



PRINCE EDWARD ISLAND MUTUAL INSURANCE COMPANY 2022 ANNUAL REPORT



NOTICE OF ANNUAL GENERAL MEETING
of the
PRINCE EDWARD ISLAND MUTUAL
INSURANCE COMPANY

The Annual Meeting of the Members of the Prince Edward Island Mutual Insurance Company for the 2022 year will be held at The Oval, above Red Shores at Summerside Raceway, 55 Greenwood Drive, Summerside, PEI on the **11th day of April, 2023, beginning at 2:00 p.m.**

The purpose of the meeting is to receive the financial statements and the auditor's report for 2022; to elect directors; to appoint auditors; and to transact business of the 2022 Annual Meeting.

Please check our website, www.peimutual.com for updates in advance of the Annual Meeting.

A copy of PEI Mutual's Annual Report for 2022 is available on our website or by contacting head office.



Josh Toombs,
Corporate Secretary

PRESIDENT'S REPORT 2022

We have an incredible team at PEI Mutual. We also have a financially stable company and are in a position to serve you, the members, for many years to come.

My grandfather spoke of the Yankee Gale of 1851. For years to come, we will speak about Hurricane Fiona hitting Abegweit, our Island home. Usually in the insurance industry the pennies of the many pay the losses of a few. However, for a catastrophe, like Fiona, PEI Mutual is an owning member of Farm Mutual Re based in Cambridge, Ontario. This reinsurance is helping to pay the losses incurred from Fiona.

Hurricane Fiona demonstrated that PEI Mutual cannot operate without Reinsurance. Our reinsurance costs are already increasing. Since PEI Mutual is financially secure, you will not see an increase in your rates this year, as a result of this event. With Farm Mutual Re helping to pay for Fiona claims, PEI Mutual was able to add \$6.7 million dollars to our Member's Security Fund. PEI Mutual remains financially strong.

The incredible team at PEI Mutual consists of your management, agents, staff and your board of directors. From the one storm, this team answered 10,000 inquiries and reports of damage. This is roughly 8- 10 years work in one event. Optimistically we have nearly half of the Fiona claims completed. Our experienced employees, many new employees and even people who volunteered to help worked much overtime, going over and above what could be expected. Thank you. Thank you. Thank you.

We welcomed a new CEO in May, Craig Noonan, of Summerside. Craig joins us with a wealth of experience in management and leadership, and has had an immediate positive impact on our team. Welcome Craig. We have also added numerous other staff members and agents. We are happy to have you join the team and welcome you to PEI Mutual. We also welcomed one new director, Megan MacCallum from Brackley. Welcome Megan.

I would like to personally thank four people who retired before this Annual Meeting. Rose Doucette, who retired after 40 years of service in the office and then returned to help with Fiona. Former Director Joan Dennis also returned to help with Fiona. Agent Bruce Simpson, retired after 40 years of service, and finally our most recent retiree, Director Stewart MacRae. Together you have helped inspire our team to new heights of service.

As Mutual members and policyholders you were given two gifts this year. First, as PEI Mutual had a successful year in 2021, your rates were lowered by 8% by way of an increased Mutual Rebate in 2022. Second, with increasing cost of construction 10% was added to the limits of homes and buildings that were eligible for inflation factor protection.

We need to prepare for the future together. We are privileged to have insurance to protect our homes and businesses. This is not the case everywhere. Windstorms and high-water levels remain a huge threat going forward. Together we can keep PEI Mutual strong.

George Matheson,

President

CEO'S REPORT 2022

Member Service

In 2022, we encountered some significant milestones at PEI Mutual, including a change in leadership, a significant and extreme weather event, as well as a continued return to a post-pandemic reality and re-adjustment of our service delivery model.

Throughout all this, we have retained our commitment to providing exceptional service and doing our best to meet the expectations of our policyholders, keeping their needs at the forefront.

We are proud to be the insurance provider of choice on PEI, and will continue to work to improve and innovate for the future.

Thank you to all of our valued members across Prince Edward Island, as well as to our team who have worked hard to support each other in serving your insurance needs over the past 12 months.

2022 Financial Results

Even in the aftermath of Hurricane Fiona, PEI Mutual was able to achieve very good financial results in 2022. Premiums written were up by \$2.0 million over the previous year and our Mutual membership continued to grow as we added 1,100 net-new policies during the year.

