets. In general, these producers have to meet or exceed certain criteria, including written premium targets and profitability to qualify for this compensation. Premium taxes are paid by EFH to provincial governments, calculated as a percentage of direct written premiums.

Operating expenses are the non-commission selling, underwriting and administrative expenses incurred to support EFH's business. A significant portion of these expenses is related to employee compensation and benefits. The effective control and management of these expenses can enhance the underwriting results from the operation.

YEAR ENDED DECEMBER 31, 2017 COMPARED TO 2016

2017 Highlights

- Net operating income decreased by 94% to $0.05 per share from $0.86 per share.
- A combined operating ratio of 102% compared to 96% due to increased severity in Atlantic Auto and Motorcycle in addition to higher technology expenses in 2017. This was partially offset by stronger results in Ontario Auto.
- A 31% increase in direct written premium in 2017, primarily due to growth in Commercial Lines products launched in 2016 and organic growth in Personal Lines.
- Total pre-tax return of invested assets of $7.8 million comparable to $7.5 million in 2016 due to stronger preferred share and equity returns in 2017.

The following financial information compares results for the full year 2017 and 2016.

($ THOUSANDS except per share amounts)	2017	2016	$ Change	% Change
Direct written and assumed premiums	285,718	217,486	68,232	31
Net written premiums	266,807	199,601	67,206	34
Net earned premiums	227,396	181,060	46,336	26
Net claims incurred	156,814	110,772	46,042	42
Net acquisition costs	51,994	41,545	10,449	25
Operating expenses	31,031	29,156	1,875	6
Underwriting (loss)	(12,443)	(414)	(12,029)	(2,906)
Severance expense	(262)	(4,266)	4,004	94
Investment income	17,196	16,507	689	4
Impact of discount rate	3,254	(2,822)	6,076	215
Net income before interest expense and income taxes	7,745	9,005	(1,260)	(14)
Interest expense	155	217	(62)	(29)
Income taxes expense	947	1,670	(723)	(43)
Net income	6,643	7,118	(475)	(7)
Net income attributable to shareholders	6,489	6,606	(117)	(2)
Net operating income attributable to shareholders	613	10,354	(9,741)	(94)
Earnings per share				
Basic	$0.55	$0.56	$(0.01)	(2)
Diluted	$0.54	$0.55	$(0.01)	(2)
Net operating income per share – diluted (1)	$0.05	$0.86	$(0.81)	(94)
Trailing twelve month return on equity (ROE) - continuing operations (2)	4.6%	4.2%		

(1) Net operating income is defined as underwriting income plus interest and dividend income, net of tax. Underwriting income excludes impact of change in claims discount rates, and non-recurring items. Net investment income consists of interest income, dividend income and premium financing charges, less interest expense, as per Note 6 of the Company's Financial Statements. Net operating income is adjusted to that attributable to shareholders for per share calculation.

(2) ROE calculated on rolling twelve-month basis

Insurance Operations

Direct Written and Net Earned Premiums

Direct written premiums increased by 31%, while net earned premiums increased 26%. The increase in premium was driven by organic growth in Personal Lines and new Commercial Lines products launched in 2016.

Claims Incurred

Net claims expense increased by 42% due to increased severity in Atlantic auto, catastrophic losses from the British Columbia wild fires and increased Commercial Auto losses.

Net favourable development on prior year claims of $25.7 million was recorded in the year compared to $17.2 million in 2016. The favourable development arose from both the Personal Lines and Commercial Lines segments, with the majority (62%) arising from Ontario Auto within Personal Lines. $3.3 million of the aggregate development for the year related to a change in discount rate.

Acquisition Costs

Acquisition costs, which consist mainly of commissions, premium taxes and a portion of general expenses related to policy acquisitions, increased by 25% in line with the increase in net earned premiums.

Operating Expenses

Operating expenses increased $1.9 million or 6% to $31.0 million in 2017 compared to $29.2 million in the same period last year, primarily due to increased information technology and incremental headcount. The increase in operating expenses is lower than the growth rate of earned premiums, resulting in a decrease in the operating expense ratio.

Underwriting Income

Underwriting loss of $12.4 million was recorded in 2017 compared to an underwriting loss of $0.4 million in 2016. The underwriting loss was due to weak Personal Lines results.

Investment Income

Investment income increased by $0.7 million, to $17.2 million in 2017 compared to $16.5 million in 2016. Income from fair value changes on FVTPL investments of $3.5 million was comparable to an income of $3.9 million in the same period of 2016. The total fair value of the investment portfolio as at December 31, 2017, (including cash and short-term and premium financing receivables) was $469 million compared to $410 million as at December 31, 2016.

Net Income before Income Taxes

Income before taxes was $7.7 million in 2017, compared to $9.0 million in 2016, due to an increased underwriting loss and increase in discount rate on unpaid claims, which was offset by reduced severance expenses and slightly higher investment income.

Income Taxes

For the year ended December 31, 2017, the provision for income taxes reflects an expense of $0.9 million compared to an expense of $1.7 million for the same period last year. The approximate effective rate decreased to 13% for 2017 from 19% for the previous year.

BALANCE SHEET ANALYSIS

The Balance Sheet analysis that follows should be read in conjunction with the consolidated financial statements for the fourth quarter of 2017, and notes therein.

Balance Sheet Highlights

Selected balance sheet highlights and book value per share details are as follows:

($ THOUSANDS except per share amounts)	2017	2016	2015	2014	2013
Cash and short-term deposits	44,459	50,588	23,373	27,326	18,156
Investments	370,933	336,535	513,099	504,290	454,317
Total assets	590,586	800,219	923,795	740,299	619,928
Provision for unpaid claims	262,966	255,129	397,214	344,692	296,857
Unearned premiums	160,577	120,184	264,584	168,555	127,247
Total equity attributable to shareholders	142,822	137,414	180,935	183,616	172,360
Book value per share (1)	$12.01	$11.70	$15.75	$15.82	$14.57
MCT Ratio - Echelon Insurance	212%	237%	241%	211%	219%
- ICPEI	355%	340%	296%	229%	N/A

(1) Shareholders' equity divided by the number of shares issued and outstanding.

Investments

EFH has an investment policy that seeks to provide a stable income base to support EFH's liabilities in line with its risk appetite and tolerance. In addition to this risk-return analysis, the chosen asset mix also considers the amount of regulatory capital that is required.

EFH's investment portfolio is invested in well-established, active and liquid markets in Canada. Fair value for most investments is determined by reference to observable market data.

Fair Value of Investments

The following table sets forth EFH's invested assets as at December 31, 2017 and December 31, 2016.

($ Thousands)	Fair values			
Available-for-sale	As at December 31, 2017	% of Total	As at December 31, 2016	% of Total
Fixed income				
Canadian				
Federal	39,408		67,826	
Provincial	29,883		44,147	
Municipal	14		519	
Corporate	127,701		136,984	
	197,006		249,476	
Fixed income lent through securities lending program				
Federal	63,864		15,390	
Provincial	17,564		998	
Municipal	1,322		845	
Corporate	8,535		1,885	
	91,285		19,118	
Total fixed income	290,305	70%	268,594	69%
Commercial mortgages pooled funds	—		17,423	
Money market pooled funds	1,014		200	
Short-term fixed income and mortgage pooled funds	19,303		17,229	
Specialty pooled fund	8,240		—	
Total pooled funds	28,557	7%	34,852	9%
Common shares				
Canadian	889		312	
Foreign	8,428		—	
Total common shares	9,317	2%	312	—%
Total available-for-sale	328,179		303,758	
Fair value through profit or loss				
Preferred shares	42,754		32,678	
Preferred shares lent through securities lending program	—		99	
Total preferred shares	42,754	10%	32,777	8%
Total investments	370,933	89%	336,535	86%
Cash and short-term deposits	44,459	11%	50,588	14%
Total investments including cash and short-term deposits	415,392	100%	387,123	100%

Impairment Assets and Provisions for Losses

EFH has an established policy to write down or make a provision for any investment with objective evidence that the value of the investment is impaired.

