Unaudited Condensed Consolidated Interim Financial Statements of

# EFH Holdings Inc.

For three months ended March 31, 2021 and 2020

NOTICE OF NO AUDITOR REVIEW OF
CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS

In accordance with National Instrument 51-102 of the Canadian Securities Administrators, the Company discloses that its external auditors have not reviewed the unaudited condensed consolidated interim financial statements for the three months ended March 31, 2021. These financial statements have been prepared by management and approved by the Audit Committee and the Board of Directors of the Company.

**EFH HOLDINGS INC.**
**Consolidated Balance Sheet**
(unaudited, in thousands of Canadian dollars)

| | Note | March 31, 2021 | December 31, 2020 |
|---|---|---|---|
| **Assets** | | | |
| Cash and short-term deposits | 7 | 9,801 | 11,859 |
| Accounts receivable | | 12,208 | 12,039 |
| Investments | 7 | 45,249 | 44,582 |
| Due from insurance companies | | 969 | 596 |
| Deferred policy acquisition costs | | 5,253 | 5,110 |
| Income taxes recoverable | | 497 | 460 |
| Prepaid expenses and other assets | | 1,779 | 1,688 |
| Reinsurers' share - unearned premiums | | 681 | 799 |
| - provision for unpaid claims | 8 | 2,819 | 3,683 |
| Right of use asset | | 383 | 482 |
| Goodwill | | 378 | 378 |
| Deferred income taxes | | 225 | 195 |
| Total assets | | 80,242 | 81,871 |
| **Liabilities** | | | |
| Accounts payable and accrued liabilities | | 1,932 | 3,549 |
| Unearned premiums | | 22,717 | 22,571 |
| Unearned commission | | 200 | 220 |
| Income taxes payable | | 412 | 1,620 |
| Lease liability | | 323 | 409 |
| Provision for unpaid claims | 8 | 29,781 | 29,668 |
| Total liabilities | | 55,365 | 58,037 |
| **Equity** | | | |
| Share capital | | 2,794 | 2,794 |
| Contributed surplus | | 1,507 | 1,507 |
| Retained earnings | | 14,959 | 14,186 |
| Accumulated other comprehensive income | 12 | 581 | 616 |
| Equity attributed to shareholders of the Company | | 19,841 | 19,103 |
| Non-controlling interest | 14 | 5,036 | 4,731 |
| Total equity | | 24,877 | 23,834 |
| Total liabilities and equity | | 80,242 | 81,871 |

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

**EFH HOLDINGS INC.**
**Consolidated Statement of Income and Comprehensive Income**
(unaudited, in thousands of Canadian dollars, except per share amounts)

| | Note | 3 months ended March 31 2021 | 2020 |
|---|---|---|---|
| Revenue | | | |
| Gross written and assumed premiums | | 11,374 | 8,037 |
| Less premiums ceded to reinsurers | | (407) | (427) |
| Net written and assumed premiums | | 10,967 | 7,610 |
| Change in gross unearned premiums | | (146) | 1,248 |
| Change in unearned premiums, reinsurers' share | | (118) | (399) |
| Change in provision for unearned premiums | | (264) | 849 |
| Net earned premiums | | 10,703 | 8,459 |
| Investment income | 7 | 674 | (21) |
| Total revenue | | 11,377 | 8,438 |
| Expenses | | | |
| Gross claims incurred | | 5,130 | 4,322 |
| Claims from reinsurers | | 274 | 64 |
| Net incurred claims | | 5,404 | 4,386 |
| Gross acquisition costs | | 2,596 | 1,907 |
| Acquisition (recoveries) from reinsurers | | (16) | (17) |
| Net acquisition costs | | 2,580 | 1,890 |
| Operating costs | 11 | 1,922 | 1,677 |
| Total expenses | | 9,906 | 7,953 |
| Income before taxes and discount rate impact on claims | | 1,471 | 485 |
| Impact of change in discount rate on claims [1] | | (5) | 131 |
| Income before income taxes | | 1,466 | 616 |
| Income tax expense | 10 | 377 | 168 |
| Net income | | 1,089 | 448 |
| Attributed to: | | | |
| Shareholders of the Company | | 773 | 331 |
| Non-controlling interest | 14 | 316 | 117 |
| Net income | | 1,089 | 448 |
| Other comprehensive income (loss), net of taxes that may be classified subsequently to net income<br>Available-for-sale investments: | | | |
| Change in net unrealized gains | | (100) | (2,370) |
| Reclassification of net realized losses / (gains) to net income | | 35 | (65) |
| Tax impact | | 19 | 109 |
| Other comprehensive (loss) | | (46) | (2,326) |