The impact of Hurricane Fiona on claims experience was very significant. Total losses incurred were up by \$97.5 million over 2021, with Fiona being the cause of \$95.0 million of this increase. The company is very fortunate to have a catastrophe reinsurance treaty in place with Farm Mutual Re which provides exceptional protection to the Members' Surplus in times of catastrophic events. With regard to Fiona, PEI Mutual will only be retaining approximately \$2.0 million of this loss. This excellent protection will result in higher reinsurance rates and costs for PEI Mutual to the future, but as we witnessed first-hand this year, it is a critical factor in the protection of our Members' Surplus which has been built up over the past 137 years.

Investment income was quite good this year as well at \$3.9 million. Although the financial markets generally did not perform well during 2022, PEI Mutual did achieve a positive return on both our equities (6.08%) and bonds (3.52%).

Together with an underwriting profit of \$5.2 million and investment profit of \$3.9 million, the company achieved a net income after tax of \$6.7 million. These profits have been added to the Members' surplus which now sits at \$79.9 million – an exceptionally strong position as at December 31, 2022.

Mutual Rebates

As a Mutual company, PEI Mutual looks to provide rebates to our Members based on the financial results of our current fiscal year. Following another strong year in 2022, our Board of Directors has declared that the current 18% mutual rebate will remain effective and be applied to policy renewal premiums through April 30, 2024.

Hurricane Fiona

2022 brought us the most significant weather event in our company's 137-year history, Hurricane Fiona. This storm devastated our Island and tested the resilience of our community as a whole. I was and continue to be inspired by the patience and understanding of Islanders, as well as the extreme commitment to service by our team.

Ranking 7th on the list of all-time catastrophe's in Canadian History, and the # 1 costliest extreme weather event ever in Atlantic Canada, it is said to be the largest ever incurred by a Canadian Mutual Insurer. To add some perspective, our claims activity climbed more than 10 times our annual average, in a single-event.

With this, we were forced as a company to look for support as well as to explore new and innovative ways to operate most efficiently. The demand on our team was significant, and I have been so proud of the way they have responded to go over and above the call of duty, in order to serve Islanders.

Coming together/Power of Mutuality

On a positive note, Hurricane Fiona allowed us to deepen our connection with partners in the mutual community, calling on our colleagues, sister companies, and other stakeholders for support. Our request for help was met with a resounding response, allowing us to supplement our workforce with a fully-functioning remote call-in center, as well as to significantly enhance our capacity for adjusting claims, both in-person and remotely.

All of this contributed significantly to our success in working through this trying time and showcased the strong bond between Canadian Mutuals and power of mutuality at it's best.

In addition, we had to look at new and innovative ways to do things as a company, including providing virtual training for those who would be joining our team from out-of-province, and the addition of SMS text message claim reporting. We also called on a number of retired employees to re-join us, which provided some welcome support in the form of experienced help. As well, we placed focus on cross-training our existing team members, allowing us to re-purpose some of our internal resources to priority areas. Finally, we added a number of temporary team members who were quick to learn and adapt to the ever-changing needs of the situation. This support proved to be invaluable.

Communication quickly became of paramount importance, as with so many players involved, it was increasingly clear that we would need to ensure clarity and consistency in messaging to all groups. Our team embraced the concept of daily huddles, which proved to be of significant value in keeping people informed and on the same page.

A lot of lessons were learned that will inform our processes going forward, as well as to serve as an example for others in the future.

Digital Transformation

In 2022, we embarked on the challenge of the build and customization of a new, cloud-based Enterprise IT System, a project that we will see through to completion with our organization-wide adoption in May of 2023.

This system will bring us many opportunities for enhancing and modernizing the way we serve our members into the future, as well as the potential for creating efficiency in our operations by leveraging the data and real-time access to information that this type of solution offers. This will also allow for us to evaluate many of the manual processes that exist in our current operations and create opportunities for us to enhance the speed of service to our policyholders.

One of the key areas of interest for our members will be the new customer portal, which will enable policyholders the opportunity for enhanced digital communications as well as some self-service options.

The Enterprise IT System will act as the cornerstone of a digital transformation that we will undergo in the coming years, with the goal of working toward becoming a paperless environment with consistent real-time access to information, and exploring other means of web-based connection.

CEO Appointment

2022 also saw the appointment of myself, as the CEO. My thanks go to the Board of Directors for their confidence in selecting me for this important and influential role. It is my pledge that I will always treat the opportunity with the duty and care it deserves, throughout what I intend to be a long-standing and successful tenure.

Since joining the company in June, I have been focused on getting to know our team, and working with our Board of Directors, gaining a thorough understanding our business and identifying opportunities for the future.

From the moment I arrived, I have been inspired by our team and their commitment to service as well as the incredible strength of the other leaders in our organization.