There were no impairments recognized during the twelve months ended December 31, 2017 and 2016.

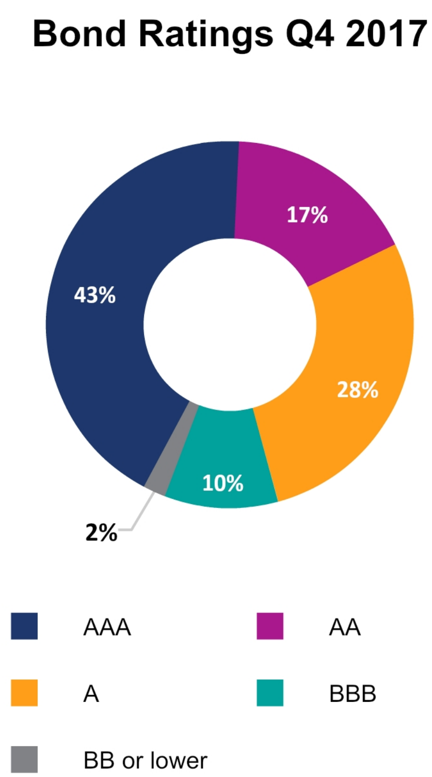
A gross unrealized loss of $3.3 million (December 31, 2016 – $1.7 million) on investments held as at December 31, 2017, is recorded, net of tax, in the amount of $2.4 million (December 31, 2016 – $1.2 million) in Accumulated Other Comprehensive Income. The Company has concluded, based on its review, that these fair value deficiencies do not meet the criteria for impairment and they will be monitored on an ongoing basis.

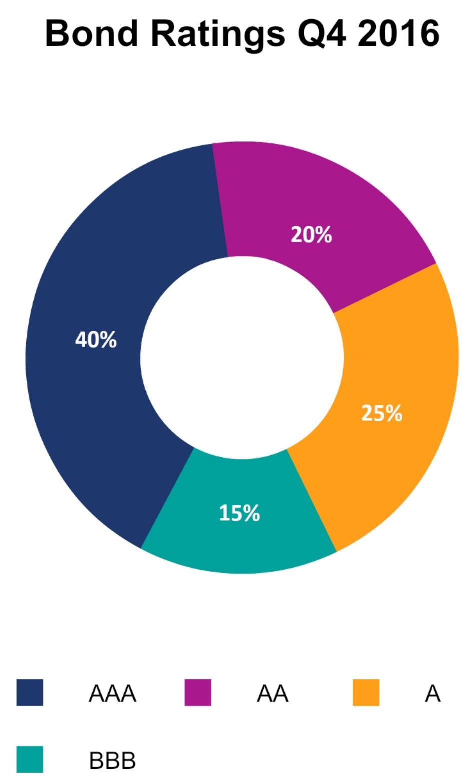
Fixed Income Securities

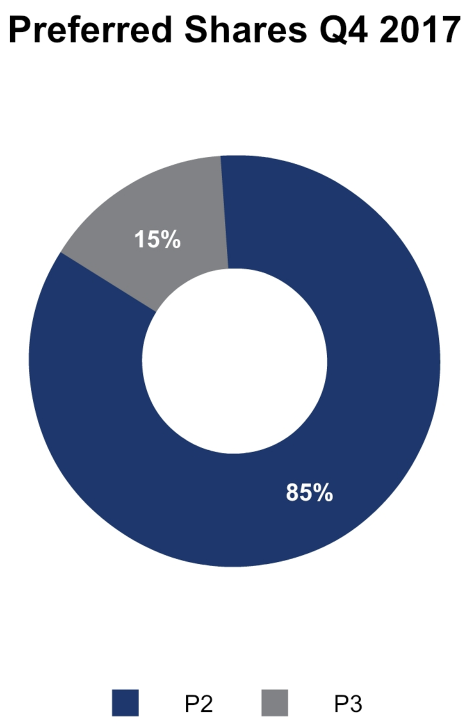
EFH holds fixed income securities to provide a steady, predictable level of income with reasonable liquidity and minimal risk of loss and a fixed sum at maturity. EFH's portfolio is diversified by selecting various types of government and corporate bonds. Constraints on types of issuers take liquidity, diversification and risk into account by limiting the portfolio mix by issuer.

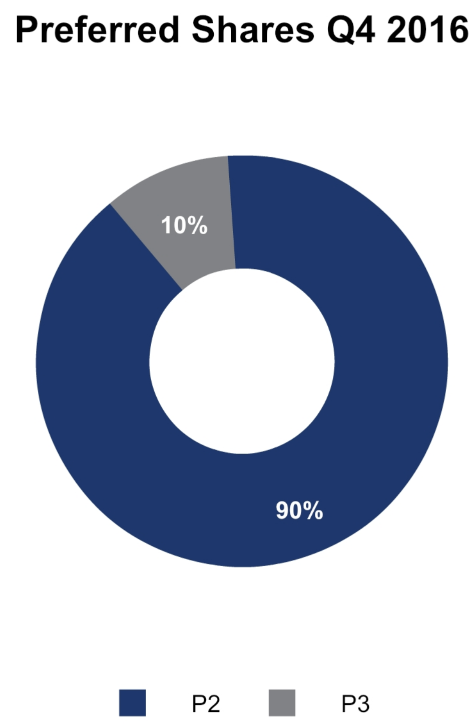
EFH's bond portfolio has a high overall credit quality with an average rating of AA. The preferred shares have an average rating of P2. The duration of the bond portfolio is 2.7 years.

The charts below show EFH's fixed income and preferred share portfolios by credit quality as at December 31, 2017 compared to December 31, 2016.









Sector Mix by Asset Class

The following table shows sector exposure by asset class as at December 31, 2017:

Sector	Fixed Income Securities & Pooled Funds [(1)]	Preferred Shares	Common Shares	Total
Government	51%	—%	—%	44%
Financial Services	26%	50%	17%	28%
Infrastructure	9%	—%	—%	8%
Industrial Products	4%	13%	18%	5%
Utilities	—%	31%	1%	4%
Energy	3%	—%	1%	3%
Pipelines	2%	6%	—%	2%
Telecommunication	2%	—%	4%	2%
Consumer Discretionary	—%	—%	32%	1%
Technology	—%	—%	17%	—%
Other	3%	—%	10%	3%
Total	100%	100%	100%	100%
Total	$317,699	$42,754	$9,317	$369,770

(1) Fixed income securities and pooled funds do not include any cash being carried by the pooled funds, $1.2 million as at December 31, 2017.

Common Share Portfolio

As at December 31, 2017, 10% of the common share portfolio was invested in Canadian equities.

Recoverable from Reinsurers

($ THOUSANDS)	As at December 31, 2017	As at December 31, 2016
Reinsurers' share of unpaid claims	23,471	27,023
Reinsurers' share of unearned premiums	9,957	8,975
Total	33,428	35,998

As at December 31, 2017, the recoverable from reinsurers decreased by $2.6 million, or 7%, to $33.4 million from $36.0 million as at December 31, 2016. The increase in reinsurers share of unearned premium was due to growth while the decrease in reinsurers share of unpaid claims was due to an increase in the Company's retention on large claims in recent years. All reinsurers, with balances due, have a rating of A– or above as determined by Standard & Poor's and A.M. Best, except for several Specialty Programs distributors who share a portion of the risk with EFH, for whom the Company holds deposits as collateral.

Accounts Receivable

($ THOUSANDS)	As at December 31, 2017	As at December 31, 2016
Premium financing receivables	53,538	32,216
Agents and brokers	17,215	9,787
Other	4,869	4,702
Total	75,622	46,705

Premium financing receivables represent 71% of total receivables as at December 31, 2017. Premium financing receivables increased to $53.5 million at December 31, 2017, from $32.2 million at December 31, 2016, due to the growth in direct bill premiums. Agent and broker receivables increased from $9.8 million in 2016 to $17.2 million in 2017 due to growth in broker billed premiums.