**EFH HOLDINGS INC.**
**Consolidated Statement of Changes in Equity**
(unaudited, in thousands of Canadian dollars)

| | Note | 3 months ended March 31 2021 | 2020 |
|---|---|---|---|
| Attributed to: | | | |
| Shareholders of the Company | | (35) | (2,264) |
| Non-controlling interest | 14 | (11) | (62) |
| Other comprehensive (loss) | | (46) | (2,326) |
| Total comprehensive income (loss) | | 1,043 | (1,878) |
| Attributed to: | | | |
| Shareholders of the Company | | 738 | (1,933) |
| Non-controlling interest | 14 | 305 | 55 |
| Total comprehensive income (loss) | | 1,043 | (1,878) |
| Earnings per share attributable to shareholders of the Company | 13 | | |
| Earnings per share – basic | | $0.06 | $0.03 |
| Earnings per share – diluted | | $0.06 | $0.03 |

(1) As interest rates may change each period, and have an impact to the incurred claims and therefore management believes it is beneficial to the users to see the impact of this change separately in order to understand the true movement in claims incurred.

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

| | Share Capital | Contributed Surplus | Accumulated Other Comprehensive Income | Retained Earnings | Shareholders' Equity | Non-controlling Interest | Total Equity |
|---|---|---|---|---|---|---|---|
| Balance at January 1, 2021 | 2,794 | 1,507 | 616 | 14,186 | 19,103 | 4,731 | 23,834 |
| Net income | - | - | - | 773 | 773 | 316 | 1,089 |
| Other comprehensive (loss) | - | - | (35) | - | (35) | (11) | (46) |
| Total comprehensive (loss) income | - | - | (35) | 773 | 738 | 305 | 1,043 |
| Balance at March 31, 2021 | 2,794 | 1,507 | 581 | 14,959 | 19,841 | 5,036 | 24,877 |

| | Share Capital | Contributed Surplus | Accumulated Other Comprehensive Income | Retained Earnings | Shareholders' Equity | Non-controlling Interest | Total Equity |
|---|---|---|---|---|---|---|---|
| Balance at January 1, 2020 | 2,794 | 1,507 | 2,034 | 83,140 | 89,475 | 3,732 | 93,207 |
| Net income | - | - | - | 331 | 331 | 117 | 448 |
| Other comprehensive loss | - | - | (2,264) | - | (2,264) | (62) | (2,326) |
| Total comprehensive (loss) income | - | - | (2,264) | 331 | (1,933) | 55 | (1,878) |
| Balance at March 31, 2020 | 2,794 | 1,507 | (230) | 83,471 | 87,542 | 3,787 | 91,329 |

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

**EFH HOLDINGS INC.**
**Consolidated Statement of Cash Flows**
(unaudited, in thousands of Canadian dollars, except per share amounts)