I feel we have established a strong foundation of trust and accountability in the company, and I am proud of the culture we are building at PEI Mutual. Our team enjoys an environment centered around positivity, transparency, and a strong emphasis on communication. We embrace diversity and look for opportunities to celebrate each other and our successes often.

I have also spent some time meeting and connecting with colleagues within the Mutual community across Canada and particularly within the Maritime region and have enjoyed learning about the uniqueness and shared values of the sector.

Having been faced with adversity from the hurricane, we are still making progress on several fronts outside of the instability and uncertainty of a catastrophic weather-event environment. Our company is in a strong financial position, and each day as we move forward, we are able to see a clear path toward our future success. We have taken steps to add the necessary tools and resources for continued progress. Our team is in good spirits and working exceptionally well together.

As a leader, my focus has been on providing the vision and support to empower our people to perform at their best, while strategically positioning our company for success. Some of the key areas of focus have been to build our capacity - adding some key positions to support our already exceptional team, to enhance our culture – by creating opportunities for collaboration, listening and recognition, as well as to manage through change.

Looking ahead, PEI Mutual is well positioned for the future, and I look forward to what 2023 and beyond may bring.

Thank you

In closing, I would like to offer my sincere thanks to our members for placing your trust in us, and for your support in making us the insurance provider of choice on PEI. Moreover, I appreciate the extension of your patience and understanding while working with us through one of the greatest challenges in our company's storied history.

A special thank you is extended our team who bonded together to “weather the storm” of the most significant weather event impacting the insurance industry in Atlantic Canada, and to have come out the other side stronger than ever.

We are looking forward to serving our policyholders in 2023 and providing exceptional experiences, with our focus remaining on putting people first in everything we do – striving to be the best place to work, the insurance provider of choice, and to make the most impact in our communities.

Sincerely,

Craig Noonan

CEO



Financial Statements

Prince Edward Island Mutual Insurance Company

December 31, 2022

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MANAGEMENT RESPONSIBILITY FOR FINANCIAL REPORTING

DECEMBER 31, 2022

The accompanying financial statements and all other information contained in this annual report are the responsibility of the management of Prince Edward Island Mutual Insurance Company. The financial statements have been prepared by management in accordance with International Financial Reporting Standards and have been approved by the Board of Directors.

Preparation of financial information is an integral part of management's broader responsibilities for the ongoing operations of Prince Edward Island Mutual Insurance Company. Management maintains a system of internal accounting controls to provide reasonable assurance that transactions are accurately recorded on a timely basis, are properly approved and result in reliable financial information. Such information also includes data based on management's best estimates and judgements.

The Audit Committee and the Board of Directors review and approve the annual financial statements. In addition, the Audit Committee meets periodically with financial officers of Prince Edward Island Mutual Insurance Company and the external auditors, and reports to the Board of Directors thereon.

The accompanying financial statements have been audited by Grant Thornton LLP, authorized to practice public accounting by the Chartered Professional Accountants of Prince Edward Island, who are engaged by the Board of Directors and whose appointment was ratified at the annual meeting of the policyholders. The auditors have access to the Audit Committee, without management present, to discuss the results of their work. Their report dated February 14, 2023, expresses their unqualified opinion on the Company's 2022 financial statements.



Craig Noonan,
CEO



Rudy Smith,
CFO/Treasurer

Independent auditor's report

To the Policyholders of

Prince Edward Island Mutual Insurance Company

Opinion

We have audited the financial statements of Prince Edward Island Mutual Insurance Company ("the Company"), which comprise the statement of financial position as at December 31, 2022, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of Prince Edward Island Mutual Insurance Company as at December 31, 2022, 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 *Auditor's Responsibilities for the Audit of the Financial Statements* section of our 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.

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 International Financial Reporting Standards (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.

Auditor's 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 auditor's 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 these 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. 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 auditor's 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 auditor's 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.

We 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.

Grant Thornton LLP

Chartered Professional Accountants

Summerside, PE, Canada
February 14, 2023

Prince Edward Island Mutual Insurance Company
Statement of Financial Position
December 31, 2022

	2022	2021
Assets		
Cash and cash equivalents	\$ 2,379,611	\$ 13,342,688
Receivables (Note 6)	5,623,007	5,191,897
Income taxes receivable	2,471,248	-
Prepaid expenses	81,070	66,983
Deferred policy acquisition expenses	1,864,618	1,738,966
Reinsurer's share of provision for unpaid claims (Note 9)	87,585,195	1,732,534
Investments (Note 7)	92,702,651	85,565,182
Property, plant and equipment (Note 8)	3,827,771	3,968,174
Intangible asset (Note 8)	2,222,338	-
Deferred income taxes (Note 11)	349,618	516,344
	<u>\$ 199,107,127</u>	<u>\$ 112,122,768</u>

