

Financial Statements of

**SOUTHEASTERN MUTUAL
INSURANCE COMPANY**

And Independent Auditors' Report thereon

Year ended December 31, 2020

SOUTHEASTERN MUTUAL INSURANCE COMPANY

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Year ended December 31, 2020

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INDEPENDENT AUDITORS' REPORT

To the Policyholders of Southeastern Mutual Insurance Company

Opinion

We have audited the financial statements of Southeastern Mutual Insurance Company (the Company), which comprise:

- the statement of financial position as at December 31, 2020
- the statement of income for the year then ended
- the statement of comprehensive income for the year then ended
- the statement of changes in equity for the year then ended
- the statement of cash flows for the year then ended
- the schedule of operating expenses for the year then ended
- and notes to the financial statements, including a summary of significant accounting policies

(Hereinafter referred to as the “financial statements”).

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2020, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for Opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the “***Auditors’ Responsibilities for the Audit of the Financial Statements***” section of our auditors’ report.

We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.



Other Matter – Comparative Information

The financial statements as at and for the year ended December 31, 2019 were audited by another auditor who expressed an unmodified opinion on those financial statements on March 10, 2020.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit.

We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.



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The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

A handwritten signature in black ink that reads 'KPMG LLP'. The signature is written in a cursive, slightly slanted style. Below the signature is a horizontal line that starts under the 'K' and ends under the 'P', with a small upward tick at the end.

Chartered Professional Accountants

Moncton, Canada

April 7, 2021

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Statement of Financial Position

December 31, 2020, with comparative information for 2019

	2020	2019
Assets		
Cash and cash equivalents	\$ 2,358,456	\$ 1,605,858
Accrued interest receivable	78,200	77,200
Premiums receivable	3,973,307	2,869,304
Income taxes recoverable	—	347,527
Deferred premium acquisition costs (note 4)	1,662,119	1,219,010
Reinsurers' shares of unpaid claims and adjustment expenses (note 4)	524,784	1,580,950
Investments (note 5)	21,324,963	18,694,673
Property and equipment (note 6)	1,438,401	1,522,520
Intangible asset (note 7)	314,706	354,437
Held in trust (note 8)	407,725	531,160
Prepaid expenses	64,127	29,987
	\$ 32,146,788	\$ 28,832,626

Liabilities

Accounts payable and accrued liabilities (note 9)	\$ 1,082,407	\$ 644,699
Income taxes payable	822,710	—
Unearned premiums (note 4)	8,717,799	6,468,728
Provision for unpaid claims (note 4)	1,642,329	3,951,130
Mortgage payable (note 11)	1,031,917	1,092,917
Deferred income taxes (note 10)	104,706	79,338
	13,401,868	12,236,812
Equity:		
Policyholders' equity	16,782,207	15,025,636
Accumulated other comprehensive income	1,962,713	1,570,178
	18,744,920	16,595,814
Subsequent event (note 8)		
	\$ 32,146,788	\$ 28,832,626

See accompanying notes to financial statements.

On behalf of the Board:

Director

Director

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Statement of Income

Year ended December 31, 2020, with comparative information for 2019

	2020	2019
Premiums written	\$ 16,011,009	\$ 12,050,488
Reinsurance premiums paid	(1,992,521)	(1,377,100)
Change in unearned premiums (note 4)	(2,249,071)	(1,030,350)
Net premiums earned	11,769,417	9,643,038
Service charge revenue	269,390	234,325
Underwriting revenue	12,038,807	9,877,363
Claims:		
Claims incurred	4,433,806	6,736,567
Adjusting expenses	584,712	606,776
Reinsurance recoveries	(474,618)	(1,507,926)
Net claims and adjustment expenses incurred (note 4)	4,543,900	5,835,417
	7,494,907	4,041,946
Premium acquisition expenses:		
Commissions paid	2,374,278	1,740,356
Change in commissions earned	(363,231)	(185,426)
Net commission expenses	2,011,047	1,554,930
Agent expenses	201,891	53,570
Agent benefits	171,503	167,076
Premium tax	413,807	347,372
Fire Marshall's tax	95,769	92,612
Other premium acquisition costs	48,299	36,473
	2,942,316	2,252,033
Operating expenses (schedule)	2,574,028	2,758,118
	5,516,344	5,010,151
Underwriting income (loss)	1,978,563	(968,205)
Investment and other income (expense):		
Loss on sale of associate	—	(199,392)
Investment income (note 13)	471,848	476,808
Rental income (loss) net of expenses (note 13)	6,951	(99)
	478,799	277,317
Income (loss) before income taxes	2,457,362	(690,888)
Income taxes (note 10)		
Current (recovery)	675,423	(453,351)
Deferred	25,368	249,000
	700,791	(204,351)
Net income (loss)	\$ 1,756,571	\$ (486,537)

See accompanying notes to financial statements.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Statement of Comprehensive Income

Year ended December 31, 2020, with comparative information for 2019

	2020	2019
Net income (loss)	\$ 1,756,571	\$ (486,537)
Other comprehensive income (loss) subject to reclassification:		
Unrealized gain (loss) on available-for-sale financial assets:		
Equities and preferred shares	326,574	696,986
Bonds and debentures	308,278	(16,757)
	<u>634,852</u>	<u>680,229</u>
Reclassification of realized gain (loss) on available for sale financial assets to net income:		
Equities and preferred shares	(55,431)	76,843
Bonds and debentures	–	(79,730)
	<u>(55,431)</u>	<u>(2,887)</u>
Other comprehensive income from associate	–	81,155
Net unrealized gain	<u>579,421</u>	<u>758,497</u>
Current income tax (note 10)	186,886	193,000
Other comprehensive income	<u>392,535</u>	<u>565,497</u>
Total comprehensive income	<u>\$ 2,149,106</u>	<u>\$ 78,960</u>

See accompanying notes to financial statements.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Statement of Changes in Equity

Year ended December 31, 2020, with comparative information for 2019

	2020	2019
Policyholders' equity :		
Balance, beginning of year	\$ 15,025,636	\$ 15,512,173
Net income (loss)	1,756,571	(486,537)
Balance, end of year	16,782,207	15,025,636
Accumulated other comprehensive income:		
Balance, beginning of year	1,570,178	1,004,681
Other comprehensive income	392,535	565,497
Balance, end of year	1,962,713	1,570,178
Total equity	\$ 18,744,920	\$ 16,595,814

Accumulated other comprehensive income ("AOCI") is composed of unrealized gains on available-for-sale financial assets, net of income taxes of \$1,962,713 (2019 - \$1,570,178).

See accompanying notes to financial statements.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Statement of Cash Flows

Year ended December 31, 2020, with comparative information for 2019

	2020	2019
Operating activities:		
Net income (loss)	\$ 1,756,571	\$ (486,537)
Adjustments for:		
Depreciation and amortization	169,895	166,166
Interest on mortgage	32,511	32,774
Current income tax expense	675,423	(453,351)
Deferred income tax expense	25,368	249,000
Gain on disposal of investments	(56,939)	(26,755)
Amortization of bond premiums	66,102	21,045
Interest received	(326,767)	(328,865)
Dividends received	(154,244)	(142,233)
Loss on sale of associate	-	199,392
	2,187,920	(769,364)
Changes in non-cash balances:		
Accrued interest receivable	(1,000)	(16,000)
Premiums receivable	(1,104,003)	(570,796)
Deferred premium acquisition costs	(443,109)	(230,729)
Reinsurers' unpaid claims and adjustment expenses	1,056,166	(1,490,304)
Prepaid expenses	(34,140)	510,241
Accounts payable and accrued liabilities	437,708	250,710
Unearned premiums	2,249,071	1,030,350
Provision for unpaid claims	(2,308,801)	2,461,827
	2,039,812	1,175,935
Interest received	326,767	328,865
Dividends received	154,244	142,233
Income taxes received (paid)	307,928	(54,041)
Cash provided by operating activities	2,828,751	1,592,992
Financing activities:		
Payments on mortgage payable	(61,000)	(61,000)
Interest paid	(32,511)	(32,774)
Cash used in financing activities	(93,511)	(93,774)
Investing activities:		
Purchase of property, equipment and intangible assets	(46,045)	(585,870)
Proceeds from sale of investments	7,351,700	4,986,448
Purchase of investments	(9,411,732)	(8,593,981)
Proceeds on sale of associate	123,435	2,788,603
Cash used in investing activities	(1,982,642)	(1,404,800)
Increase in cash and cash equivalents	752,598	94,418
Cash and cash equivalents, beginning of year	1,605,858	1,511,440
Cash and cash equivalents, end of year	\$ 2,358,456	\$ 1,605,858