Provision for Unpaid Claims

EFH establishes loss reserves to provide for future amounts required to pay claims related to insured events that have occurred and been reported but have not yet been settled, and related to events that have occurred but have not yet been reported to EFH. Provision for unpaid claims consists of the aggregate amount of individual case reserves established and management's estimate of claims incurred but not reported, based on the volume of business currently in force and historical claims experience and are determined by EFH's appointed actuary. Provisions for unpaid claims are discounted to present value. 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 investment portfolio has experienced an increase in yields compared to December 31, 2016. The discount rates used for December 31, 2017, and 2016 for the following entities are below:

Entity	As at December 31, 2017	As at December 31, 2016
Echelon Insurance	2.65%	1.90%
ICPEI	2.80%	1.75%

Share Capital

As of February 15, 2018, there were 11,891,076 common shares issued and outstanding.

LIQUIDITY AND CAPITAL MANAGEMENT

The purpose of liquidity management is to ensure there is sufficient cash to meet all of EFH's financial commitments and obligations as they come due. EFH believes that it has the flexibility to obtain, from internal sources, the funds needed to fulfill its cash requirements, during the following financial year and to satisfy regulatory capital requirements.

Contractual obligations include operating leases, for which $1.8 million is due in less than a year and $9.1 million is due over the next eight years.

EFH is primarily a holding company and, as such, has limited direct operations of its own. EFH's principal assets are the shares of its insurance and reinsurance subsidiaries. Accordingly, its future cash flows depend in part upon the availability of dividends and other statutorily permissible distributions from its insurance subsidiaries. The ability to pay such dividends and to make such other distributions is limited by applicable laws and regulations of the jurisdictions in which the insurance subsidiaries are domiciled, which subject the insurance subsidiaries to significant regulatory restrictions. These laws and regulations require, among other things, that the insurance subsidiaries maintain minimum solvency requirements and may also limit the amount of dividends that the insurance subsidiaries can pay to EFH.

Capital Management

The total capitalization of EFH at December 31, 2017, was $146.7 million compared to $141.4 million at December 31, 2016.

The Minimum Capital Test (MCT) ratio of the Company's subsidiary, Echelon Insurance, as at December 31, 2017, was 212%, which comfortably exceeds the supervisory regulatory capital level required by the Office of the Superintendent of Financial Institutions (OSFI). ICPEI's MCT ratio of 355% was in excess of provincial supervisory targets. As at December 31, 2017, the Company has approximately $29 million of excess deployable capital invested in equities and liquid assets in the holding company.

Normal Course Issuer Bid (NCIB)

No shares were repurchased in 2017. However, in the comparative period of 2016 there were 51,000 common shares repurchased and canceled at an average cost of $13.24 per share for a total consideration of $0.7 million.

YEAR ENDED DECEMBER 31, 2016 COMPARED TO 2015

The following chart compares results for the full year 2016 and 2015**:**

($ THOUSANDS except per share amounts)	2016	2015	$ Variance	% Variance
Direct written and assumed premiums	217,486	199,473	18,013	9 %
Net written premiums	199,601	180,336	19,265	11 %
Net earned premiums	181,060	176,468	4,592	3 %
Net claims incurred	110,772	109,827	945	1 %
Net acquisition costs	41,545	39,448	2,097	5 %
Operating expenses	29,156	27,639	1,517	5 %
Underwriting income (loss)	(414)	(447)	33	7 %
Severance	(4,266)	—	(4,266)	NA
Investment income	16,507	12,613	3,894	31 %
Impact of discount rate – increase in claims	(2,822)	1,024	(3,846)	(376)%
Other income	—	748	(748)	(100)%
Net income before income taxes	9,005	13,938	(4,933)	(35)%
Interest Expense	217	—	217	NA
Income taxes expense	1,670	1,676	(6)	0 %
Net income	7,118	12,262	(5,144)	(42)%
Net income attributable to shareholders	6,606	12,254	(5,648)	(46)%
Net operating income attributable to shareholders	10,354	9,922	432	4 %
Earnings per share				
Basic	$0.56	$1.05	$(0.49)	(47)%
Diluted	$0.55	$1.02	$(0.47)	(46)%
Net operating income per share – diluted [(1)]	$0.86	$0.83	$0.03	4 %
Trailing twelve month return on equity (ROE) [(2)]	4.2%	6.7%		

(1) Net operating income is defined as underwriting income plus interest and dividend income, net of tax. Underwriting income excludes impact of change in claims discount rates, and non-recurring items. Net investment income consists of interest income, dividend income and premium financing charges, less interest expense, as per Note 6 of the Company's Financial Statements. Net operating income is adjusted to that attributable to shareholders for per share calculation.

(2) ROE calculated on rolling twelve-month basis

5 YEAR FINANCIAL HIGHLIGHTS

	Year ended December 31				
($ THOUSANDS EXCEPT PER SHARE AMOUNTS)	**2017**	**2016**	**2015**	**2014**	**2013**
Revenue					
Direct written and assumed premiums					
Personal Lines	189,454	154,992	146,578	133,275	134,902
Commercial Lines	96,264	62,494	52,895	54,069	39,702
Total direct written premiums	285,718	217,486	199,473	187,344	174,604
Net written premiums	266,807	199,601	180,336	171,396	157,117
Net earned premiums	227,396	181,060	176,468	167,517	154,137
Underwriting expenses					
Incurred claims	156,814	110,772	109,827	92,966	101,363
Acquisition costs	51,994	41,545	39,448	40,824	36,799
Operating expenses	31,031	29,156	27,639	25,621	18,955
Total underwriting expense	239,839	181,474	176,915	159,411	157,117
Underwriting income (loss)	(12,443)	(414)	(447)	8,106	(2,980)
Impact of discount rate on claims	3,254	(2,822)	1,024	(2,391)	207
ICPEI Integration Cost	—	—	—	(1,347)	—
Severance expense	(262)	(4,266)	—	(1,166)	—
Investment income	17,196	16,507	12,613	22,019	17,474
Other income	—	—	748	—	—
Income before interest expense and income taxes	7,745	9,005	13,938	25,221	14,701
Interest expense	155	217	—	—	—
Income tax expense (recovery)					
Current	921	1,738	1,555	5,300	4,129
Deferred	26	(68)	121	209	(895)
	947	1,670	1,676	5,509	3,234
Net income on continued operations	6,643	7,118	12,262	19,712	11,467
Net income (loss) on discontinued operations attributable to shareholders of the Company	(4,855)	(36,646)	(5,677)	(980)	(7,742)
Net income	1,788	(29,528)	6,585	18,732	3,725
Attributed to:					
Shareholders of the Company	6,489	6,606	12,254	18,722	4,681
Non-controlling interest	154	512	8	10	(956)
	6,643	7,118	12,262	18,732	3,725
Earnings per share attributable to shareholders of the Company:					
Net income per share continued operations basic	$0.55	$0.56	$1.05	$1.72	$0.97
Net income per share continued operations diluted	$0.54	$0.55	$1.02	$1.67	$0.95
Book value per share	$12.01	$11.70	$15.75	$15.82	$14.57
Net operating income [1]	613	10,354	9,922	15,753	7,569
Net operating income per share - diluted [2]	$0.05	$0.86	$0.83	$1.31	$0.63

[1] Net operating income is defined as underwriting income plus interest and dividend income, net of tax. Net operating income is adjusted to that attributable to shareholders for per share calculation.

[2] Net operating income is adjusted to that attributable to shareholders for per share calculation.