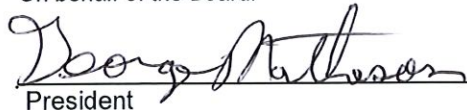
Liabilities

Accounts payable and accrued liabilities	\$ 1,145,637	\$ 1,191,781
Income taxes payable	-	3,466,550
Provision for unpaid claims (Note 9)	98,347,540	15,409,252
Unearned premium reserve	19,762,716	18,922,306
	<u>119,255,893</u>	<u>38,989,889</u>

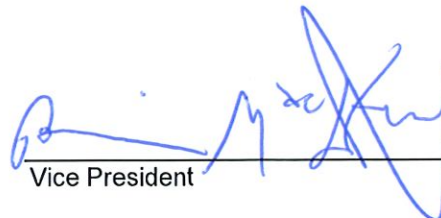
Members' Surplus

Unappropriated members' surplus	79,851,234	73,132,879
Commitment (Note 21)		
	<u>\$ 199,107,127</u>	<u>\$ 112,122,768</u>

On behalf of the Board:


 President

Director


 Vice President

Director

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

Prince Edward Island Mutual Insurance Company
Statement of Comprehensive Income
For the Year-Ended December 31, 2022

	2022	2021
Underwriting Income		
Gross premiums written	\$ 36,076,844	\$ 34,084,009
Less: reinsurance ceded	(3,623,764)	(2,994,178)
Net premiums written	32,453,080	31,089,831
Less: increase in unearned premiums	(840,410)	(1,155,705)
Net premiums earned	31,612,670	29,934,126
Direct losses incurred		
Gross claims and adjustment expenses (Note 12)	110,999,250	13,461,664
Less: Reinsurer's share of claims and adjustment expenses	(94,638,354)	(831,136)
Net losses incurred	16,360,896	12,630,528
	15,251,774	17,303,598
Expenses		
Fees, commissions and other acquisition expenses (Note 13)	3,278,209	3,085,840
Other operating and administrative expenses (Note 14)	6,822,138	5,821,867
	10,100,347	8,907,707
Net underwriting income	5,151,427	8,395,891
Investment and other income (Note 16)	4,244,638	7,951,117
Income before income taxes	9,396,065	16,347,008
Provision for income taxes (Note 11)	2,677,710	4,888,229
Net income and comprehensive income for the year	\$ 6,718,355	\$ 11,458,779

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

Prince Edward Island Mutual Insurance Company
Statement of Members' Surplus
For the Year-Ended December 31, 2022

	Unappropriated Members' Surplus
Balance at January 1, 2021	\$ 61,674,100
Net income and comprehensive income	<u>11,458,779</u>
Balance at December 31, 2021	73,132,879
Net income and comprehensive income	<u>6,718,355</u>
Balance at December 31, 2022	<u>\$ 79,851,234</u>

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

Prince Edward Island Mutual Insurance Company
Statement of Cash Flows
For the Year-Ended December 31, 2022

	2022	2021
Operating activities		
Net income and comprehensive income	\$ 6,718,355	\$ 11,458,779
Adjustments for:		
Depreciation of property, plant and equipment	308,642	293,850
Bond premium amortized	369,785	394,603
Gain on sale of investments	(551,545)	(342,864)
(Gain) loss on disposal of property, plant and equipment	2,094	(17,985)
Deferred income taxes	166,726	(93,373)
Unrealized (gain) loss on investments	(173,284)	(4,688,312)
	6,840,773	7,004,698
Change in non-cash operating working capital:		
Receivables	(431,110)	(791,249)
Prepaid expenses	(14,087)	(6,064)
Deferred policy acquisition expenses	(125,652)	(46,491)
Reinsurers' share of provision for unpaid claims	(85,852,661)	(114,766)
Accounts payable and accrued liabilities	(46,144)	509,413
Income taxes payable/receivable	(5,937,798)	3,781,139
Provision for refund of premium	-	(4,558,831)
Provision for unpaid claims	82,938,288	2,823,027
Unearned premium reserve	840,410	1,155,705
	(1,787,981)	9,756,581
Investing activities		
Purchase of investments	(13,213,921)	(13,785,323)
Proceeds on disposal of investments	6,431,496	4,430,990
Purchase of property, plant and equipment and intangibles	(2,392,671)	(170,184)
Proceeds on disposal of property, plant and equipment	-	27,888
	(9,175,096)	(9,496,629)
Net increase in cash and cash equivalents	(10,963,077)	259,952
Cash and cash equivalents, beginning of year	13,342,688	13,082,736
Cash and cash equivalents, end of year	\$ 2,379,611	\$ 13,342,688
Income taxes paid, net of refunds	\$ 8,448,782	\$ 1,197,702

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

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

1. Nature of operations

The Company is incorporated without share capital under the laws of Prince Edward Island and is subject to the Prince Edward Island Insurance Act. It is licensed to write property and casualty insurance in Prince Edward Island. The Company's head office is located at 116 Walker Avenue, Summerside, Prince Edward Island.