| | 3 months ended | |
|---|---|---|
| | **March 31, 2021** | **March 31, 2020** |
| Cash provided by (used in) | | |
| Operating activities | | |
| Net income | 1,089 | 448 |
| Adjusted for | | |
| Reinsurers' share of unearned premiums | 118 | 399 |
| Reinsurers' share of unpaid claims | 864 | 309 |
| Provision for unpaid claims | 113 | (938) |
| Unearned premiums | 146 | (1,248) |
| Deferred income taxes | (30) | 97 |
| Unearned commissions | (20) | (28) |
| Deferred policy acquisition costs | (143) | 205 |
| Amortization on leased assets | 99 | 97 |
| Amortization on property plant equipment and intangible assets | 97 | 61 |
| Amortization of premiums on bonds | 40 | 6 |
| Fair value change on FVTPL investments | (262) | 802 |
| Prepaid expenses & other assets | (80) | (128) |
| | 942 | (366) |
| Cash flow from changes in | | |
| Accounts receivable | (169) | 714 |
| Net realized gains | 10 | (53) |
| Income taxes recoverable | (1,227) | 71 |
| Due from insurance companies | (373) | (479) |
| Other liabilities | (1,617) | (790) |
| Cash used by operating activities | (1,345) | (455) |
| Financing activities | | |
| Payment of lease liabilities | (86) | (76) |
| Cash used by financing activities | (86) | (76) |
| Investing activities | | |
| Purchases of property, equipment and intangible assets | (107) | (30) |
| Purchases of investments | (8,119) | (7,923) |
| Sale/maturity of investments | 7,599 | 7,804 |
| Cash used by investing activities | (627) | (149) |
| Decrease in cash and short-term deposits | (2,058) | (680) |
| Cash and short-term deposits, beginning of year | 11,859 | 70,932 |
| Cash and short-term deposits, end of year | 9,801 | 70,252 |
| Supplementary information | | |
| Income taxes paid | 1,632 | - |

## 1. Nature of operations

EFH Holdings Inc. ("the Company"), incorporated in Canada on August 18, 1997, under the Business Corporations Act (Ontario) is domiciled in Canada and its shares are traded on the TSX Venture Exchange. The Company's name was changed from Echelon Financial Holdings Inc. to EFH Holdings Inc. after receiving approval from shareholders on December 11, 2020. The Company is principally engaged, through its subsidiary, in property and casualty insurance in Canada through its 75% owned subsidiary – The Insurance Company of Prince Edward Island ("ICPEI"). The Company's head office is located at 2800 Skymark Avenue, Suite 200, Mississauga, Ontario.

## *2.* COVID-19 pandemic

COVID 19 continues to be a serious threat and the situation is evolving daily. The risk varies between and within communities and regions. Ontario region has been affected more compared to the PEI region. ICPEI continues to implement its emergency operational plan, which included transitioning most employees to work from home and only a small number of staff in the office to perform functions which could not be performed remotely.

ICPEI has provided a number of accommodations to its policyholders if they experience hardship because of COVID-19 and adjust their auto premiums due to reduction of use. ICPEI has only experienced a very minor increase in the number of customer defaults and very few requests to lower monthly premiums based on lower usage of vehicles. These did not have a significant impact on the results of the Company. The number of motor vehicle claims decreased in the year compared to prior year. The impact is reflected in the lower claims expense.

The effects on the Company's development of critical estimates during the first quarter of 2021 are described below:

***Investment valuation***

The Company's valuation technique and recognition of impairment remain unchanged. The Company's investments are valued at fair value using Level 1 or Level 2 inputs that are primarily based on quoted market prices. The Company has no Level 3 investments that require more assumptions and judgement in their valuation. COVID 19 did not have any adverse impact on valuation of investments.

***Provision for unpaid claims***

ICPEI does not provide insurance coverage specifically for pandemic risk. However, in its commercial property policies, it offers coverage for business interruption. Based on outside legal counsel review, ICPEI does not believe that business interruption claims from pandemic Covid-19 are covered perils. ICPEI will continue to monitor all developments in future. There has been no development since the annual financial statement for the year ended 31st December 2020.

***Credit risk***

During the first quarter of 2021, the Company's exposure to credit risk continued to remain high primarily due to the continued potential effects of COVID-19 pandemic on the Company's reinsurers, insurance contract receivables from customers, and issuers of the Company's investments in bonds. There were no significant changes used in the first quarter of 2021 to monitor and evaluate credit risks. There was no downgrade of reinsurers' credit rating and there were no significant delinquent payments from customers. Valuation of investment bonds is based on observable market values, which already reflect the associated credit risks associated with the issuers.

## 3. Basis of preparation

These condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) applicable to the preparation of interim financial statements, including IAS 34, Interim Financial Reporting. The condensed consolidated interim financial statements should be read in conjunction with the annual financial statements for the year ended December 31, 2020, which have been prepared in accordance with IFRS.

These consolidated financial statements have been authorized for issue by the Board of Directors on May 20, 2021.