See accompanying notes to financial statements.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Schedule of Operating Expenses

Year ended December 31, 2020, with comparative information for 2019

	2020	2019
Advertising and donations	\$ 96,916	\$ 147,409
Association fees and memberships	19,827	14,196
Conventions and meetings	9,217	22,918
Depreciation and amortization	153,095	150,149
Directors' remuneration (note 12)	103,306	94,255
Directors' expenses (note 12)	4,001	6,334
Information technology	469,973	612,971
Insurance and bonding	39,296	11,550
Interest and bank charges	61,195	59,841
Interest on mortgage	32,511	32,774
Loss prevention	72,580	99,573
Occupancy	80,743	93,222
Office, postage and stationary	64,327	76,516
Professional fees	155,242	86,929
Salaries and employee benefits	1,173,576	1,152,979
Scholarship	6,000	6,000
Telephone	21,060	19,402
Training and education	5,616	13,199
Travel	5,547	57,901
	<u>\$ 2,574,028</u>	<u>\$ 2,758,118</u>

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements

Year ended December 31, 2020

Southeastern Mutual Insurance Company (the "Company") is incorporated under the laws of New Brunswick and is subject to the Insurance Act of New Brunswick. The Company sells property and casualty insurance in New Brunswick (the "Province"). Products include personal, commercial and farm insurance. The Company's head office is located in Riverview, New Brunswick.

1. Basis of presentation:

(a) Statement of compliance:

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

The financial statements were approved by the Board of Directors on April 7, 2021.

(b) Basis of measurement:

The financial statements have been prepared on a historical cost basis, except for the available-for-sale financial assets which are measured at fair value.

(c) Functional and presentation currency:

These financial statements are presented in Canadian dollars, which is the Company's functional currency.

(d) Use of estimates and judgments:

The preparation of the financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, revenue and expenses. Actual results may differ from those estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the year in which the estimates are revised and in any future periods affected.

Information about critical judgments in applying accounting policies that have the most significant effect on amounts recognized in the financial statements is discussed in note 3.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements

Year ended December 31, 2020

2. Significant accounting policies:

The accounting policies set out below have been applied consistently to all periods presented in these financial statements, unless otherwise indicated.

(a) Financial instruments

The Company's financial instruments are classified into one of the following four categories, as defined below

- Financial assets at fair value through profit or loss ("FVTPL")
- Available-for-sale ("AFS")
- Loans and receivables
- Other financial liabilities

All financial instruments are initially recognized at fair value and are subsequently accounted for based on their classification as described below. The classification depends on the purpose for which the financial instruments were acquired and their characteristics. Instruments classified as FVTPL may never be reclassified and, except in very limited circumstances, the classification of other instruments is not changed subsequent to initial recognition. Financial assets purchased and sold, where the contract requires the asset to be delivered within an established time frame, are recognized on a settlement date basis.

Transaction costs are expensed as incurred for FVTPL financial instruments. For other financial instruments, transaction costs are capitalized on initial recognition. The effective interest method of amortization is used for any transaction costs capitalized on initial recognition and for the premiums or discounts earned on AFS investments.

The fair value of a financial instrument on initial recognition is normally the transaction price, i.e. the fair value of the consideration given or received. Subsequent to initial recognition, the fair values are determined based on available information. The fair values of investments are based on the quoted market prices at bid. Unless otherwise disclosed, the carrying values of financial instruments approximate their fair values.

(i) Financial assets at fair value through profit or loss ("FVTPL")

A financial asset is classified as FVTPL if it was classified as held-for-trading or is designated as such upon initial recognition. FVTPL financial assets are purchased with the intention of generating profits in the near term or are voluntarily so designated by the Company. Changes in fair values are recorded as unrealized gain (loss) on financial assets at fair value through profit or loss in the statement of income with the related tax impact included in the current and deferred tax line items.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

2. Significant accounting policies:

(b) Financial instruments (continued)

(ii) Available-for-sale (“AFS”)

Changes in fair values are recorded, net of income taxes, in other comprehensive income (“OCI”) in the statement of comprehensive income until the financial instrument is disposed of, or where there has been a significant or prolonged decline in the fair value of an AFS financial asset. When the instrument is disposed of, the gain or loss is reclassified from OCI to realized gain (loss) in the statement of income. Gains and losses on the sale of AFS financial instruments are calculated on an average cost basis.

(iii) Loans and receivables

Financial instruments classified as loans and receivables are carried at amortized cost using the effective interest rate method. When there is a significant or prolonged decline in value, the value of these financial instruments is written down to the estimated net realizable value.

(iv) Financial liabilities

Financial liabilities are recognized initially on the trade date at which the Company becomes party to the contractual provisions of the instrument. The Company derecognizes a financial liability when its contractual obligations are discharged or cancelled or expire.

(c) Investment income and expenses

Interest income from fixed income securities is recognized on an accrual basis using the effective interest rate method and reported within investment income.

Dividends on equity investments are recognized when the shareholder's right to receive payment is established, which is the ex-dividend date, and are reported within investment income.

General investment expenses are recognized as incurred.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

2. Significant accounting policies (continued):

(d) Impairment

(i) Financial assets

A financial asset not carried at FVTPL is assessed at each reporting date to determine whether there is objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

Factors considered in determining whether a loss is significant or prolonged include the duration and extent to which fair value has been below cost, financial condition and near-term prospects of the issuer, and the Company's ability and intent to hold the investment for a period of time sufficient to allow for any anticipated recovery.

If an AFS investment becomes impaired, the loss is reclassified from OCI to realized gain (loss) in the statement of income.

The cumulative loss that is removed from accumulated other comprehensive income and recognized in income is the difference between the acquisition cost, net of any principal repayment and amortization, and the current fair value, less any impairment loss previously recognized in income.

If, in a subsequent period, the fair value of an impaired AFS debt security increases and the increase can be related objectively to an event occurring after the impairment loss was recognized in income, then the impairment loss is reversed, with the amount of the reversal recognized in income.

The Company considers evidence of impairment for receivables at both a specific asset and collective level. All individually significant receivables are assessed for specific impairment. Receivables that are not individually significant are collectively assessed for impairment. In assessing collective impairment, the Company uses historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgment as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical trends.

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognized in income and reflected in an allowance account against receivables. Interest on the impaired asset continues to be recognized through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through income.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

2. Significant accounting policies (continued):

(d) Impairment (continued)

(ii) Non-financial assets

The carrying amounts of the Company's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. An impairment loss is recognized if the carrying amount of an asset exceeds its estimated recoverable amount.

The recoverable amount of an asset is the greater of its value in use and its fair value less expected selling costs. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Impairment losses are recognized in income in the period in which the impairment is determined.

(e) Cash and cash equivalents

Cash and cash equivalents are comprised of cash on hand, balances with banks and highly liquid temporary investments which are readily convertible into cash and which are subject to insignificant risk of changes in value.