These financial statements have been authorized for issue by the Board of Directors on February 14, 2023.

2. Basis of presentation

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (the IASB).

These financial statements were prepared on a historical cost basis except for those financial assets and liabilities that have been measured at fair value.

The Company's functional and presentation currency is the Canadian dollar. The financial statements are presented in Canadian dollars.

The preparation of financial statements in compliance with IFRS requires management to make certain critical accounting estimates. It also requires management to exercise judgment in applying the Company's accounting policies. The areas involving a higher degree of judgment of complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 4.

3. Significant accounting policies

Insurance contracts

In accordance with IFRS 4, Insurance Contracts, the Company has continued to apply the accounting policies it applied in accordance with pre-changeover Canadian GAAP.

Balances arising from insurance contracts primarily include unearned premiums, provisions for unpaid claims and adjustment expenses, the reinsurer's share of provisions for unearned premiums and unpaid claims and adjustment expenses, deferred policy acquisition expenses, and salvage and subrogation recoverable.

(a) Premiums and unearned premiums

Premiums written comprise the premiums on contracts incepting in the financial year. Premiums written are stated gross of commissions payable to agents.

The Company earns premium income evenly over the term of the insurance policy generally using the pro rata method. The portion of the premium related to the unexpired portion of the policy at the end of the fiscal year is reflected in unearned premiums.

(b) Deferred policy acquisition expenses

Acquisition costs are those expenses such as agents' commissions, which relate directly to the acquisition of premiums. These costs are deferred and amortized over the terms of the related policies to the extent that they are considered to be recoverable from unearned premiums.

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

3. Significant accounting policies (cont'd)

(c) Provisions for unpaid claims and adjustment expenses

Individual loss estimates are provided on each claim reported. In addition, provisions are made for adjustment expenses, changes in reported claims and for claims incurred but not reported, based on past experience and business in force. The estimates are regularly reviewed and updated, and any resulting adjustments are included in current income.

Claim liabilities are carried on an undiscounted basis.

(d) Reinsurers' share of provisions for unpaid claims and adjustment expenses

The Company enters into reinsurance contracts in the normal course of business in order to limit potential losses arising from certain exposures. Reinsurance premiums are accounted for in the same period as the related premiums for the direct insurance business being reinsured. Reinsurance liabilities, comprised of premiums payable for the purchase of reinsurance contracts, are included in accounts payable and accrued liabilities and are recognized as an expense when due.

Expected reinsurance recoveries on unpaid claims and adjustment expenses are recognized as assets at the same time and using principles consistent with the Company's method for establishing the related liability.

(e) Refund of premium

Under the discretion of the board of directors the Company may declare a refund to its policyholders based on the premiums paid in the fiscal period. This refund is recognized as an expense in the period for which it is declared.

Financial instruments

The Company's financial assets are classified as fair value through profit or loss, or amortized cost. Financial liabilities are classified as amortized cost. Financial assets and liabilities are initially recognized at fair value with subsequent measurement based on classification. The classification depends on the purpose for which the financial instruments were acquired, their characteristics and choice where applicable.

Financial assets are measured at fair value except for those classified as amortized cost, which are initially recognized at fair value net of any transaction costs directly attributable to the issuance of the instrument, then subsequently carried at amortized cost using the effective interest method.

Financial liabilities are initially measured at fair value net of any transaction costs directly attributable to the issuance of the instrument, and are subsequently carried at cost using the effective interest rate method.

Fair values are based on quoted market values where available from active markets, otherwise fair values are estimated using a variety of valuation techniques and models.

Property, plant and equipment

Property, plant & equipment is initially recorded at cost and subsequently measured at cost less accumulated depreciation and accumulated impairment losses, with the exception of land which is not depreciated. Assets under construction are not depreciated until they are available for use. Depreciation of an asset commences when it is available for use and is recognized in net income using the diminishing balance method over the estimated useful life of the assets at the following rates:

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

3. Significant accounting policies (cont'd)

Building structure	4%
Building components	8%
Office equipment	20%
Computer equipment	45%
Vehicles	30%
Land improvements	8%

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

Intangible assets

Intangible assets consist of computer software which is not integral to the computer hardware owned by the Company. Software is initially recorded at cost and subsequently measured at cost less accumulated amortization and accumulated impairment losses. Software is amortized on a straight-line basis over its estimated useful life.