## 4. Summary of significant accounting policies

The accounting policies adopted are consistent with those of the previous financial year-end.

**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, since the percentage of liabilities connected with insurance contracts over total liabilities meets the 90% threshold. The company has deferred adoption, until the new insurance contracts standard is adopted effective January 1, 2023.

***IFRS 17, Insurance Contracts***

IASB published IFRS 17 with effective date delayed to January 1, 2023, 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.

## 5. Critical accounting estimates and assumptions

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

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

In preparing these condensed consolidated interim financial statements, the significant judgements made by management in applying accounting policies and the key sources of estimation uncertainty were the same as those applied to the annual 2020 consolidated financial statements.

## 6. Seasonality

The P&C insurance business is seasonal in nature. While net earned premiums reflect the premium volume from quarter to quarter, net underwriting income can be driven by weather conditions or random occurrences, which may vary significantly by quarter.

## 7. Investments

The following table provides a breakdown of the investment portfolio:

| | **Fair values** | |
|---|---|---|
| **Available for sale** | **As at March 31, 2021** | **As at December 31, 2020** |
| Fixed income | | |
| Canadian | | |
| Federal | 4,685 | 6,704 |
| Provincial | 6,044 | 5,163 |
| Municipal | 107 | 110 |
| Corporate | 7,414 | 6,747 |
| Foreign | | |
| Corporate | 440 | - |
| Total fixed income | 18,690 | 18,724 |
| Corporate value pooled fund | 6,874 | 6,481 |
| Money market pooled funds | 1,128 | 852 |
| Short-term fixed income and mortgage pooled funds | 14,345 | 14,439 |
| Total pooled funds | 22,347 | 21,772 |
| Common shares | | |
| Canadian | 390 | 339 |
| Total common shares | 390 | 339 |
| Total available for sale | 41,427 | 40,835 |
| Fair value through profit or loss | | |
| Preferred shares | 3,822 | 3,747 |
| Total preferred shares | 3,822 | 3,747 |
| Total investments | 45,249 | 44,582 |
| Cash and short-term deposits | 9,801 | 11,859 |
| Total investments including cash and short-term deposits | 55,050 | 56,441 |

**Fair value**

The Company is responsible for determining the fair value of its investment portfolio by utilizing market-driven fair value measurements from active markets, where available, by considering other observable and unobservable inputs, and by employing valuation techniques, which make use of current market data. The technique employed has remained the same from December 31, 2020. The Company uses a fair value hierarchy to categorize the inputs used in valuation techniques to measure fair value. A description of the inputs used in the valuation of financial instruments is as follows:

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

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

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

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

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

The following table provides the classification of the Company's investments within the fair value hierarchy, as outlined, as at March 31, 2021 and December 31, 2020:

| **March 31, 2021** | | | |
|---|---|---|---|
| | **Level 1** | **Level 2** | **Total** |
| Fixed income | - | 18,690 | 18,690 |
| Corporate value pooled funds | - | 6,874 | 6,874 |
| Money market pooled funds | - | 1,128 | 1,128 |
| Short-term fixed income and mortgage pooled funds | - | 14,345 | 14,345 |
| Common Shares | 390 | - | 390 |
| Preferred Shares | 3,822 | - | 3,822 |
| | 4,212 | 41,037 | 45,249 |

| **December 31, 2020** | | | |
|---|---|---|---|
| | **Level 1** | **Level 2** | **Total** |
| Fixed income | - | 18,724 | 18,724 |
| Corporate value pooled funds | - | 6,481 | 6,481 |
| Money market pooled funds | - | 852 | 852 |
| Short-term fixed income and mortgage pooled funds | - | 14,439 | 14,439 |
| Common Shares | 339 | - | 339 |
| Preferred Shares | 3,747 | - | 3,747 |
| | 4,086 | 40,496 | 44,582 |

The Company's policy is to recognize transfers into and transfers out of fair value hierarchy levels as of the date of the event or change in circumstances that caused the transfer. There were no transfers from the existing portfolio for the quarter ended March 31, 2021 or December 31, 2020.