OUTLOOK

EFH's long-term target is to deliver a minimum 12% after tax return on shareholder's equity and a 95% combined ratio on its underwriting operations. The Company has made significant progress in the past year focusing on its core business in Canada, building a strong management team, focusing on broker relationships and improved technology. The overarching goal is to create a broker focused insurance operation that offers a wide suite of profitable and sustainable insurance solutions, aligned directly to the brokers needs.

In 2018, we will continue execution on the strategy outlined below with a focus on underwriting profitability and maximizing our return on equity. We have a strong balance sheet that will provide us with a solid launching pad for 2018 and beyond.

STRATEGY

EFH's purpose is to bring piece of mind to individuals and businesses by protecting their assets. To do this, the company provides a range of insurance solutions that meet the evolving needs of our broker partners. EFH is committed to doing so while operating responsibly and ethically, and delivering strong underwriting results and return on shareholders' equity.

EFH's products are distributed exclusively through insurance brokers and agents. With a growing number of insurers selling directly to consumers, EFH's commitment to the broker channel differentiates Echelon Insurance and ICPEI from competitors and forms a foundation for mutually beneficial relationships. On this commitment, the Company has built and maintained an effective network of distribution partners by:

Focus on Canada Offering Diverse Products that Satisfy Unmet Needs

The bulk of EFH's products were designed to respond to the unmet needs of our distribution partners.

Echelon Insurance has excelled in the non-standard auto market by delivering expertly underwritten coverage for hard to insure drivers. ICPEI's nuanced understanding of Maritime families and businesses has shaped the products and coverages that meet the unique needs of Atlantic Canadians. Now, Echelon Insurance has identified new areas where brokers are unsatisfied with existing products and service, and is responding by launching Surety and Commercial Auto solutions.

Investing in Talent and Leveraging Relationships

EFH's management and underwriting teams have the skillsets to understand and effectively underwrite risks. Echelon Insurance and ICPEI benefit from this seasoned expertise, but also from employee reputations and long-standing relationships in their industries. With the addition of Commercial Automobile and Surety teams in 2016, EFH gained a number of new broker relationships.

Improving Technology and Connectivity

EFH is committed to investing in technology to connect more seamlessly with its brokers and agents. In 2014, The Company acquired and launched a new policy management system that will be instrumental in streamlining how brokers and agents write business with Echelon Insurance. It has rolled out this system across Canada, and is working towards consolidating its systems into this sole policy management system to simplify broker system interactions.

The type and number of distributors that EFH partners with varies by business line. Property and Automobile products are marketed through a broad network of insurance brokers and agents across Canada. These distributors have both the expertise to underwrite good risks, and the volume of premium to support good loss ratios in these business lines.

LINES OF BUSINESS

PERSONAL LINES

EFH offers standard and specialty private passenger vehicle coverage in the Maritime provinces through ICPEI, and non-standard and specialty private passenger vehicle coverage across the rest of Canada through Echelon Insurance.

In addition to automobile products which form the bulk of EFH's Personal Lines business, Property coverage is offered in select provinces.

PERSONAL AUTOMOBILE

Non-standard Automobile insurance is the largest single component of EFH's business, with approximately $130 million in direct premiums written over the 12 months ended December 31, 2017. Offered through Echelon Insurance, the non-standard automobile product targets drivers of private passenger and single commercial vehicles who are unable to obtain coverage from standard insurers.

The Company provides coverage for specialty automobiles and recreational vehicles through both Echelon Insurance and ICPEI. Coverage is available for motorcycles, antique and classic cars, trailers, motorhomes, snowmobiles and all-terrain vehicles. Standard Personal and Commercial Automobile insurance is offered across the Maritimes through ICPEI only.

Moving forward, the Company intends to increase focus on profitable automobile products, evaluating whether these could be successfully expanded into new regional markets within Canada.

PERSONAL PROPERTY

The Company offers homeowners, condo and tenant packages through ICPEI in the Maritimes and through Echelon Insurance in Quebec and British Columbia.

COMMERCIAL LINES

The Company writes Commercial Property, Liability and Automobile coverage for small- to mid-sized businesses under the Echelon Insurance and ICPEI brands.

In addition to standard commercial policies, Echelon Insurance also excels in niche business lines, including Surety, Commercial Automobile, and Specialty Programs. Since 2016, the Company has grown its Commercial Lines Management and underwriting teams to include seasoned experts with proven track-records and deep networks in their respective markets. Commercial Lines represents $96 million, and 34% of the Company's business.

With a now-profitable portfolio and an experienced and connected management team, steps are underway to expand the Company's commercial product offering into Ontario, Quebec and Alberta. Echelon Insurance will target underserved and specialty brokers, offering flexible, risk-underwritten coverage.

COMMERCIAL PROPERTY & CASUALTY

EFH offers Commercial Property coverage in the Maritimes, Quebec and British Columbia, differentiating from competitors by applying risk vs. class underwriting. Simple, low-touch packages target small to mid-sized businesses like contractors and professional service providers. Coverages can be customized to meet the more unique needs of larger businesses.

COMMERCIAL AUTOMOBILE

The Company offers Commercial Automobile coverage through Echelon Insurance in Alberta, Ontario and Quebec, and through ICPEI in the Maritimes. Coverage is available for single vehicles, cargo trailers, fleets, and owner operators. Packaged policies are also offered to fleets and owner operators, and can be customized to include Commercial Automobile, Motor Truck Cargo Liability, Commercial General Liability, and Garage coverages, as well as special endorsements.

SPECIALTY PROGRAMS

EFH partners with MGAs across Canada to underwrite a range of specialty and warranty programs including new home and home system warranties. In 2018, EFH will continue to grow its warranty programs by building deeper expertise and operational infrastructure in home, product and equipment warranty.

SURETY

In 2016, Echelon Insurance introduced a Surety division to meet growing demand for mid-market surety bonds. Echelon Insurance focuses on distributing contract and commercial bonds through the broker channel. Unlike an insurance product, a surety bond is a guarantee issued to minimize the risk of a contractor's financial failure and inability to complete a construction project.

ORGANIZATIONAL STRATEGIES

EFH's key to profitable growth is personalized service and sophisticated pricing, underwriting and claims management. EFH will invest in its business and its people. It will continue to develop a sophisticated and scalable operational platform to grow. EFH will continue to invest aggressively in technology, with a focus on service and financial analytics.

COMPETITIVE STRENGTHS

EFH believes that it is uniquely positioned to deliver peace of mind to our customers by being a meaningful and committed partner to Canadian brokers for the following reasons:

Wide range of products and underwriting expertise

EFH offers its distributors a comprehensive line of personal and commercial insurance products, enabling them to meet the varying needs of their clients. Our underwriting teams are experienced and specialized, allowing EFH to effectively assess risks that don't fit the fully-automated processes of larger, standard insurers.

Entrepreneurial culture

EFH fosters a responsive, team environment which encourages experimentation and allows the flexibility to provide unique, tailor-made solutions. The Company's values are collaborative, dynamic, respectful and focused.

Commitment to the broker channel

EFH's products are distributed exclusively through the broker channel. The Company believes that the insurance needs of Canadian individuals and businesses are best served by independent insurance brokers, who can ensure that they have the right insurance protection in place.

Financial strength

EFH has a strong capital base with shareholder equity of $142.8 million. The Minimum Capital Test (MCT) ratio of Echelon Insurance as at December 31, 2017, was 212% comfortably in excess of the Office of the Superintendent of Financial Institutions' (OSFI) supervisory target. In addition to any excess capital at Echelon, the Company has approximately $29 million of excess deployable capital invested in liquid assets in the holding company as at December 31, 2017.

It has a high quality investment portfolio with 100% of its fixed income portfolio in investment grade, 88% rated A and above and the average rating of the fixed income portfolio is AA. It has no debt on its balance sheet, little goodwill and intangible assets consisting mostly of computer software. Echelon has an A.M. Best financial strength rating of B++ (Good). EFH intends to maintain its strong balance sheet through appropriate pricing, underwriting discipline, conservative accounting and loss reserving practices.