Impairment of non-financial assets

Non-financial assets are subject to impairment tests whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. Where the carrying value of an asset exceeds its recoverable amount, which is the higher of value in use and fair value less costs to sell, the asset is written down accordingly.

Where it is not possible to estimate the recoverable amount of an individual asset, the impairment test is carried out on the asset's cash-generating unit, which is the lowest group of assets in which the asset belongs for which there are separately identifiable cash flows. The Company has one cash-generating unit for which impairment testing is performed.

Impairment charges are included in net income, except to the extent they reverse gains previously recognized in other comprehensive income.

Income taxes

Income tax expense comprises of current and deferred tax. Current tax and deferred tax are recognized in net income except to the extent that it relates to a business combination, or items recognized directly in equity or in other comprehensive income.

Current income taxes are recognized for the estimated income taxes payable or receivable on taxable income or loss for the current year and any adjustment to income taxes payable in respect of previous years. Current income taxes are determined using tax rates and tax laws that have been enacted or substantively enacted by the year-end date.

Deferred tax assets and liabilities are recognized where the carrying amount of an asset or liability differs from its tax base, except for taxable temporary differences arising on the initial recognition of goodwill and temporary differences arising on the initial recognition of an asset of liability in a transaction which is not a business combination and at the time of the transaction affects neither accounting or taxable profit or loss.

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

3. Significant accounting policies (cont'd)

Recognition of deferred tax assets for unused tax losses, tax credits and deductible temporary differences is restricted to those instances where it is probable that future taxable profit will be available against which the deferred tax asset can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

The amount of the deferred tax asset or liability is measured at the amount expected to be recovered from or paid to the taxation authorities. This amount is determined using tax rates and tax laws that have been enacted or substantively enacted by the year-end date and are expected to apply when the liabilities / (assets) are settled / (recovered).

Provisions

Provisions are recognized for liabilities of uncertain timing or amount that have arisen as a result of past transaction, including legal, equitable or constructive obligations. The provision is measured at the best estimate of the expenditure required to settle at the reporting date.

Foreign currency translation

Foreign currency accounts are translated into Canadian dollars as follows:

At the transaction date, each asset, liability, revenue and expense denominated in a foreign currency is translated into Canadian dollars by the use of the exchange rate in effect at that date. At the year-end date, unsettled monetary assets and liabilities are translated into Canadian dollars by using the exchange rate in effect at the year-end date and the related translation differences are recognized in net income. Exchange gains and losses arising on the retranslation of monetary available-for-sale financial assets are treated as a change in fair value and recognized in net income or other comprehensive income.

Cash and cash equivalents

Cash and cash equivalents comprise cash on hand together with other short-term, highly liquid investments that are readily convertible into known amounts of cash, and which are subject to an insignificant risk of changes in value.

Standards, amendments and interpretations not yet effective

Certain new standards, amendments and interpretations have been published that are mandatory for the Company's accounting periods beginning on or after January 1, 2023, or later periods that the Company has decided not to adopt early.

Of those new standards, amendments and interpretations that are not yet effective, IFRS 17 Insurance Contracts is expected to have a material impact on the Company's financial statements in the period of the initial application.

- IFRS 17 Insurance Contracts supersedes IFRS 4 Insurance Contracts. IFRS 17 establishes the principles for recognition, measurement, presentation and disclosure of insurance contracts. IFRS 17 requires entities to measure insurance contract liabilities using updated estimates and assumptions that reflect the timing of cash flows and any uncertainty relating to insurance contracts. Additionally, IFRS 17 requires entities to recognize profits as it delivers insurance services. The effective date for IFRS 17 is January 1, 2023. The Company has not yet determined the impact of adoption. However, it is expected to significantly impact the overall financial statements.

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

4. Critical accounting estimates and judgments

The Company makes estimates and assumptions about the future that affect the reported amounts of assets and liabilities. Estimates and judgments are continually evaluated and based on historical experience and other IAS factors, including expectations of future events that are believed to be reasonable under the circumstances. In the future, actual experience may differ from these estimates and assumptions.

The effect of a change in an accounting estimate is recognized prospectively by including it in comprehensive 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.

The estimates and assumptions that have a significant risk of causing material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

Deferred policy acquisition expenses

Deferred policy acquisition expenses are those expenses such as agents' commissions, which relate directly to the acquisition of policies. These expenses, to the extent that they are considered recoverable, are estimated, deferred and amortized over the terms of the related policies.