The fair values of cash and short-term deposits, account receivables and financial liabilities approximate their carrying values due to their short-term nature.

The Company has interests in unconsolidated structured entities, through investments in pooled funds, which are included in investments on the balance sheet. These entities are not controlled by the Company. The carrying value of pooled funds and maximum exposure to loss as of March 31, 2021 was $22,347 (December 31, 2020 – $21,772). Investments in pooled funds consist of units invested in underlying money market and mortgage securities managed by third-party managers. The pooled funds are perpetual private trusts created under trust agreements. Financing is only provided to the pooled funds through the purchase of units and is therefore limited to the investment made.

**Impaired assets and provisions for losses**

A gross unrealized loss of $148 on Available for Sale (AFS) investments at March 31, 2021 (December 31, 2020 – $25) is recorded, net of tax, in the amount of $103 (December 31, 2020 – $17) in Accumulated Other Comprehensive Income.

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

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

No impairment on AFS investments was recognized in the first quarter of 2021. An impairment of $124 was recognized for the period ended March 31, 2020.

**Investment income**

The table below provides additional details on net investment income.

| | 3 months ended March 31 | |
|---|---|---|
| | **2021** | **2020** |
| Interest income | 404 | 692 |
| Dividend income | 52 | 103 |
| Net realized (losses) gains | (10) | 177 |
| Impairment (writedown) | - | (124) |
| Fair value change on FVTPL investments | 262 | (802) |
| Investment expenses | (34) | (67) |
| Investment income | 674 | (21) |

## 8. Provision for unpaid claims

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

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

| Entity | March 31, 2021 | December 31, 2020 |
|---|---|---|
| ICPEI | 1.74% | 1.75% |

The Company recorded a $463 addition, as at March 31, 2021, to the net provision for unpaid claims relating to unfavourable development in prior years' estimates (December 31, 2020 – $113 unfavourable).

To recognize the uncertainty in establishing these best estimates, to allow for possible deterioration in experience, and to provide greater comfort that the actuarial liabilities are adequate to pay future claims, the Company includes provisions for adverse deviations (PFADs) in some assumptions relating to claims development, reinsurance recoveries, and future investment income. The PFADs selected are in the mid-range of those recommended by the Canadian Institute of Actuaries. The aggregate impact of the provision for adverse deviation is to increase the provision for unpaid claims on a net basis by $1,869 as at March 31, 2021 (December 31, 2020 – $1,846).

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

**Claims development**

| **Provision for unpaid claims analysis** | **March 31, 2021** | **December 31, 2020** |
|---|---|---|
| Unpaid claims, beginning of year, net | 25,985 | 23,361 |
| Unfavourable prior year claims development | 463 | 113 |
| Net claims incurred in current period | 4,946 | 20,143 |
| Paid on claims occurring during | | |
| Current period | (1,753) | (10,788) |
| Prior period | (2,679) | (6,844) |
| Unpaid claims, end of period, net | 26,962 | 25,985 |
| Reinsurers' share | 2,819 | 3,683 |
| Gross unpaid claims | 29,781 | 29,668 |

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

Assumptions used to develop the provision estimate for unpaid claims and adjustment expenses are selected by class of business and geographic location. Consideration is given to the characteristics of the risks, historical trends, and the amount of data available on individual claims, inflation and any other pertinent factors. Some assumptions require a significant amount of judgement such as the expected impacts of future judicial decisions and government legislation. There were no new assumptions identified in the first quarter as having a potential or identifiable material impact on the overall claims estimate.

## 9. Risk management

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

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

**Insurance risk**

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

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

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

### Interest rate risk

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

The sensitivity analysis for interest rate risk as set out in the table below illustrates the impact of changes in interest rates on other comprehensive income ("OCI") relating to the fixed income investment portfolio as at March 31, 2021, and December 31, 2020, based on parallel 50 basis point shifts in interest rates up and down in 25 basis point increments.