RISK FACTORS

Careful consideration should be given to the following factors, which must be read in conjunction with the detailed information appearing elsewhere in this report. Any of the matters highlighted in these risk factors could have a material adverse effect on EFH's results of operations, business prospects or financial condition.

Nature of the Industry

The P&C insurance business in Canada is affected by many factors which can cause fluctuations in the results of operations of EFH. Many of these factors are beyond EFH's control. An economic downturn in those jurisdictions in which EFH writes business could result in less demand for insurance and lower policy amounts. As a P&C insurance company, EFH is subject to claims arising out of catastrophes, which may have a significant impact on its results of operations and financial condition. These factors, together with the industry's historically cyclical competitive pricing, could result in fluctuations in the underwriting results and net income of EFH. A significant portion of the earnings of insurance companies is derived from the income from their investment portfolios. EFH's investment income will fluctuate depending on the returns and values of securities in its investment portfolio.

Regulation

EFH is subject to the laws and regulations of the jurisdictions in which it carries on business. These laws and regulations cover many aspects of its business, including premium rates for automobile insurance; the assets in which it may invest; the levels of capital and surplus and the standards of solvency that it must maintain; and the amount of dividends which it may declare and pay.

Changes to laws or regulations are impossible to predict and could materially adversely affect EFH's business, results of operations and financial condition. Should OSFI be concerned about an unsafe course of conduct or an unsound practice in conducting the business of a federally regulated insurance company, OSFI may direct the insurance company to refrain from a course of action or to perform acts necessary to remedy the situation. In certain circumstances, OSFI may take control of the assets of an insurance company or take control of the company itself. More restrictive laws, rules or regulations may be adopted in the future that could make compliance more difficult and/or expensive. Specifically, recently adopted legislation addressing privacy issues, among other matters, is expected to lead to additional regulation of the insurance industry in the coming years, which could result in increased expenses or restrictions on EFH's operations.

Competition

The P&C insurance business is highly competitive with pricing being a primary means of competition. Other elements of competition include availability and quality of products, quality and speed of service, financial strength, distribution systems and technical expertise.

EFH competes with many other insurance companies. Certain of these competitors are larger and have greater financial resources than EFH has. In addition, certain competitors have from time to time decreased their prices in an apparent attempt to gain market share.

As competitors introduce new products and as new competitors enter the market, the Company and its insurance subsidiaries may encounter additional and more intense competition. There can be no assurance that EFH will continue to increase revenues or be profitable. To a large degree, future revenues of EFH are dependent upon its ability to continue to develop and market its products and to enhance the capabilities of its products to meet changes in customer needs.

Cyclicality

Historically, the results of companies in the P&C insurance industry have been subject to significant fluctuations and uncertainties. The profitability of P&C insurers can be affected significantly by many factors, including regulatory regimes, developing trends in tort and class action litigation, adoption of consumer initiatives regarding rates or claims handling procedures, and privacy and consumer protection laws that prevent insurers from assessing risk, or factors that have a high correlation with risks considered, such as credit scoring.

The financial performance of the P&C insurance industry has historically tended to fluctuate in cyclical patterns of “soft” markets characterized generally by increased competition, resulting in lower premium rates and underwriting standards, followed by “hard” markets characterized generally by lessening competition, stricter underwriting standards and increasing premium rates. EFH’s profitability tends to follow this cyclical market pattern with profitability generally increasing in hard markets and decreasing in soft markets. These fluctuations in demand and competition could produce underwriting results that would have a negative impact on EFH’s results of operations and financial condition.

Unpredictable Catastrophic Events

Catastrophes can be caused by various natural and unnatural events. Natural catastrophic events include hurricanes, windstorms, earthquakes, hailstorms, explosions, severe winter weather and fires. Unnatural catastrophic events include hostilities, terrorist acts, riots, crashes and derailments. The incidence and severity of catastrophes are inherently unpredictable. The extent of losses from a catastrophe is a function of both the total amount of insured exposure in the area affected by the event and the severity of the event. Most catastrophes are restricted to small geographic areas; however, hurricanes, windstorms and earthquakes may produce significant damage in large, heavily populated areas. Catastrophes can cause losses in a variety of P&C insurance lines. Claims resulting from natural or unnatural catastrophic events could cause substantial volatility in EFH’s financial results for any fiscal quarter or year and could materially reduce EFH’s profitability or harm EFH’s financial condition. EFH’s ability to write new business also could be affected. EFH may experience an abrupt interruption of activities caused by unforeseeable and/or catastrophic events. EFH’s operations may be subject to losses resulting from such disruptions. Losses can relate to property, financial assets, trading positions and also to key personnel. If EFH’s business continuity plans cannot be put into action or do not take such events into account, losses may further increase.

Interest Rates

An increase in interest rates may result in lower values for EFH’s bond portfolio and increased costs of borrowing for EFH on future debt instruments, preferred shares or credit facilities. Such increased costs would negatively affect EFH’s operating results.

Negative Publicity in the Industry

EFH’s products and services are ultimately distributed to individual consumers. From time to time, consumer advocacy groups or the media may focus attention on EFH’s products and services, thereby subjecting its industry to periodic negative publicity. EFH also may be negatively impacted if its industry engages in practices resulting in increased public attention to its business. Negative publicity may also result in increased regulation and legislative scrutiny of practices in the P&C insurance industry as well as increased litigation. Such consequences may increase EFH's costs of doing business and adversely affect EFH's profitability by impeding its ability to market its products and services or increasing the regulatory burdens under which EFH operates.

Reliance on Brokers

EFH distributes its products primarily through a network of brokers. These brokers sell EFH's competitors' products and may stop selling EFH products altogether. Strong competition exists among insurers for brokers with demonstrated ability to sell insurance products. Premium volume and profitability could be materially adversely affected if there is a material decrease in the number of brokers that choose to sell EFH products.

Product and Pricing

EFH prices its products taking into account numerous factors, including claims frequency and severity trends, product line expense ratios, special risk factors, the capital required to support the product line, and the investment income earned on that capital. EFH's pricing process is designed to ensure an appropriate return on capital and long-term rate stability, avoiding wide fluctuations in rate unless necessary. These factors are reviewed and adjusted periodically to ensure they reflect the current environment.

However, pricing for automobile insurance must be submitted to each provincial government regulator and in certain Provinces pre-approved by the regulator. It is possible that, in spite of EFH's best efforts, regulator decisions may impede automobile rate increases or other actions that EFH may wish to take. Also, during periods of intense competition for any product line to gain market share, EFH's competitors may price their products below the rates EFH considers acceptable. Although EFH may adjust its pricing up or down to maintain EFH's competitive position, EFH strives to ensure its pricing will produce an appropriate return on invested capital. There is no assurance that EFH will not lose market share during periods of intense pricing competition.

Underwriting and Claims

EFH is exposed to losses resulting from the underwriting of risks being insured and the exposure to financial loss resulting from greater than anticipated adjudication, settlement and claims costs. EFH's success depends upon its ability to accurately assess the risks associated with the insurance policies that EFH writes.

EFH's underwriting objectives are to develop business within EFH's target markets on a prudent and diversified basis and to achieve profitable underwriting results (i.e. a combined operating ratio below 100%). There can be no assurances that EFH will properly assess the risks associated with the insurance policies that it writes and may, therefore, experience increased adjudication, settlement and claims costs.

Loss Reserves and Claims Management

The amounts established and to be established by EFH for loss and loss adjustment expense reserves are estimates of future costs based on various assumptions, including actuarial projections of the cost of settlement and the administration of claims, estimates of future trends in claims severity and frequency, and the level of insurance fraud. Most or all of these factors are not directly quantifiable, particularly on a prospective basis, and the effects of these, and unforeseen factors could negatively impact EFH's ability to accurately assess the risks of the policies that it writes. In addition, future adjustments to loss reserves and loss adjustment expenses that are unanticipated by management could have an adverse impact upon the financial condition and results of operations of EFH. Although EFH's management believes its overall reserve levels as at December 31, 2017, are adequate to meet its obligations under existing policies, actual losses may deviate, perhaps substantially, from the reserves reflected in EFH's financial statements. To the extent reserves prove to be inadequate, EFH would have to increase such reserves and incur a charge to earnings.