(f) Property and equipment

(i) Recognition and measurement

Property and equipment are recorded at cost or deemed cost less accumulated amortization and any recognized impairment loss plus subsequent additions. Cost includes expenditures that are directly attributable to the acquisition of the asset.

Gains and losses on disposals of property and equipment are determined by comparing the proceeds with the carrying amount of the item disposed and are recognized on a net basis within income.

(ii) Subsequent costs

The cost of replacing a part of an item of property and equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Company, and its cost can be measured reliably. The carrying amount of the replaced part is derecognized. The costs of the day-to-day maintenance and repairs are expensed as incurred.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

2. Significant accounting policies (continued):

(f) Property and equipment (continued)

(iii) Depreciation

Depreciation is recognized in net income and is amortized on a straight-line basis over the estimated useful life of the assets as follows:

Building	2.5% to 10%
Furniture and fixtures	10%
Computer hardware	17%
Vehicles	20%

Depreciation methods, useful lives and residual values are reviewed periodically and adjusted if necessary.

(g) Intangible assets

Intangible assets consist of computer software which is not integral to the computer hardware owned by the Company. Software is recorded at cost less accumulated amortization and accumulated impairment losses. Software is amortized on a straight-line basis over its estimated useful life of 3 to 12 years. The amortization expense is included within the operating expenses in the statement of income.

(h) Insurance contracts

(i) Classification

Insurance contracts are those contracts that transfer significant insurance risk at the inception of the contract. Insurance risk arises when the Company agrees to compensate the policyholder if a specified uncertain future event adversely affects the policyholder. Contracts not meeting the definition of insurance contracts are classified as investment contracts, derivative contracts or service contracts. The Company has reviewed all the contracts issued to its policyholders and concluded that they all meet the definition of insurance contracts.

Premiums are taken into income on a pro rata basis over the contract period. Premiums on policies written with monthly payment terms are accounted for on an annualized basis. Premiums related to the unexpired portion of the policy at the end of the fiscal year are reflected in unearned premiums. Premiums receivable represents the premiums due for the remaining months of the contracts. The Company records a liability for the unearned portion of premiums.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

2. Significant accounting policies (continued):

(h) Insurance contracts (continued)

(iii) Deferred premium acquisition costs

Commissions and premium taxes related to securing new insurance contracts and renewing existing insurance contracts are deferred to the extent they are considered recoverable. All other costs are recognized as expenses when incurred. The deferred premium acquisition costs are subsequently amortized over the terms of the related policies. To the extent they are considered non-recoverable, they are expensed as incurred.

(iv) Provision for unpaid claims and adjustment expenses

The provision for unpaid claims consists of case estimates prepared by claims adjusters and a provision for incurred but not reported claims ("IBNR"). The estimates include related investigation, settlement and adjustment expenses. The valuation of claims liabilities is measured on a non-discounted basis.

(v) Liability adequacy test

At the end of each reporting period, the Company performs a liability adequacy test on its insurance liabilities less deferred premium acquisition costs to ensure the carrying value is adequate. In performing these tests, current best estimates of future contractual cash flows and claims handling and administration expenses, as well as investment income from the assets backing such liabilities are used. Any deficiency is immediately charged to income initially by writing off deferred premium acquisition costs and by subsequently establishing a provision for losses arising from liability adequacy tests (the "premium deficiency"). Impairment losses resulting from liability inadequacy can be reversed in future years if the impairment no longer exists.

(vi) Reinsurance contracts held

Contracts entered into by the Company with the reinsurer under which the Company is compensated for losses on one or more contracts issued by the Company and that meet the classification requirements for insurance contracts are classified as reinsurance contracts held.

Reinsurance does not relieve the Company of its liability to its policyholders and is reflected on the statement of financial position on a gross basis to indicate the extent of credit risk related to reinsurance and the obligations to policyholders.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

2. Significant accounting policies (continued):

(h) Insurance contracts (continued)

(vi) Reinsurance contracts held (continued)

The benefits to which the Company is entitled under its reinsurance contracts held are recognized as amounts recoverable from reinsurer (reinsurance asset). These assets consist of short-term balances due from reinsurer, as well as longer term receivables that are dependent on the expected claims and benefits arising under the related reinsured insurance contracts. Amounts recoverable from reinsurer are measured consistently with the amounts associated with the reinsured insurance contracts and in accordance with the terms of each reinsurance contract.

The Company assesses its reinsurance assets for impairment on a yearly basis. If there is objective evidence that the amount recoverable is impaired, the Company reduces the carrying amount of the reinsurance asset to its recoverable amount and recognizes that impairment loss in the statement of income. The carrying amount is reduced through the use of an allowance account.

(i) Income taxes

Income tax expense comprises current and deferred taxes. Current tax and deferred tax are recognized in income except to the extent that it relates to items recognized directly in equity or in OCI.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to taxes payable in respect of previous years.

Deferred tax is a result of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amount used for tax purposes. Deferred tax assets are recognized only to the extent it is probable that sufficient taxable profits will be available against which the benefit of these deferred tax assets can be utilized.

Deferred tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Changes in deferred income taxes related to a change in tax rates are recognized in income in the period in which the tax change was enacted or substantively enacted.

Deferred income tax assets and liabilities are offset when they arise from the same taxation authority and the Company has both the legal right and the intention to settle on a net basis or to realize the asset and settle the liability simultaneously.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

2. Significant accounting policies (continued):

(k) Future changes in accounting policies

(i) IFRS 17, *Insurance Contracts*

On May 18, 2017 the IASB issued IFRS 17 Insurance Contracts. On June 25, 2020, the IASB issued amendments to IFRS 17 aimed at helping companies implement the Standard and to defer the effective date. IFRS 17 will replace IFRS 4 Insurance Contracts. The new standard and its amendments are effective for annual periods beginning on or after January 1, 2023.

This Standard introduces consistent accounting for all insurance contracts. The Standard requires a company to measure insurance contracts using updated estimates and assumptions that reflect the timing of cash flows and any uncertainty relating to insurance contracts. Additionally, IFRS 17 requires an entity to recognize profits as it delivers insurance services, rather than when it receives premiums.

The Company intends to adopt IFRS 17 in its financial statements for the annual period beginning on January 1, 2023. The extent of the impact of adoption of the standard has not yet been determined.

(ii) IFRS 9, *Financial Instruments*

In July 2014, the IASB issued the complete amended IFRS 9, Financial Instruments. The mandatory effective date of IFRS 9 is for annual periods beginning on or after January 1, 2019 and must be applied retrospectively with some exemptions. Early adoption is permitted. The restatement of prior periods is not required and is only permitted if information is available without the use of hindsight.

IFRS 9 introduces new requirements for the classification and measurement of financial assets based on the business model in which they are held and the characteristics of their contractual cash flows. It also amends the impairment model by introducing a new 'expected credit loss' model for calculating impairment.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

2. Significant accounting policies (continued):

(k) Future changes in accounting policies (continued)

(ii) IFRS 9, *Financial Instruments (continued)*

The standard also introduces additional changes relating to financial liabilities.

IFRS 9 also includes a new general hedge accounting standard which aligns hedge accounting more closely with risk management. This new standard does not fundamentally change the types of hedging relationships or the requirement to measure and recognize ineffectiveness, however it will provide more hedging strategies that are used for risk management to qualify for hedge accounting and introduce more judgment to assess the effectiveness of a hedging relationship. Special transitional requirements have been set for the application of the new general hedging model.

In September 2016, the IASB issued amendments to IFRS 4, Insurance Contracts to address accounting mismatches and volatility that may arise in profit or loss in the period between the effective date of IFRS 9 and the new insurance contracts standard, IFRS 17 Insurance Contracts, issued in May 2019. The amendments allow insurance entities whose predominant activities are to issue insurance contracts within the scope of IFRS 4, an optional temporary exemption from applying IFRS 9 until the effective date of IFRS 17.