| Change in interest rates As at March 31, 2021 | Fair value of fixed income and pooled funds | Hypothetical change on fair value | Effect on OCI net of tax |
|---|---|---|---|
| 50 basis point rise | 40,449 | (1.4)% | (410) |
| 25 basis point rise | 40,743 | (0.7)% | (205) |
| No change | 41,037 | - | - |
| 25 basis point decline | 41,331 | 0.7% | 205 |
| 50 basis point decline | 41,625 | 1.4% | 410 |

| Change in interest rates As at December 31, 2020 | Fair value of fixed income and pooled funds | Hypothetical change on fair value | Effect on OCI net of tax |
|---|---|---|---|
| 50 basis point rise | 39,890 | (1.5)% | (423) |
| 25 basis point rise | 40,193 | (0.7)% | (211) |
| No change | 40,496 | - | - |
| 25 basis point decline | 40,800 | 0.7% | 211 |
| 50 basis point decline | 41,103 | 1.5% | 423 |

### Liquidity risk

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

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

The maturity profile of bonds is as follows, as at March 31, 2021 and December 31, 2020:

| **March 31, 2021** | **Less than 1 year** | **1 – 3 years** | **3 – 5 years** | **Greater than 5 years** | **Total** |
|---|---|---|---|---|---|
| Bonds | 311 | 7,082 | 3,957 | 7,340 | 18,690 |
| Cash and cash equivalents | 9,801 | - | - | - | 9,801 |
| Accounts receivable | 12,208 | - | - | - | 12,208 |
| Total | 22,320 | 7,082 | 3,957 | 7,340 | 40,699 |
| Percentage of total | 55% | 17% | 10% | 18% | 100% |

| **December 31, 2020** | **Less than 1 year** | **1 – 3 years** | **3 – 5 years** | **Greater than 5 years** | **Total** |
|---|---|---|---|---|---|
| Bonds | 668 | 6,724 | 7,109 | 4,223 | 18,724 |
| Cash and cash equivalents | 11,859 | - | - | - | 11,859 |
| Accounts receivable | 12,039 | - | - | - | 12,039 |
| Total | 24,566 | 6,724 | 7,109 | 4,223 | 42,622 |
| Percentage of total | 58% | 16% | 16% | 10% | 100% |

The following tables summarize the expected timing of cash flows arising from insurance obligations, on an undiscounted basis, as at March 31, 2021 and December 31, 2020:

| **March 31, 2021** | **Less than 1 year** | **1 – 3 years** | **3 – 5 years** | **Greater than 5 years** | **Total** |
|---|---|---|---|---|---|
| Gross claim liabilities | 14,243 | 6,814 | 3,258 | 4,020 | 28,335 |
| Less: Reinsurance recoverable | 662 | 778 | 223 | 1,019 | 2,682 |
| Net actuarial liabilities | 13,581 | 6,036 | 3,035 | 3,001 | 25,653 |

| **December 31, 2020** | **Less than 1 year** | **1 – 3 years** | **3 – 5 years** | **Greater than 5 years** | **Total** |
|---|---|---|---|---|---|
| Gross claim liabilities | 10,209 | 10,683 | 4,087 | 3,257 | 28,236 |
| Less: Reinsurance recoverable | 625 | 2,361 | (223) | 730 | 3,493 |
| Net actuarial liabilities | 9,584 | 8,322 | 4,310 | 2,527 | 24,743 |

**Equity price risk**

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

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

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

The table below summarizes the potential impact of a 10% change in the value of the equity securities (common and preferred shares) on net income and OCI for the three months ended March 31, 2021, and the year ended December 31, 2020. Certain shortcomings are inherent in the method of analysis presented, as the analysis is based on the assumption that all equity holdings increased/decreased by 10% with all other variables held constant.

| Change in equity holdings | Effect on net income (loss) net of tax | | Effect on OCI net of tax | |
|---|---|---|---|---|
| | March 31, 2021 | December 31, 2020 | March 31, 2021 | December 31, 2020 |
| 10% rise | 266 | 261 | 27 | 25 |
| 10% decline | (266) | (261) | (27) | (25) |

### Credit risk

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

### Fixed income portfolio

A breakdown of the fixed income portfolio by credit rating is shown below as at March 31, 2021 and December 31, 2020:

| | As at March 31, 2021 | | As at December 31, 2020 | |
|---|---|---|---|---|
| | Fair value | % | Fair value | % |
| AAA | 6,344 | 34% | 8,179 | 44% |
| AA | 5,105 | 27% | 4,577 | 24% |
| A | 6,208 | 33% | 4,918 | 26% |
| BBB | 1,033 | 6% | 1,050 | 6% |
| Total | 18,690 | 100% | 18,724 | 100% |