Errors and Omissions Claims

Where the Company acts as a licensed insurance agency, it is subject to claims and litigation in the ordinary course of business resulting from alleged errors and omissions in placing insurance. The placement of insurance and the handling of claims involve substantial amounts of money. Since errors and omissions claims against the Company may allege the Company's potential liability for all or part of the amounts in question, claimants may seek large damage awards and these claims can involve significant defense costs. Errors and omissions could include, for example, the Company’s employees or sub-agents failing, whether negligently or intentionally, to place coverage or file claims on behalf of customers, to appropriately and adequately disclose insurer fee arrangements to its customers, to provide insurance providers with complete and accurate information relating to the risks being insured or to appropriately apply funds that it holds for its customers on a fiduciary basis. It is not always possible to prevent or detect errors and omissions, and the precautions the Company takes may not be effective in all cases.

EFH’s business, financial condition and/or results may be negatively affected if its errors and omissions insurance coverage proves to be inadequate or unavailable. In addition, errors and omissions claims may harm EFH’s reputation or divert management resources away from operating the business.

The Company maintains liability insurance covering errors or omissions that may occur while acting in its role as an insurance consultant. This coverage has an aggregate limit of liability of $2 million.

Investments

EFH’s investment assets are exposed to any combination of risks related to interest rates, foreign exchange rates and changing market values.

EFH’s investment portfolio consists of diversified investments in fixed-income securities and preferred and common stocks. Investment returns and market values of investments fluctuate from time to time. A decline in returns could reduce the overall profitability of EFH. A change in interest rates, market values or foreign exchange rates may affect Echelon’s regulatory strength tests.

Reinsurance

Consistent with industry practice, EFH utilizes reinsurance to manage its claims exposure and diversifies its business by types of insurance and geographic area. The availability and cost of reinsurance are subject to prevailing market conditions that are generally beyond the control of EFH and may affect EFH’s level of business and profitability. There can be no assurance that developments may not occur in the future which might cause a shortage of reinsurance capacity in those classes of business which EFH underwrites, which could result in the curtailment of issuing of policies in a certain line of business or containing limits above a certain size.

Reinsurer Credit Risk

EFH’s reinsurance arrangements are with a limited number of reinsurers. This reinsurance may cause an adverse effect on EFH’s results of operations if one or more of its reinsurers are unable to meet its financial obligations. Although all of its reinsurers were rated A or higher by A.M. Best at the time of entering into the reinsurance arrangements, these ratings are subject to change and may be lowered.

Although reinsurance makes the assuming reinsurers liable to EFH to the extent of the risk each reinsurer assumes, EFH is not relieved of its primary liability to its insureds as the direct insurer. As a result, EFH bears credit risk with respect to its reinsurers. EFH cannot ensure that its reinsurers will pay all reinsurance claims on a timely basis or at all. EFH evaluates each reinsurance claim based on the facts of the case, historical experience with the reinsurer on similar claims, and existing law and includes in its reserve for uncollectible reinsurance any amounts deemed uncollectible. The inability to collect amounts due to EFH under reinsurance arrangements would reduce EFH’s net income and cash flow.

Technology and Cyber Security Risk

EFH is heavily dependent on systems technology to process large volumes of transactions and there would be a risk if the technology employed is inadequate or inappropriate to support current and future business needs and objectives. EFH continues to implement new computer applications as part of a comprehensive approach to improve systems technology. EFH regularly tests and improves its Disaster Recovery and Business Continuity Plan to protect itself, its producers and policyholders in the event of a technology failure; however, there is no assurance that EFH will be able to respond to technology failures effectively and with minimal disruption.

The threat of Cyber attacks is a major Infrastructure Risk. As with all financial services, EFH faces continual challenges to protect its data and customer information. These attacks can come through hacking security controls and identity theft, including installing ransomware technology within our network. To ensure the Company is protected from these attacks EFH has implemented cyber security programs to respond and manage through immediate detection of such threats, using sound best practices software and notification technologies.

Liquidity

EFH manages its cash and liquid assets in an effort to ensure there is sufficient cash to meet all of EFH's financial obligations as they fall due. As a federally regulated insurance company, Echelon is required to maintain an asset base comprised of liquid securities that can be used to satisfy its ongoing commitments. EFH believes that internally-generated funds provide the financial flexibility needed to fulfill cash commitments on an ongoing basis. EFH has no material commitments for capital expenditures; however, there can be no assurances that EFH's cash on hand and liquid assets will be sufficient to meet any future obligations that may come due.

Future Capital Requirements

EFH's future capital requirements will depend upon many factors, including the expansion of EFH's sales and marketing efforts and the status of competition. There can be no assurance that financing will be available to EFH on acceptable terms, or at all. If additional funds are raised by issuing equity securities, further dilution to the existing stockholders will result. If adequate funds are not available, EFH may be required to delay, scale back or eliminate its programs. Accordingly, the inability to obtain such financing could have a material adverse effect on EFH's business, financial condition and results of operations.

Risk Management

EFH has developed a comprehensive process of risk management and internal control which emphasizes the proactive identification of risks facing the organization and the effective management and control of these risks. The foundation of the process is an ongoing thorough operational analysis by senior management committees and a structured oversight process undertaken by the Board of Directors and appointed committees. Underlying this structure are internal control procedures which are designed to safeguard EFH's assets and protect the organization and its stakeholders from potential risk.

As a provider of insurance products, effective risk management is fundamental to EFH's ability to protect the interests of EFH's customers and shareholders. The Company is exposed to risks of loss pertaining to insurance products. EFH is exposed to potential loss from various market risks, including interest rate and equity market fluctuation risk, credit risk, liquidity risk and, to a lesser extent, foreign currency risk.

Market Risk

Market risk is the risk of loss arising from adverse changes in market rates and prices, such as interest rates, foreign currency exchange rates, and other relevant market rate or price changes. Market risk is directly influenced by the volatility and liquidity in the markets in which the related underlying assets are traded. This risk is mitigated by matching liabilities and assets.

The primary market risk to the investment portfolio is the interest rate risk associated with investments in fixed income securities. EFH’s exposure to unhedged foreign exchange risk is not significant. The investment policy is capital efficient and minimizes interest rate mismatch risk. Management does not currently anticipate significant changes in EFH’s primary market risk exposures or in how those exposures are managed in future reporting periods based upon what is known or expected to be in effect in future reporting periods.

Interest Rate and Equity Market Fluctuation

Movements in short and long-term interest rates, as well as fluctuations in the value of equity securities, affect the level and timing of recognition of gains and losses on securities that EFH holds, and cause changes in realized and unrealized gains and losses. Generally, EFH's investment income will be reduced during sustained periods of lower interest rates as higher yielding fixed income securities are called, mature, or are sold and the proceeds are reinvested at lower rates. During periods of rising interest rates, the market value of EFH’s existing fixed income securities will generally decrease and the realized gains on fixed income securities will likely be reduced. These will be partially offset by changes on the Company’s discounted actuarial liabilities. General economic conditions, political conditions and many other factors can also adversely affect the stock markets and, consequently, the value of the equity securities EFH owns.

Credit Risk

Credit risk is the possibility that counterparties may not be able to meet payment obligations when they become due. The credit risk exposure is concentrated primarily in the fixed income and preferred share investment portfolios and, to a lesser extent, in reinsurance recoverables.

EFH’s risk management strategy and investment policy is to invest in debt instruments of high credit quality issuers and to limit the amount of credit exposure with respect to any one issuer. The Company attempts to limit its credit exposure by imposing fixed income portfolio limits on individual corporate issuers based upon credit quality (see “Investments” – “Fixed Income Securities” and “Reinsurance” sections).