The amendments introduce two approaches that may be adopted by insurers in the period between the effective date of IFRS 9 and IFRS 17:

- overlay approach – an option for all issuers of insurance contracts to reclassify amounts between profit or loss and other comprehensive income for eligible financial assets by removing any additional accounting volatility that may arise from applying IFRS 9; and
- temporary exemption – an optional temporary exemption from IFRS 9 for companies whose activities are predominately connected with insurance. This exemption allows an entity to continue to apply existing financial instrument requirements in IAS 39 to all financial assets until the earlier of the application of IFRS 17 or January 1, 2023.

In June 2020, the IASB extended the IFRS 9 temporary exemption until the earlier of the application of IFRS 17 or January 1, 2023.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

2. Significant accounting policies (continued):

(k) Future changes in accounting policies (continued)

(ii) IFRS 9, *Financial Instruments (continued)*

The Company evaluated its liabilities at December 31, 2015, the prescribed date of assessment under the temporary exemption provisions and concluded that all of the liabilities were predominantly connected with insurance. Approximately 90% of the Company's liabilities at December 31, 2015 are liabilities that arise because the Company issues insurance contracts and fulfils obligations arising from insurance contracts. Additionally, the Company has not previously applied any version of IFRS 9. Therefore, the Company is an eligible insurer that qualifies for optional relief from the application of IFRS 9.

As at January 1, 2018, the Company elected to apply the optional transitional relief under IFRS 4 that permits the deferral of the adoption of IFRS 9 for eligible insurers. The Company will continue to apply IAS 39 until January 1, 2023. See note 5 for additional disclosures which enable comparison between the Company and entities that applied IFRS 9 at January 1, 2019.

3. Significant judgments and estimates:

The Company makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgments are continually evaluated and based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The effect of a change in an accounting estimate is recognized in income in the period of the change, if the change affects that period only; or in the period of the change and future periods, if the change affects both.

(a) Significant judgments

Significant judgments made in applying accounting policies are as follows:

(i) Impairments on AFS financial assets

As of each reporting date, the Company evaluates AFS financial assets in an unrealized loss position for impairment on the basis described in note 2(d).

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

3. Significant judgments and estimates (continued):

(a) Significant judgments (continued)

(i) Impairments on AFS financial assets

For investments in bonds and debentures, evaluation of whether impairment has occurred is based on the Company's best estimate of the cash flows expected to be collected at the individual investment level. The Company considers all available information relevant to the collectability of the investment, including information about past events, current conditions, and reasonable and supportable forecasts. Estimating such cash flows is a quantitative and qualitative process that incorporates information received from third party sources along with certain internal assumptions and judgments regarding the future performance of any underlying collateral for asset-backed securities. Where possible, this data is benchmarked against third party sources.

Impairments for bonds and debentures in an unrealized loss position are deemed to exist when the Company does not expect full recovery of the amortized cost of the investment based on the estimate of cash flows expected to be collected or when the Company intends to sell the investment prior to recovery from its unrealized loss position.

For equity investments, the Company recognizes an impairment loss in the period in which it is determined that an investment has experienced significant or prolonged losses and is not expected to recover to its cost.

There were no write-downs of AFS financial assets in 2020 (2019 - \$nil).

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

3. Significant judgments and estimates (continued):

(b) Estimates

Information about assumptions and estimation uncertainties that have a risk of resulting in material adjustment within the next 12 months are as follows:

(i) Provision for unpaid claims

Determining the reserve for unpaid claims involves an assessment of the future development of the claims. The process takes into account the consistency of the Company's claims handling procedures, the amount of information available, the characteristics of the line of business from which the claim arises, and the delays in reporting of claims. The provision for unpaid claims is an estimate and, as such, is subject to variability, which could be material. Changes to the estimates could result from future events such as receiving additional claim information, changes in judicial interpretations of contracts or significant changes in severity or frequency of claims from past trends. In general, the longer the term required for settlement of a group of claims, the more variable the estimates.

The estimate is principally based on the Company's historical experience. Methods of estimation have been used that the Company believes produce reasonable results given current information. As additional experience and other data become available, the estimates could be revised. Any future changes in estimation would be reflected in the statement of income in the year in which the change occurred.

The assumptions underlying the valuation of the provision for unpaid claims are reviewed and updated by the Company on an ongoing basis to reflect recent and emerging trends in experience and changes in risk profit of the business.

(ii) Deferred premium acquisition costs

Deferred premium acquisition costs are deferred and amortized in accordance with the accounting policy in note 2(h)(iii). The Company estimates expenses eligible for deferral based on the nature of expenses incurred.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

4. Insurance contracts:

Deferred premium acquisition costs

The following is a schedule of the changes in deferred premium acquisition costs for the year:

	2020	2019
Balance, beginning of year	\$ 1,219,010	\$ 988,280
Acquisition costs incurred during the year	3,385,425	2,482,763
Expensed during the year	(2,942,316)	(2,252,033)
Balance, end of year	\$ 1,662,119	\$ 1,219,010

Unearned premiums

Unearned premiums on the statement of financial position consist of the unearned portions of premiums. The following is a schedule of the changes in the above for the year:

	2020	2019
Balance, beginning of year	\$ 6,468,728	\$ 5,438,378
Premiums written in year	16,011,009	12,050,488
Premiums earned in year	(13,761,938)	(11,020,138)
Change in year	2,249,071	1,030,350
Balance, end of year	\$ 8,717,799	\$ 6,468,728

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

4. Insurance contracts (continued):

Provision for unpaid claims

Changes in claim liabilities recorded in the statement of financial position for the years ended December 31, 2020 and 2019 and their impact on claims and adjustment expenses for the two years is as follows:

2020	Insurance contract liabilities	Reinsurance of liabilities	Net
Unpaid claims, beginning of year	\$ 3,951,130	\$ 1,580,950	\$ 2,370,180
Change in provision for insured events of prior years	(871,307)	(405,540)	(465,767)
Provision for insured events of current year	5,889,825	880,158	5,009,667
	5,018,518	474,618	4,543,900
Net payments attributable to:			
Prior events	2,867,550	1,064,317	1,803,233
Current year events	4,459,769	466,467	3,993,302
	7,327,319	1,530,784	5,796,535
Unpaid claims, end of year	\$ 1,642,329	\$ 524,784	\$ 1,117,545

2019	Insurance contract liabilities	Reinsurance of liabilities	Net
Unpaid claims, beginning of year	\$ 1,489,303	\$ 90,646	\$ 1,398,657
Change in provision for insured events of prior years	25,303	52,853	(27,550)
Provision for insured events of current year	7,318,040	1,455,073	5,862,967
	7,343,343	1,507,926	5,835,417
Net payments attributable to:			
Prior events	1,010,102	17,622	992,480
Current year events	3,871,414	—	3,871,414
	4,881,516	17,622	4,863,894
Unpaid claims, end of year	\$ 3,951,130	\$ 1,580,950	\$ 2,370,180

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

4. Insurance contracts (continued):

Provision for unpaid claims (continued)

The Company has determined estimated settlements in the next fiscal year on the provision for unpaid claims noted above to be \$1,019,000 (2019 - \$2,174,000). This estimate was determined through the use of historical data on claims payments year over year.

Claims development

The estimation of claim development involves assessing the future behavior of claims, taking into account the consistency of the Company's claim handling procedures, the amount of information available, the characteristics of the line of business from which the claim arises and historical delays in reporting claims. In general, the longer the term required for settlement of a group of claims the more variable the estimates. Short-term settlement claims are those which are expected to be substantially paid within a year of being reported.