Provision for unpaid claims

The estimation of the provision for unpaid claims and the related reinsurers' share are the Company's most critical accounting estimates. There are several sources of uncertainty that need to be considered by the Company in estimating the amount that will ultimately be paid on these claims. The uncertainty arises because all events affecting the ultimate settlement of claims have not taken place and may not take place for some time. Changes in the estimate of the provisions 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 based on the Company's historical experience and industry experience. More details are included in Note 9.

Unearned premium reserve

The unearned premium reserve is calculated based on the estimated unexpired term of all policies of the Company in force as of December 31. The factor used to estimate the unexpired term is based on the Company's historical experience.

Income taxes

The Company periodically assesses its liabilities and contingencies related to income taxes for all years open to audit based on the latest information available. For matters where it is probable that an adjustment will be made, the Company records its best estimate of the tax liability including the related interest and penalties in the current tax provision. Management believes they have adequately provided for the probable outcome of these matters; however, the final outcome may result in a materially different outcome than the amount included in the tax liabilities.

Catastrophic event

On September 24, 2022, Prince Edward Island was hit by post-tropical storm Fiona. This was an historic weather event including high winds and heavy rains, which resulted in catastrophic damage to Island properties. As at December 31, 2022, PEI Mutual's gross losses incurred associated with this catastrophic event were estimated at \$95 million, with approximately \$93.2 million being recoverable under the company's Catastrophe reinsurance treaty.

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

5. Financial instrument classification

The carrying amount of the Company's financial instruments by classification is as follows:

	Fair value through profit or loss	Amortized cost	Total
December 31, 2022			
Cash and cash equivalents	\$ 2,379,611	\$ -	\$ 2,379,611
Receivables (Note 6)	5,623,007	-	5,623,007
Investments (Note 7)	25,342,347	67,360,304	92,702,651
Accounts payable and accrued liabilities	-	1,145,637	1,145,637
	\$ 33,344,965	\$ 68,505,941	\$ 101,850,906

	Fair value through profit or loss	Amortized cost	Total
December 31, 2021			
Cash and cash equivalents	\$ 13,342,688	\$ -	\$ 13,342,688
Receivables (Note 6)	5,191,897	-	5,191,897
Investments (Note 7)	23,937,857	61,627,325	85,565,182
Accounts payable and accrued liabilities	-	1,191,781	1,191,781
	\$ 42,472,442	\$ 62,819,106	\$ 105,291,548

6. Receivables

	2022	2021
Policyholders for premiums	\$ 4,928,286	\$ 4,606,969
Accrued interest	678,487	576,714
Other	16,234	8,214
	\$ 5,623,007	\$ 5,191,897

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

7. Investments

The following table provides cost and fair value information of investments by type of security and issuer. The maximum exposure to credit risk would be the carrying value as shown below.

Carrying value	2022	2021
Investments at amortized cost	\$ 67,360,304	\$ 61,627,325
Investments at fair value through profit or loss	25,342,347	23,937,857
	<u>\$ 92,702,651</u>	<u>\$ 85,565,182</u>

	December 31, 2022		December 31, 2021	
	Cost	Fair Value	Cost	Fair Value
Investments at amortized cost				
Term deposits and GICs	\$ 12,120,000	\$ 12,120,000	\$ 10,347,000	\$ 10,347,000
Bonds, at par less unamortized purchase discounts and premiums				
- Federal	197,272	207,598	196,362	222,194
- Provincial	14,631,911	14,253,201	13,694,445	14,775,060
- Municipal	13,430,977	13,019,905	13,115,454	14,416,181
- Corporate	26,980,145	25,723,593	24,274,064	25,885,316
Total bonds	<u>55,240,304</u>	<u>53,204,297</u>	<u>51,280,325</u>	<u>55,298,751</u>
	<u>\$ 67,360,304</u>	<u>\$ 65,324,297</u>	<u>\$ 61,627,325</u>	<u>\$ 65,645,751</u>

Investments at fair value through profit or loss				
Equities - Canadian				
Common Stock	\$ 14,266,565	\$ 19,715,136	\$ 13,285,973	\$ 19,027,298
Equities - US				
Common Stock	<u>3,583,388</u>	<u>5,627,211</u>	<u>3,332,774</u>	<u>4,910,559</u>
	<u>\$ 17,849,953</u>	<u>\$ 25,342,347</u>	<u>\$ 16,618,747</u>	<u>\$ 23,937,857</u>

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

7. Investments (cont'd)

The following table summarizes fair value measurements recognized in the statement of financial position or disclosed in the Company's financial statements, categorized by level according to the significance of the inputs used in making the measurements.