Foreign Exchange Risk

Foreign exchange risk is the possibility that changes in exchange rates may produce an unintended effect on earnings and equity when measured in domestic currency.

EFH is exposed to foreign exchange risk on its receivable from the sale of its International segment’s operations in Europe. The Company has entered into derivative contract with a major Canadian bank to hedge the principal repayment from the loan receivable from New Nordic Odin Guernsey Limited. The total notional value of the derivative contracts is $6.6 million.

CORPORATE GOVERNANCE

Active oversight remains a priority for the Board of Directors. The board is directly involved, through its committees, in overseeing all aspects of EFH’s operation. The objective of the board is to meet or exceed best practices in corporate governance. There is independent oversight from the board and the respective committees to key corporate functions such as financial reporting, compliance, risk assessment and management, as well as human resources and succession planning.

EFH’s Board of Directors has established the following committees to ensure that risks are effectively identified, monitored, controlled and reported on:

Audit and Risk Committee*:* The Audit and Risk Committee reviews all financial information, monitors internal controls and provides oversight of management’s risk-control processes, specifically focusing on financial related risks. Echelon also has an Audit and Risk Committee of its directors in accordance with the requirements of the Insurance Companies Act (Canada).

Governance Committee*:* The Governance Committee is responsible for director nominations, monitoring related party transactions, officer compensation, benefit plans and the monitoring of regulatory compliance and market conduct programs put in place by management to ensure their effectiveness.

Investment Committee*:* The Investment Committee ensures that risks associated with the investment of corporate and policyholder funds are effectively managed to accomplish EFH's investment objectives of prudent, conservative management of funds and compliance with regulatory restrictions while achieving competitive rates of return.

In addition to these board committees, management has formed a number of working committees which have been assigned the responsibility of identifying and managing specific corporate risks, including (i) underwriting and claims committees to manage the risks associated with the development and pricing of EFH's products, claims adjudication and reserving; (ii) a technology committee and a system prioritization committee to ensure the prioritization and implementation of effective technology solutions; (iii) an Enterprise Risk Management committee to instill a consistent approach to risk management and appropriate processes and procedures are in place to ensure compliance with all applicable regulatory requirements (iv) a Reinsurance committee that works closely with EFH's reinsurance brokers to ensure that effective reinsurance programs are in place that provide EFH with protection against the occurrence of significant and unusual claims risk and development.

EFH has established a Disaster Recovery Plan and a Business Continuity Plan with the objectives of protecting critical Company information and infrastructure and resuming business operations in a timely effective manner in the event of a business interruption.

FUTURE CHANGES IN ACCOUNTING POLICIES AND DISCLOSURE

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 has evaluated and meets the requirements to defer the adoption of IFRS 9 until the new insurance contracts standard is adopted effective January 1, 2021.

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. 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. Revenue arising from insurance contracts and from financial instruments is outside the scope of IFRS 15. There are no other revenues arising from other sources of income.

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 its 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 recognize 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.

CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

The Company's disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed by EFH is recorded, processed, summarized and reported in a timely manner. This includes controls and procedures that are designed to ensure that information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

As of December 31, 2017, an evaluation was carried out, under the supervision of the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures as defined under Multilateral Instrument 52-109. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the design of these disclosure controls and procedures was effective.

Internal Controls over Financial Reporting

As at the quarter ended December 31, 2017, the Chief Executive Officer and the Chief Financial Officer evaluated the design of the Company's internal control over financial reporting. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the design of internal controls as at December 31, 2017, was effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

A new policy management system is being rolled out across the country and management is satisfied that sufficient internal controls over financial reporting are in place during the transition and partial completion of the project.

CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The Company's significant accounting policies are disclosed in note 3 to the consolidated financial statements for the years ended December 31, 2017 and 2016.

The preparation of the Company's consolidated financial statements requires management to use estimates that affect the amounts reported in the financial statements. These estimates 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 could change and impact future results.

Policy Liabilities

Policy liabilities consist of provisions for unpaid claims.

Provision for unpaid claims are maintained to cover the Company's estimated ultimate liability for unpaid losses and loss adjustment expenses with respect to reported and unreported claims incurred as of the end of each accounting period. The provision for unpaid claims and adjustment expenses is first determined on a case-by-case basis as claims are reported and then reassessed as additional information becomes known. The provision also accounts for the future development of these claims, including claims incurred but not reported (IBNR). Provisions for unpaid claims do not represent an exact calculation of liability, but instead represent estimates developed using projection techniques in accordance with Canadian accepted actuarial practice. These estimates are expectations of the ultimate cost of settlement and administration of claims based on the Company's assessment of facts and circumstances then known, its review of historical settlement patterns, estimates of trends in claims severity and frequency, legal theories of liability and other factors. The appointed actuary of EFH's subsidiaries, using appropriate actuarial techniques, evaluates the adequacy of the policy liabilities at the end of each reporting period.

Variables in the reserve estimation process can be affected by both internal and external events, such as changes in claims handling procedures, economic inflation, legal trends and legislative changes. Many of these items are not directly quantifiable, particularly on a prospective basis. Additionally, there may be significant reporting lags between the occurrence of the insured event and the time it is actually reported to the insurer. These estimates are refined in a systematic ongoing process as historical loss experience develops and additional claims are reported and settled. Because the establishment of reserves is an inherently uncertain process involving estimates, current reserves may not be sufficient. Adjustments to reserves, both positive and negative, are reflected in the consolidated statements of income for the period in which such estimates are updated.

The provision for unpaid claims and adjustment expenses is discounted to take into account the time value of money. Changes in market interest rates and investment portfolio yield are the primary factors influencing the discount rate. Based on the net provision for unpaid claims and adjustment expenses as at December 31, 2017, a 1% increase in the discount rate would result in a decrease in the net provision of $5.1 million and a 1% decrease in the discount rate would increase the net provision by $5.3 million. It also includes a provision for adverse deviation, as required by Canadian accepted actuarial practice.

Impairment of Financial Assets

The Company considers an impairment if there is objective evidence that an available-for-sale financial asset is impaired, including in the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its carrying value. The Company considers an impairment if there is objective evidence that a loan or receivable collectability is impaired at which time the Company will write down the loan or receivable to the expected recoverable cost.

Factors considered by the Company include but are not limited to:

a) significant financial difficulty of the issuer or obligor;

b) a breach of contract, such as a default or delinquency in interest or principal payments;

c) the lender, for economic or legal reasons relating to the borrower's financial difficulty, granting to the borrower a concession that the lender would not otherwise consider;

d) it becoming probable that the borrower will enter bankruptcy or other financial reorganization;

e) the disappearance of an active market for that financial asset because of financial difficulties; or

f) observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group, including:

   (i) adverse changes in the payment status of borrowers in the group (e.g., an increased number of delayed payments or an increased number of credit card borrowers who have reached their credit limit and are paying the minimum monthly amount); or

   (ii) national or local economic conditions that correlate with defaults on the assets in the group (e.g., an increase in the unemployment rate in the geographical area of the borrowers, a decrease in property prices for mortgages in the relevant area, a decrease in oil prices for loan assets to oil producers, or adverse changes in industry conditions that affect the borrowers in the group).

Reinsurance

Reinsurer’s share of the provision for unpaid claims include amounts for expected recoveries related to provision for unpaid claims. Amounts recoverable from reinsurers are estimated in a manner consistent with claim and claim adjustment expense reserves. The ceding of an insurance liability to a reinsurer does not discharge EFH's primary liability to the policyholders. The Company’s policy is to record an estimated allowance for doubtful accounts on the basis of periodic evaluations of balances due from reinsurers, reinsurer solvency, credit ratings of reinsurers, collateral held by the Company, management’s experience and current economic conditions.

The Company is exposed to disputes on, and defects in, contracts with reinsurers and the possibility of default by reinsurers.