The tables below present the development of claim payments and the estimated total cost of claims for the years 2011 to 2020 on a gross and net claims basis. The upper half of the table shows the cumulative amounts paid or estimated to be paid during successive years related to each claim year.

The original estimates will be increased or decreased, as more information becomes known about the original claims and overall claim frequency and severity.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

4. Insurance contracts (continued):

Provision for unpaid claims (continued)

Claims Development

Gross Claims	(\$'000)											
	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Total	
Net estimate of cumulative claims cost												
At the end year of claim	\$ 2,969	\$ 2,152	\$ 2,550	\$ 2,879	\$ 3,630	\$ 2,970	\$ 4,433	\$ 5,123	\$ 7,157	\$ 5,895		
One year later	3,057	2,114	2,567	2,806	3,444	2,942	4,203	5,111	6,420			
Two years later	3,022	2,119	2,591	2,803	3,426	2,998	4,255	5,016				
Three years later	3,031	2,086	2,580	2,768	3,468	3,003	4,205					
Four years later	3,034	2,086	2,580	2,768	3,447	2,954						
Current estimate of cumulative claim costs	3,034	2,086	2,580	2,768	3,447	2,954	4,205	5,016	6,420	5,895	38,405	
Cumulative payments	3,034	2,086	2,580	2,768	3,447	2,942	4,115	4,925	6,406	4,460	36,763	
Outstanding claims	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 12	\$ 90	\$ 91	\$ 14	\$ 1,435	\$ 1,642	

Claims Net of Reinsurance	(\$'000)											
	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Total	
Net estimate of cumulative claims cost												
At the end year of claim	\$ 2,519	\$ 2,135	\$ 2,358	\$ 2,879	\$ 3,423	\$ 2,743	\$ 4,205	\$ 4,858	\$ 5,702	\$ 4,980		
One year later	2,444	2,037	2,290	2,806	3,289	2,791	4,099	4,794	5,860			
Two years later	2,406	2,043	2,314	2,803	3,271	2,826	4,151	4,706				
Three years later	2,408	2,010	2,314	2,768	3,312	2,831	4,101					
Four years later	2,415	2,010	2,314	2,768	3,291	2,782						
Current estimate of cumulative claim costs	2,415	2,010	2,314	2,768	3,291	2,782	4,101	4,706	5,860	4,980	35,227	
Cumulative payments	2,415	2,010	2,314	2,768	3,291	2,770	4,012	4,703	5,847	3,979	34,109	
Outstanding claims	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 12	\$ 89	\$ 3	\$ 13	\$ 1,001	\$ 1,118	

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

5. Investments:

(a) Investments are classified on an available-for-sale basis, and therefore are carried at their fair value.

	2020	2019
Available-for-Sale		
Bonds and debentures maturing within one year:		
Provincial/Municipal Governments	\$ 654,719	\$ 336,233
Canadian Corporate	955,931	2,724,456
	<u>1,610,650</u>	<u>3,060,689</u>
Bonds and debentures maturing between one and five years:		
Provincial/Municipal Governments	2,618,313	2,233,760
Canadian Corporate	5,708,877	3,754,177
	<u>8,327,190</u>	<u>5,987,937</u>
Bonds and debentures maturing in more than five years:		
Provincial/Municipal Governments	1,158,638	255,412
Canadian Corporate	977,123	1,439,145
	<u>2,135,761</u>	<u>1,694,557</u>
Total bonds and debentures	12,073,601	10,743,183
Equities	6,954,591	4,525,349
Preferred shares	1,548,673	1,278,044
Short term investments	748,098	2,148,097
	<u>\$ 21,324,963</u>	<u>\$ 18,694,673</u>

The Company's effective interest rate on bonds and debentures is calculated based on interest received and accrued in the year less amortization of bond premiums in the year. The effective interest rate on these investments is 2.97% (2019 - 2.89%).

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

5. Investments (continued):

(b) Additional disclosures

The following additional disclosure, required by IFRS 9 for eligible insurers, presents the fair value and the amount of change in the fair value of the Company's financial assets, showing separately the fair value of financial assets with contractual terms that give rise to cash flows that are solely payments of principal and interest on the principal amount outstanding ("SPPI") and the fair value of financial assets that do not give rise to cash flows that are solely payments of principal and interest on the principal amount outstanding ("Non-SPPI"):

2020	SPPI		Non-SPPI	
	Fair Value	Change in fair value	Fair value	Change in fair value
Bonds and debentures	\$12,073,601	\$ 308,278	\$ –	\$ –
Equities	–	–	6,954,591	209,291
Preferred shares	1,548,673	117,283	–	–
Short-term investments	–	–	748,098	–
	\$13,622,274	\$ 425,561	\$ 7,702,689	\$ 209,291

2019	SPPI		Non-SPPI	
	Fair Value	Change in fair value	Fair value	Change in fair value
Bonds and debentures	\$10,743,183	\$ (16,757)	\$ –	\$ –
Equities	–	–	4,525,349	632,133
Preferred shares	1,278,044	64,853	–	–
Short-term investments	–	–	2,148,097	–
	\$12,021,227	\$ 48,096	\$ 6,673,446	\$ 632,133

The additional disclosure, required by IFRS 9 for eligible insurers, to present the credit risk ratings of SPPI financial assets is included in note 15 (b).

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

6. Property and equipment:

	Land	Building	Furniture and fixtures	Computer hardware	Vehicles	Total
Cost or deemed cost						
Balance December 31, 2019	\$ 338,000	\$ 1,143,174	\$ 203,025	\$ 388,024	\$ 30,798	\$ 2,103,021
Additions	–	19,377	3,901	18,484	–	41,762
Balance December 31, 2020	338,000	1,162,551	206,926	406,508	30,798	2,144,783
Accumulated depreciation						
Balance December 31, 2019	–	224,485	131,082	209,534	15,400	580,501
Additions	–	57,930	11,667	50,128	6,156	125,881
Balance December 31, 2020	–	282,415	142,749	259,662	21,556	706,382
Net book value, December 31, 2020	\$ 338,000	\$ 880,136	\$ 64,177	\$ 146,846	\$ 9,242	\$ 1,438,401

	Land	Building	Furniture and fixtures	Computer hardware	Vehicles	Total
Cost or deemed cost						
Balance December 31, 2018	\$ 338,000	\$ 969,226	\$ 170,313	\$ 363,935	\$ 30,798	\$ 1,872,272
Additions	–	173,948	32,712	24,089	–	230,749
Balance December 31, 2019	338,000	1,143,174	203,025	388,024	30,798	2,103,021
Accumulated depreciation						
Balance December 31, 2018	–	169,256	120,901	158,570	9,240	457,967
Additions	–	55,229	10,181	50,964	6,160	122,534
Balance December 31, 2019	–	224,485	131,082	209,534	15,400	580,501
Net book value, December 31, 2019	\$ 338,000	\$ 918,689	\$ 71,943	\$ 178,490	\$ 15,398	\$ 1,522,520

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

7. Intangible assets:

	Computer software	
Cost		
Balance, December 31, 2019	\$	510,446
Additions		4,283
Balance, December 31, 2020		514,729
Accumulated amortization		
Balance, December 31, 2019		156,009
Amortization for the year		44,014
Balance, December 31, 2020		200,023
Net book value		
Balance, December 31, 2019		354,437
Balance, December 31, 2020		314,706

Amortization of intangible assets included in operating expenses amounted to \$43,632 in 2020 (2019 - \$44,014).

8. Held in trust:

On January 1, 2019, the Company sold its interest in United General Insurance Corporation for net proceeds in the amount of \$3,319,763. As part of the sale, legal counsel has held back a portion of the proceeds from the sale. This holdback is included in the statement of financial position as funds Held in Trust. The holdback was paid out in full on January 12, 2021.