### Preferred share portfolio

A breakdown of the preferred shares portfolio by credit rating is shown below as at March 31, 2021 and December 31, 2020:

| | As at March 31, 2021 | | As at December 31, 2020 | |
|---|---|---|---|---|
| | Fair value | % | Fair value | % |
| P2 | 3,273 | 86% | 3,234 | 86% |
| P3 | 549 | 14% | 513 | 14% |
| Total | 3,822 | 100% | 3,747 | 100% |

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

### 10. Income taxes

The income tax is as follows:

| | 3 months ended March 31 | |
|---|---|---|
| | **2021** | **2020** |
| Current | 407 | 70 |
| Deferred | (30) | 98 |
| | 377 | 168 |

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

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

The difference is broken down as follows:

| | 3 months ended March 31 | |
|---|---|---|
| | **2021** | **2020** |
| Income tax expense calculated on statutory rates | 26.5% | 27.0% |
| Increase (decrease) in income tax rates resulting from: | | |
| Non-taxable dividend income | (1.0)% | (4.6)% |
| Statutory rate difference | 0.2% | 3.7% |
| Other | - | 1.2% |
| Effective income tax rate | 25.7% | 27.3% |

### 11. Operating costs by nature

The table below presents operating costs by major category.

| | 3 months ended March 31 | |
|---|---|---|
| | **2021** | **2020** |
| Salaries and benefits | 970 | 703 |
| Systems costs | 177 | 115 |
| Professional fees | 88 | 82 |
| Directors' and Regulatory Filing fees | 31 | 54 |
| Occupancy and lease cost | 176 | 149 |
| Printing and postage | 39 | 34 |
| Facility | 143 | 112 |
| Management Fees | 47 | 44 |
| Other expenses | 251 | 384 |
| | 1,922 | 1,677 |

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

### 12. Accumulated other comprehensive income

A breakdown of the accumulated other comprehensive income is shown below as at March 31, 2021 and December 31, 2020:

| | As at March 31, 2021 | As at December 31, 2020 |
|---|---|---|
| Gross unrealized gains | 793 | 841 |
| Tax impact | (212) | (225) |
| Ending balance | 581 | 616 |

### 13. Earnings per share

Earnings per share are calculated in the following table:

| | 3 months ended March 31 | |
|---|---|---|
| **Total Earnings per Share** | **2021** | **2020** |
| Basic earning per share: | | |
| Net income available to shareholders | 773 | 331 |
| Average number of common shares | 12,007 | 12,007 |
| Basic earnings per share | $0.06 | $0.03 |
| Diluted earnings per share: | | |
| Average number of common shares | 12,007 | 12,007 |
| Average number of dilutive common shares under employee stock compensation plan | 110 | - |
| Average number of diluted common shares | 12,117 | 12,007 |
| Diluted earnings per share | $0.06 | $0.03 |

The Company has granted 216,300 Restricted Share Units ("RSUs") to certain officers and employees of the Company. Each RSU is exercisable into one common share of the Company upon vesting. The RSUs will vest in three equal installments on the anniversaries from the date of grant.

### 14. Non-controlling interest

The Company has non-controlling interests attributable to the subsidiary of ICPEI. Please refer to Notes 1 and 16. The following tables summarize the comprehensive income attributable to the non-controlling shareholders:

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

| | 3 months ended March 31 | |
|---|---|---|
| | **2021** | **2020** |
| Revenue | | |
| Gross written and assumed premiums | 2,844 | 2,009 |
| Net earned premiums | 2,676 | 2,115 |
| Investment Income | 168 | (82) |
| Total revenue | 2,844 | 2,033 |
| Expenses | | |
| Net incurred claims | 1,351 | 1,064 |
| Net acquisition costs | 645 | 473 |
| Operating costs | 422 | 334 |
| Total expenses | 2,418 | 1,871 |
| Income before income taxes | 426 | 163 |
| Income tax expense | 110 | 46 |
| Net income attributable to NCI | 316 | 117 |
| Other comprehensive (loss) attributable to NCI | (11) | (62) |
| Comprehensive income attributable to NCI | 305 | 55 |