Income Taxes

Deferred income taxes, accumulated as a result of temporary differences, which are probable to reverse, are included in the consolidated balance sheet. In addition, the consolidated statements of income contains items that are non-taxable or non-deductible for income tax purposes, which cause the income tax provision to differ from what it would be if based on statutory rates. Recoverability of deferred tax assets is primarily based on current and expected profitability applicable to the Company and its ability to utilize any recorded tax assets taking into consideration tax planning strategies and the expiry date of tax losses.

Deferred policy acquisition cost

Portion of the deferred policy acquisition costs include general expenses that are capitalized based on management judgement.

GLOSSARY OF SELECTED INSURANCE TERMS

“Acquisition costs” commissions, premium taxes and a portion of general expenses related to policy acquisitions.

“Acquisition Expense ratio” for any period means the sum of the acquisition costs divided by Net earned premiums.

“Assumed written premiums” of an insurer for any period means the total insurance premiums written by the insurer while acting as a reinsurer during such period.

“Broker” an intermediary who negotiates policies of insurance or reinsurance with insurers on behalf of the insured or reinsured, receiving a commission from the insurer or the reinsurer for placement and other services rendered.

"Catastrophe event" or **"CAT event"** refers to a group of claims from a specific event considered to be non-recurring and therefore not reflective of normal operating performance.

“Catastrophe reinsurance” a form of insurance, which subject to specified limits, indemnifies the ceding company for the amount of loss in excess of a specified retention amount with respect to an accumulation of losses resulting from a CAT event.

“Cede” means the act of an insurer transferring or assigning part or all of the risk of an insurance policy written by it to a reinsurer by purchasing insurance from such reinsurer to cover the risk or part thereof.

“Ceded earned premiums” means ceded written premium during the period, plus the ceded unearned premiums reserve at the beginning of the period, less the ceded unearned premiums reserve at the end of the period.

“Ceded written premiums” of an insurer for any period means the total insurance premiums written transferred by the insurer to a reinsurer during such period.

“Claim” the amount owed by an insurer or reinsurer pursuant to a policy of insurance or reinsurance arising from the loss relating to an insured event.

“Claims development” a non-IFRS measure representing the change in reserve balance on unpaid claims through the process of adjudication from the initial estimate to the ultimate amount paid. The difference between prior year end estimates of ultimate undiscounted claim costs and the current estimates for the same block of claims. A favourable development represents a reduction in the estimated ultimate claim costs during the period for that block of claims. An unfavourable development represents an increase in the estimated ultimate claims costs during the period.

“Combined ratio” of an insurer for any period means the sum of the loss ratio and the expense ratio of the insurer for such period.

“Deferred policy acquisition expenses (DPAC)” means the portion of acquisition costs within a policy term which have not yet earned.

“Direct written premiums” of an insurer for any period means the total insurance premiums written by the insurer during such period.

“Expense ratio” for any period means the sum of the acquisition expense ratio and the general expense ratio.

“Facility Association” is an unincorporated non-profit organization established by the automobile insurance industry to ensure that automobile insurance is available to all owners and licensed drivers of motor vehicles where such owners or drivers are unable to obtain automobile insurance through the voluntary insurance market

“Frequency of claims” the ratio of the number of claims files opened in a period to the total number of policies in force. A measure of how often a claim is reported as a function of policies in force.

“General Expense ratio” for any period means the sum of all general expenses divided by Net earned premiums.

“Gross CASE Loss ratio” for any period means the sum of gross claims and gross claims adjustment expenses incurred expressed as a percentage of gross earned premiums.

“Gross earned premiums” means written premium during the period, plus the unearned premiums reserve at the beginning of the period, less the unearned premiums reserve at the end of the period.

“Gross Ultimate Loss ratio” for any period means the sum of claims, claims adjustment expenses and IBNR incurred expressed as a percentage of gross earned premiums.

“Incurred but not reported (IBNR)” the estimate of claims incurred but not yet reported by policyholders and not enough case reserve.

“Industry pools” consist of the “residual market” as well as mandatory risk-sharing pools (RSP) in Alberta, Ontario, Quebec, New Brunswick and Nova Scotia. These pools provide automobile insurance to individuals who are otherwise unable to purchase such coverage from private insurers acting voluntarily. All insurance companies share in the results of the pool according to their market share.

“Large Loss” s a single claim in excess of 100,000.

“Line of business” the major product groupings offered to the public.

“Loss adjustment expenses” or **“LAE”** means the expense of settling claims, including certain legal and other fees and the expense of administering the claims adjustment process.

“Market yield adjustment (MYA)” a non-IFRS measure representing the impact of changes in the discount rate on claims liabilities, the provision for adverse deviation (PFADs) and other discounting assumptions based on the change in the market-based yield of the underlying assets.

“Managing General Agent (MGA)” is an individual or business entity appointed by an insurer to solicit applications from agents for insurance contracts or to negotiate insurance contracts on behalf of an insurer and, if authorized to do so by an insurer, to effectuate and countersign insurance contracts.

“Minimum Capital Test” means the regulatory guideline under which a federally regulated insurer is measured for the adequacy of its capital.

“Net CASE Loss ratio” for any period means the sum of claims and claims adjustment expenses incurred less any ceded claims and claim expenses incurred expressed as a percentage of net earned premiums.

“Net earned premiums” of an insurer is the gross earned premiums less the ceded earned premiums.

“Net Operating Income” means net income plus or minus the after tax impact of change in market yield adjustment,, realized losses or gains on sale of investments, discontinued operations, unrealized fair value changes on FVTPL investments and one time non recurring charges.

“Net Ultimate Loss ratio” for any period means the sum of claims, claims adjustment expenses and IBNR incurred less any ceded claims, claim expenses and IBNR incurred expressed as a percentage of net earned premiums.

“Net written premiums” of an insurer for any period means direct written premiums less ceded written premiums.

“Producers” refers to, collectively, insurance brokers, agents and managing general agencies**.**

“Property and casualty (P&C) insurance” all insurance excluding life insurance and governmental insurance. Also known as general insurance.

“Provision for adverse deviation (PFAD)” margins that are added to loss reserves to provide for adverse deviation from claims reserve estimates; this includes provisions covering claims development variability and risks associated with interest rate and reinsurance recoveries.

“Reinsurance” means an arrangement in which an insurance company agrees to indemnify another insurance or reinsurance company against all or a portion of the insurance or reinsurance risks underwritten by the ceding company under one or more policies.

“Retention” has two meanings: (1) in respect of reinsurance, the amount of risk not ceded to reinsurers; (2) in respect to policies in force, the number of policyholders who renew for a subsequent term.

“Return on equity” or “ROE” for a period means net income expressed as a percentage of the average total shareholder equity in that period.

“Salvage recoverable” Salvage recoverable is the estimated value of damaged property that may be retrieved, reconditioned, and sold to reduce the amount of an insured loss.

“Severity of claims” the average cost of each claim, based on the total claims cost and number of claims opened in a period.

“Subrogation recoverable” is the estimate of the amount the insurer will collect from a negligent third party or their insurer after assuming the insured’s legal right to collect damages.

“Underwriting” means the assumption of risk for designated loss or damage by issuing a policy of insurance in respect thereof.

“Underwriting income or loss” a non-IFRS measure calculating the profit or loss from the activity of taking on insurance risks, excluding the impact of the market yield adjustment.

“Unearned Commissions” means the portion of reinsurance commissions within a policy term which have not yet earned.

“Unearned premiums” means the portion of premiums within a policy term which have not yet earned.

“Unearned premiums recoverable” means the portion of ceded written premiums within a policy term which have not yet earned.

“Unpaid claims and adjustment expenses” the liability to cover the estimated remaining cost of settling claims, including IBNR.

“Unpaid claims and adjustment expenses recoverable” the portion of the unpaid claims and adjustment expense that will be reimburse by reinsurers.’