9. Accounts payable and accrued liabilities:

	2020	2019
Payable to reinsurer	\$ 438,526	\$ 146,586
Premium and fire marshal taxes payable	320,510	217,639
Due to other government agencies	7,498	7,337
Other payables and accruals	315,873	273,137
	\$ 1,082,407	\$ 644,699

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

10. Income taxes:

(a) Recognized deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

2020	Assets	Liabilities	Net
Property and equipment	\$ –	\$ (136,286)	\$ (136,286)
Claim reserves	16,413	–	16,413
Other	15,167	–	15,167
Net tax assets (liabilities)	\$ 31,580	\$ (136,286)	\$ (104,706)

2019	Assets	Liabilities	Net
Property and equipment	\$ –	\$ (118,215)	\$ (118,215)
Claim reserves	29,627	–	29,627
Other items	9,250	–	9,250
Net tax assets (liabilities)	\$ 38,877	\$ (118,215)	\$ (79,338)

(b) Movement in temporary differences during the year

	Property and equipment	Claim reserves	Other items	Safe income gain	Total
Balance, December 31, 2018	\$ (29,793)	\$ 17,595	\$ 7,500	\$ 174,360	\$ 169,662
Recognized in income	(88,422)	12,032	1,750	(174,360)	(249,000)
Balance, December 31, 2019	(118,215)	29,627	9,250	–	(79,338)
Recognized in income	(18,071)	(13,214)	5,917	–	(25,368)
Balance, December 31, 2020	\$(136,286)	\$ 16,413	\$ 15,167	\$ –	\$(104,706)

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

10. Income taxes (continued):

(c) Components of income tax expense

The major components of income tax expense are:

	2020	2019
Current tax expense		
Current (recovery) period taxes on income	\$ 673,552	\$ (453,351)
Adjustments for prior years	1,871	–
Deferred tax expense		
Origination and reversal of temporary differences	(562)	249,000
Adjustments for prior years	25,930	–
Total income tax expense (recovery)	\$ 700,791	\$ (204,351)
Income tax recognized in other comprehensive income		
Unrealized gain (loss) on AFS financial assets	\$ 186,886	\$ 193,000
Total income tax charged directly to OCI	\$ 186,886	\$ 193,000

(d) Reconciliation of effective tax rate

The Company's provision for income taxes varies from the expected provision at statutory rates for the following reasons:

	2020	2019
Income (loss) before income taxes	\$ 2,457,362	\$ (690,888)
Combined basic Canadian federal and provincial income tax rate	29%	29%
Provision based on combined basis income tax rate	712,635	(200,358)
Adjustments for prior years	27,801	(10,118)
Permanent items and other	153	41,673
Non-taxable dividends	(39,798)	(35,548)
Income tax expense (recovery)	\$ 700,791	\$ (204,351)
Current income tax	\$ 675,423	\$ (453,351)
Deferred income tax	25,368	249,000
	\$ 700,791	\$ (204,351)

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

11. Mortgage payable:

The Company has a mortgage payable with Canadian Imperial Bank of Commerce repayable in monthly installments of \$5,083 plus interest at a rate of CIBC prime plus 0.15% per annum, totaling of 2.60% at December 31, 2020. The mortgage is secured by a Security Agreement and land and building located at 663 Pinewood Road which has a net book value of \$1,218,133. The mortgage is due on demand. The due date set in the mortgage is May 31, 2021.

The anticipated principal payments on the mortgage payable for each of the five years subsequent to December 31, 2020 are as follows:

2021	\$	61,000
2022		61,000
2023		61,000
2024		61,000
2025		61,000

12. Related party transactions:

The Company entered into the following transactions with key management personnel. Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company, including all directors, executives, and non-executive senior management.

	2020	2019
Key management remuneration	\$ 799,455	\$ 612,268

Included in the statement of income are the following items relating to key management:

	2020	2019
Property and liability insurance premiums received	\$ 10,265	\$ 9,123
Property and liabilities insurance claims incurred	—	7,534

Each director of the Company received an annual stipend in 2020 of \$7,708 per director, \$15,010 for the chair (2019 - \$7,708 per director, \$15,010 for the chair).

In addition, each director received an attendance fee in 2020 of \$424 for each attendance at board meetings, board committee meetings and various industry events.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

12. Related party transactions (continued):

The total compensation paid and expenses reimbursed to each director in respect of 2020 and 2019 was as follows:

	Annual stipend	Attendance fees – Board and committee meetings	Total compensation per Director	Courses, conferences, and mileage	Total compensation and expenses per Director
Kevin Burdett					
2020	\$ 7,708	\$ 9,149	\$ 16,857	\$ 709	\$ 17,566
2019	7,708	6,996	14,704	2,617	17,321
Jack Low					
2020	7,708	9,093	16,801	607	17,408
2019	7,708	6,360	14,068	–	14,068
James Stark					
2020	7,708	8,726	16,434	828	17,262
2019	7,708	6,784	14,492	520	15,012
Lynn Roy					
2020	5,781	6,417	12,198	217	12,415
2019	7,708	6,784	14,492	75	14,567
Nancy Whipp					
2020	1,927	2,968	4,895	551	5,446
2019	7,708	7,421	15,129	3,122	18,251
Brenda Mackenzie					
2020	5,781	6,181	11,962	424	12,386
2019	–	–	–	–	–
Peter Wright					
2020	15,010	9,149	24,159	665	24,824
2019	15,010	6,360	21,370	–	21,370
Total for all directors					
2020	\$ 51,623	\$ 51,683	\$ 103,306	\$ 4,001	\$ 107,307
2019	\$ 53,550	\$ 40,705	\$ 94,255	\$ 6,334	\$ 100,589

Each director is provided with coverage under the Blue Cross health insurance plan. These benefits include coverage for Accidental Death and Dismemberment (AD&D).

The directors did not receive any retirement benefits, pension benefits, bonuses, profit sharing benefits, incentive payments. The directors did not receive any discounts on premiums payable to the Company (other than the premium discounts applicable generally to all policyholders).

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

13. Investment and other income:

(a) Investment income:

	2020	2019
Interest from bonds and debentures net of bond amortization	\$ 260,665	\$ 307,820
Dividends	154,244	142,233
Gain on disposal of investments	56,939	26,755
	\$ 471,848	\$ 476,808

(b) Rental income (loss):

	2020	2019
Revenue and common area charges	\$ 60,804	\$ 55,146
Expenses	(37,053)	(39,229)
Depreciation allocated	(16,800)	(16,016)
Rental income (loss)	\$ 6,951	\$ (99)

14. Capital management:

The Company's capital management objective is to ensure the Company is capitalized in a manner that provides a strong financial position for its policyholders, and at the same time exceeds the regulatory capital requirements. Reinsurance is utilized to protect capital from catastrophic losses as the frequency and severity of these losses are inherently unpredictable (note 15(a)).

Government regulators expect the Company to establish an internal target capital ratio above supervisory target capital ratio when applying the Minimum Capital Test (MCT), which measures available capital against required risk-weighted capital. The MCT calculation incorporates operating results, financial position and other factors and includes a calculated amount of capital available. As of December 31, 2020 and 2019, the Company's MCT exceeded the supervisory target capital ratio required by the regulator (150%) as well as the Company's internal target ratio (450%).

Management actively monitors the MCT ratio and the effect that external and internal actions have on the capital base of the Company. In particular, management determines the effect on capital before entering into any significant transactions to ensure that policyholders are not put at risk through the depletion of capital to unacceptable levels.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

14. Capital management (continued):

The following is the detail MCT calculations of the Company:

	2020	2019
Calculated capital available	\$ 18,431,000	\$ 16,241,000
Supervisory target capital required	4,960,000	3,759,000
Internal target capital	14,881,000	11,277,000
Ratio of capital available over supervisory target capital required	372%	432%
Ratio of capital available over internal target capital	124%	144%

15. Risk management, reinsurance and other risks:

The primary goals of the Company's financial risk management are to ensure that the outcomes of activities involving elements of risk are consistent with the Company's objectives and risk tolerance, and to maintain an appropriate risk/reward balance while protecting the Company's statement of financial position from events that have the potential to materially impair its financial strength.