The following tables summarize the net assets of the non-controlling shareholders as at March 31, 2021 and December 31, 2020:

| | **March 31, 2021** | **December 31, 2020** |
|---|---|---|
| Assets | | |
| Cash and investments | 12,739 | 13,008 |
| Other assets | 6,158 | 6,224 |
| Total assets | 18,897 | 19,232 |
| Liabilities | | |
| Unearned premium | 5,679 | 5,643 |
| Unpaid claims | 7,445 | 7,417 |
| Other liabilities | 737 | 1,441 |
| Total liabilities | 13,861 | 14,501 |
| Equity | | |
| AOCI | 194 | 205 |
| Retained earnings | 4,842 | 4,526 |
| Total equity | 5,036 | 4,731 |
| Total liabilities and equity | 18,897 | 19,232 |

| | **March 31, 2021** | **December 31, 2020** |
|---|---|---|
| Cash flow from operating activities | (258) | 2,732 |
| Cash flow from investing activities | (157) | (1,850) |
| Cash flow from financing activities | (22) | (102) |
| Net (decrease) / increase in cash and short-term deposits | (437) | 780 |

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

### 15. Segmented information

The Company operates through two segments: Personal Lines and Commercial Lines businesses. Through its Personal Lines segment, the Company is engaged primarily in the underwriting of automobile insurance and personal property. Through its Commercial Lines, the Company designs and underwrites commercial property, commercial automobile.

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

The following table summarizes the net income before interest and income taxes by Personal and Commercial Lines:

| | **3 months ended March 31** | |
|---|---|---|
| | **2021** | **2020** |
| Revenue | | |
| Net earned premiums | | |
| - Personal Lines | 6,792 | 5,976 |
| - Commercial Lines | 3,911 | 2,483 |
| Total net earned premium | 10,703 | 8,459 |
| Net claims incurred | | |
| - Personal Lines | 3,869 | 2,851 |
| - Commercial Lines | 1,535 | 1,535 |
| Net claims | 5,404 | 4,386 |
| Net expenses | | |
| - Personal Lines | 2,715 | 2,180 |
| - Commercial Lines | 1,551 | 1,047 |
| Total | 4,266 | 3,227 |
| Total net expenses | 9,670 | 7,613 |
| Underwriting income (loss) before income taxes | | |
| - Personal Lines | 208 | 945 |
| - Commercial Lines | 825 | (99) |
| Total | 1,033 | 846 |
| Corporate and other | (236) | (340) |
| Underwriting income | 797 | 506 |
| Impact of change in net claims discount rate | (5) | 131 |
| Investment income (loss) | 674 | (21) |
| Total income before income taxes | 1,466 | 616 |

## 16. Subsequent Event

On April 1, 2021, the Company acquired the remaining 25% ownership of The Insurance Company of Prince Edward Island ("ICPEI") that it did not already own. Total cash consideration paid was $6,315 plus assumption of $514 liabilities. The former CEO of ICPEI was part of the minority interest group and the transaction was completed at arm's length.

Prior to this transaction, the Company owned 75% of ICPEI and these financial statements are prepared on a consolidated basis with ICPEI and the 25% ownership of ICPEI is shown as non-controlling interest in these financial statements. Going forward, the purchase will be treated as an equity transaction on April 1, 2021 and the non-controlling interest will be eliminated; the difference between the amount of the non-controlling interest and the purchase price paid plus any transaction costs and liabilities assumed will be recognized in shareholders' equity.

The transaction was financed partly by issuing 2,735,600 common shares of the Company through a non-brokered private placement at a price of $1.42 per Share for $3,885. The Company also entered into a credit facility with National Bank consisting of a $3,000 Term Loan and a $2,000 revolving credit facility. The $3,000 Term Loan was drawn on April 1, 2021 for a term of 3 years with repayment over 10 years. Interest on the facility accrues at the bankers' acceptance rate plus 2%.