Risks identified as potentially significant are managed through a combination of Board policy, management monitoring and other management practices. The Company's Investment Policy Statement establishes asset mix parameters and risk limits to help minimize undue exposure to these risks in the investment portfolio while attempting to maximize the long-term value of policyholders' equity. The Investment Policy Statement is reviewed annually by the Finance and Audit Committee. Compliance with the Investment Policy is monitored quarterly by the Finance and Audit Committee of the Board of Directors.

The Company's exposure to potential loss is primarily due to insurance risk along with credit risks, liquidity risk, market risks, including foreign currency risks, interest rate risks and equity risks.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

15. Risk management, reinsurance and other risks (continued):

(a) Insurance risk:

Reserve for unpaid claims

The principal risk the Company faces under insurance contracts is the actual claims and liabilities payments or the timing thereof may differ from expectations. This is influenced by the severity of claims, actual claims paid, and subsequent development of long-term claims. Therefore, the objective of the Company is to ensure that sufficient reserves are available to cover these liabilities.

The reserve for unpaid claims and related reinsurer's share is estimates subject to variability and which might be material in the near term. The variability arises because all events affecting the ultimate settlement of claims may not have taken place and may not take place for some time. Variability can be caused by receipt of additional claim information, changes in judicial interpretation of contracts or significant changes in severity or frequency of claims from historical trends. The estimates are principally based on the Company's historical experience. Methods of estimation are used, which the Company believes produce reasonable results given current information. All changes in estimates are recorded as incurred claims in the current period.

The risk is reduced through various internal and external control processes including minimum reserve standards, quality assurance reviews, monthly review, and legal counsel.

Reinsurance and underwriting

The Company mitigates its insurance risk by having in place underwriting guidelines as well as reinsuring insurance contracts which limit the liability of the Company to a maximum amount on any one claim. The Company uses its underwriting guidelines to minimize risk by assessing individual policies, determining if the risk is within the tolerable range and then pricing the policy accordingly.

The current reinsurance contracts are as follows:

Property claims

First \$250,000 per loss is paid by the Company, which limits the Company's exposure in any one property claim to \$250,000. In addition, the Company has obtained reinsurance which limits the Company's liability to \$625,000 in a catastrophe. Stop loss reinsurance is also in effect which protects the Company to limit the "Net Incurred Loss Ratio" to 70% of its insurance premiums.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

15. Risk management, reinsurance and other risks (continued):

(a) Insurance risk (continued):

Liability claims

The Company will pay 100% of all losses, up to a maximum retention of \$250,000 per loss, which limits the Company's exposure in any one liability claim to \$250,000.

The reinsurance of insurance contracts does not relieve the Company's obligation to the policyholders. The Company is exposed to the risk that the reinsurer will be unable to meet its obligations.

The Superintendent of Insurance also limits the Company's maximum retention through its reinsurance arrangements to be the maximum of 2% of general reserve or \$350,000. The Company's allowed maximum retention as of December 31, 2020 would be \$338,000.

Insurance pricing

Pricing risk arises when actual claims experience differs from the assumptions included in pricing calculations. Historically, the underwriting results of the property and casualty industry have fluctuated significantly due to the cyclical nature of the insurance market. The market cycle is affected by the frequency and severity of losses, levels of capacity and demand, general economic conditions and price competition. The Company's pricing process is designed to ensure an appropriate return on capital while also providing long-term rate stability. These factors are reviewed and adjusted regularly to ensure prices are responsive to the current environment and competitor behaviour.

Concentration risk

The Company writes property and casualty insurance contracts for twelve-month durations. The most significant risks arise from natural disasters, climate change and other catastrophes. The Company has a reinsurance program to limit the exposure to catastrophic losses from any one event.

The Company has a concentration of business in property insurance in the Province of New Brunswick. For the year ended December 31, 2020, property premiums represented 100% (2019 - 100%) of gross written premiums. Of gross written premiums in 2020, property premiums accounted for 90% (2019 - 89%).

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

15. Risk management, reinsurance and other risks (continued):

(a) Insurance risk (continued):

Catastrophic loss risk

Catastrophic loss risk is the exposure to losses resulting from multiple claims arising out of a single catastrophic event. Property and casualty insurance companies experience large losses arising from man-made or natural catastrophes that can result in significant underwriting losses. Catastrophes can cause losses in a variety of property and casualty lines and may have continuing effects which could delay or hamper efforts to timely and accurately assess the full extent of the damage they cause. The incidence and severity of catastrophes are inherently unpredictable. The Company evaluates catastrophic events and assesses the probability of occurrence and magnitude of catastrophic events through various modeling techniques and through the aggregation of limits exposed. The Company's exposure to catastrophic loss is also managed through geographic and product diversification as well as through the use of reinsurance.

The Company reinsures claims from a single catastrophe when the sum exceeds \$625,000 (2019 - \$625,000). Reinsurance coverage risk arises because reinsurance terms, conditions and/or pricing may change on renewal, particularly following catastrophes.

Sensitivity analysis

The risks associated with insurance contracts are complex and subject to a number of variables which complicate quantitative sensitivity analysis. The Company's uses various techniques based on past claims development and experience to determine these sensitivities. This includes indicators such as average claim cost, amount of claims occurrence, expected loss ratios and claims development. The Company considers that the liability for its unpaid claims and adjustment expenses is adequate. However, actual experience will differ from the expected outcome.

Reinsurance undertaken

The Company participates in programs to provide re-insurance for crop reinsurance through two separate reinsurance programs. The maximum retained liability for the Company in any one year is \$1,200,000 (2019 - \$1,200,000). For this reinsurance undertaken the Company has recorded \$73,771 (2019 - \$96,646) of premium income included in premiums written.

Property insurance risk

The Company's property and equipment (note 6) is insured for any losses exceeding \$250,000 for each property and liability insurance, which results in a maximum risk of \$500,000. This maximum risk takes into consideration that the Company will be subject to maximum property and liability claims. This policy follows standard reinsurance arrangements as noted above.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

15. Risk management, reinsurance and other risks (continued):

(b) Credit risks:

Credit risk arises from the potential that a counter party will fail to perform its obligations. The Company conducts a thorough assessment of debtors prior to granting credit and actively monitors the financial health of its debtors on an on-going basis. The Company is also exposed to this risk relating to its debt holdings in its investment portfolio, premiums receivable from policyholders and the reliance on reinsurers to make payment when certain loss conditions are met.

The Company's investment policy puts limits on the bond portfolio including portfolio composition limits, issuer type limits, bond quality limits, aggregate issuer limits, corporate sector limits and general guidelines for geographic exposure. All fixed income portfolios are measured for performance on a quarterly basis and monitored by management on a monthly basis. The Company performed a review of all AFS securities with unrealized losses at December 31, 2020 and concluded that, due to no objective evidence of impairment, a provision for impairment was not required.

The Company relies on reinsurance to manage underwriting risk, however, reinsurance does not release the Company from its primary commitments to its policyholders. Therefore, the Company is exposed to the credit risk associated with the amounts ceded to reinsurers.

The Company regularly assesses the financial soundness of the reinsurer it deals with. An allowance for losses on reinsurance contracts is established when a reinsurance counterparty becomes unable or unwilling to fulfill its contractual obligations. The allowance for loss is based on current recoverable and ceded claim liabilities. No information has come to the Company's attention indicating weakness or failure of its current reinsurer; consequently, no impairment provision has been made in the accounts due to credit risks.

The Company's credit exposure to any one individual policyholder included in premiums receivable from policyholders is not material.

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

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

15. Risk management, reinsurance and other risks (continued):

(b) Credit risks (continued):

The following table summarizes the Company's maximum exposure to credit risk related to financial instruments. The maximum credit exposure is the carrying value of the asset net of any allowances for losses:

	2020	2019
Cash and cash equivalents	\$ 2,358,456	\$ 1,605,858
Accrued interest receivable	78,200	77,200
Premiums receivable	3,973,307	2,869,304
Bonds and debentures	12,073,601	10,743,183
Short-term investments	748,098	2,148,097
Held in trust	407,725	531,160
	\$ 19,639,387	\$ 17,974,802

The following additional disclosure, required by IFRS 9 for eligible insurers, presents the credit risk ratings of SPPI financial assets:

2020	Bonds and debentures	Preferred shares	Total	% of total
AAA/PFD-1 (Low)	\$ 137,574	\$ –	\$ 137,574	1%
AA/PFD-2 (Low)	1,644,901	1,490,870	3,135,771	23%
A/PFD-3 (Low)	6,335,087	57,803	6,392,890	47%
BBB/PFD-4 (Low)	770,302	–	770,302	6%
Unrated	3,185,737	–	3,185,737	23%
	\$ 12,073,601	\$ 1,548,673	\$ 13,622,274	100%

2019	Bonds and debentures	Preferred shares	Total	% of total
AAA/PFD-1 (Low)	\$ 235,115	\$ –	\$ 235,115	2%
AA/PFD-2 (Low)	2,097,438	1,249,259	3,346,697	28%
A/PFD-3 (Low)	5,389,210	28,785	5,417,995	45%
BBB/PFD-4 (Low)	1,175,674	–	1,175,674	10%
Unrated	1,845,746	–	1,845,746	15%
	\$ 10,743,183	\$ 1,278,044	\$ 12,021,227	100%

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

15. Risk management, reinsurance and other risks (continued):

(c) Liquidity risks:

Liquidity risk is the risk of having insufficient cash resources to meet current financial obligations. Liquidity risk arises from the Company's general business activities and in the course of managing the assets and liabilities. The liquidity requirements of the Company's business are met primarily by funds generated by operations, asset maturities and investment returns. Cash provided from these sources normally exceeds cash requirements to meet claims costs and operating expenses.

At December 31, 2020, the Company had \$3,106,554 (2019 - \$3,753,955) of cash and cash equivalents. The Company also has a highly liquid investment portfolio. Equities and preferred shares held by the Company had a fair value of \$8,503,264 (2019 - \$5,803,393). Canadian fixed-income securities issued or guaranteed by domestic governments and investment grade corporate bonds held by the Company had a fair value of \$8,887,864 as at December 31, 2020 (2019 - \$8,897,437).

The maturity profile of the Company's investment portfolio is shown in note 5.

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

The Company maintains a line of credit with Canadian Imperial Bank of Commerce in the amount of \$125,000 with an interest rate of prime plus 0.15% (currently 2.60%). The line of credit is secured the same as the mortgage in note 11. At December 31, 2020, the Company's line of credit is available. In addition, the Company has a corporate credit card facility in the amount of \$27,500.

(d) Market risk:

Market risk is the risk of loss arising from adverse changes in market rates and prices, such as foreign currency exchange rates, interest rates, and equity market fluctuations. Market risk is directly influenced by the volatility and liquidity in the markets in which the related underlying assets are traded. Below is a discussion of the Company's primary market risk exposures and how those exposures are currently managed.

Foreign exchange risk

Foreign currency risk is the risk that the fair value or cash flows of a financial instrument will fluctuate because of changes in exchange rates and produce an adverse impact on comprehensive income when measured in the Company's operating currency.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

15. Risk management, reinsurance and other risks (continued):

(d) Market risk (continued):

The Company's foreign currency risk is related to its foreign stock holdings. Foreign currency changes are monitored by the Financial and Audit Committee. Foreign stocks included in the Company's available-for-sale financial assets primarily relate to US dollar denominated equities in the amount of \$3,608,133 (2019 - \$2,357,814) Canadian. A 10% increase or decrease in the value of the US dollar, with all other variables held constant, would increase or decrease comprehensive income by approximately \$270,000 (2019 - \$178,000), net of tax. The Company has not entered into any derivative financial instruments to hedge this currency risk exposure.

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

Interest rate risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate because of changes in market interest rates. The Company is exposed to this risk through its interest-bearing investments. Diversification techniques are utilized to minimize risk. The Company's investment policy sets out guidelines on types and ratings of investments to help minimize this risk. Typically, investment income will be reduced during sustained periods of low interest rates, but this will also create unrealized gains within the bond and debenture portfolio. It will also create realized gains to be recognized in net income to the extent any bonds are sold during the period. The reverse is true during a sustained period of increasing interest rates. At December 31, 2020, an increase or decrease of 1% in interest rates, with all other variables held constant, would increase or decrease the fair values the Company's bond and debentures and OCI by \$423,000.

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

Equity risk

Economic trends, the political environment and other factors can positively and adversely impact the equity markets and consequently the value of equity investments the Company holds. The Company's portfolio includes equities with fair values that move with the changes in stock markets. A 10% movement in the stock markets, with all other variables held constant would change the fair value of the Company's equities and OCI by \$850,000 (2019 - \$580,000).

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

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

16. Fair value of financial instruments:

Fair value hierarchy

The table below provides an analysis of the basis of measurement used to fair value financial instruments carried at fair value, categorized by the following fair value hierarchy:

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities

Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e., derived from prices)

Level 3: Inputs for the asset or liability not based on observable market data (unobservable inputs).

2020	Level 1	Level 2	Level 3	Total
Bonds and debentures				
Provincial / Municipal governments	\$ –	\$ 4,431,670	\$ –	\$ 4,431,670
Canadian corporate	–	7,641,931	–	7,641,931
Equities	6,954,591	–	–	6,954,591
Preferred shares	1,548,673	–	–	1,548,673
Short-term investments	–	748,098	–	748,098
	\$ 8,503,264	\$ 12,821,699	\$ –	\$ 21,324,963

2019	Level 1	Level 2	Level 3	Total
Bonds and debentures				
Provincial / Municipal governments	\$ –	\$ 2,825,405	\$ –	\$ 2,825,405
Canadian corporate	–	7,917,778	–	7,917,778
Equities	4,525,349	–	–	4,525,349
Preferred shares	1,278,044	–	–	1,278,044
Short-term investments	–	2,148,097	–	2,148,097
	\$ 5,803,393	\$ 12,891,280	\$ –	\$ 18,694,673

There were no transfers between Level 1 and Level 2 for the years ended December 31, 2020 and December 31, 2019. There were no Level 3 investments for the years ended December 31, 2020 and December 31, 2019.

SOUTHEASTERN MUTUAL INSURANCE COMPANY

Notes to Financial Statements (continued)

Year ended December 31, 2020

17. Impact of COVID-19:

In March 2020, the global outbreak of the novel coronavirus (COVID-19) was declared a pandemic by the World Health Organization. In response to the outbreak, governmental authorities globally introduced various recommendations and measures to try to limit spread of the pandemic, including non-essential business closures, quarantines, travel restrictions, self-isolation, social and physical distancing and shelter-in-place. These measures caused disruptions to businesses globally resulting in an economic slowdown. During the year ended December 31, 2020, the COVID-19 pandemic did not result in any material impact on the financial results of the Company. The ultimate duration and magnitude of the impact on the economy and consequential financial effect on the Company, is unknown at this time.

18. Comparative information

Certain comparative information has been reclassified to conform with the financial statement presentation adopted in the current year.