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities using the last bid price;
- Level 2 fair value measurements are those derived from 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); and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

	Carrying Value	Fair Value			Total
		Level 1	Level 2	Level 3	
December 31, 2022					
Equity investments					
- Canadian	\$ 19,715,136	\$ 19,715,136	\$ -	\$ -	\$ 19,715,136
- US	5,627,211	5,627,211	-	-	5,627,211
Bonds	67,360,304	-	65,234,297	-	65,234,297
Total	\$ 92,702,651	\$ 25,342,347	\$ 65,234,297	\$ -	\$ 90,576,644
December 31, 2021					
Equity investments					
- Canadian	\$ 19,027,298	\$ 19,027,298	\$ -	\$ -	\$ 19,027,298
- US	4,910,559	4,910,559	-	-	4,910,559
Bonds	61,627,325	-	65,645,751	-	65,645,751
Total	\$ 85,565,182	\$ 23,937,857	\$ 65,645,751	\$ -	\$ 89,583,608

There were no transfers between Level 1 and Level 2 for the years ended December 31, 2021 and 2022.

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

7. Investments (cont'd)

	Within 1 Year	2 to 5 Years	6 to 10 Years	Over 10 Years	Total
December 31, 2022					
Bonds	\$ 3,100,000	\$ 24,118,739	\$ 25,486,275	\$ 2,535,290	\$ 55,240,304
Term Deposits	2,000,000	10,120,000	-	-	12,120,000
Total	\$ 5,100,000	\$ 34,238,739	\$ 25,486,275	\$ 2,535,290	\$ 67,360,304
Percent of total	7.57%	50.83%	37.84%	3.76%	100.00%
December 31, 2021					
Bonds	\$ 900,000	\$ 18,862,815	\$ 27,462,591	\$ 4,054,919	\$ 51,280,325
Term Deposits	4,207,000	6,140,000	-	-	10,347,000
Total	\$ 5,107,000	\$ 25,002,815	\$ 27,462,591	\$ 4,054,919	\$ 61,627,325
Percent of total	8.29%	40.57%	44.56%	6.58%	100.00%

The effective interest rate for amortized cost investments is 3.52% and 3.451% on December 31, 2022 and December 31, 2021 respectively.

8. Property, plant & equipment and intangible assets

Property, plant and equipment	Land	Building	Office equipment	Computer equipment	Vehicles	Land improvements	Total
Cost							
Balance on January 1, 2021	\$ 608,343	\$ 3,985,963	\$ 363,926	\$ 323,319	\$ 415,539	\$ 106,693	\$ 5,803,783
Additions	-	24,286	1,783	54,355	89,760	-	170,184
Disposals	-	-	(4,631)	(28,343)	(64,262)	-	(97,236)
Balance on December 31, 2021	608,343	4,010,249	361,078	349,331	441,037	106,693	5,876,731
Additions	-	-	12,329	158,004	-	-	170,333
Disposals	-	-	(8,138)	(29,077)	-	-	(37,215)
Balance on December 31, 2022	\$ 608,343	\$ 4,010,249	\$ 365,269	\$ 478,258	\$ 441,037	\$ 106,693	\$ 6,009,849
Accumulated depreciation							
Balance on January 1, 2021	\$ -	\$ 879,764	\$ 251,557	\$ 239,215	\$ 294,846	\$ 36,658	\$ 1,702,040
Depreciation expense	-	143,273	22,539	60,888	61,547	5,603	293,850
Disposals	-	-	(3,174)	(25,191)	(58,968)	-	(87,333)
Balance on December 31, 2021	-	1,023,037	270,922	274,912	297,425	42,261	1,908,557
Depreciation expense	-	136,097	20,366	103,943	43,081	5,155	308,642
Disposals	-	-	(7,481)	(27,640)	-	-	(35,121)
Balance on December 31, 2022	\$ -	\$ 1,159,134	\$ 283,807	\$ 351,215	\$ 340,506	\$ 47,416	\$ 2,182,078
Net book value							
December 31, 2021	\$ 608,343	\$ 2,987,212	\$ 90,156	\$ 74,419	\$ 143,612	\$ 64,432	\$ 3,968,174 ¹
December 31, 2022	\$ 608,343	\$ 2,851,115	\$ 81,462	\$ 127,043	\$ 100,531	\$ 59,277	\$ 3,827,771

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

8. Property, plant & equipment and intangible assets (cont'd)

Intangible assets		2022		
		Cost	Accumulated Depreciation	Net book value
	Useful life			
Computer software	-	\$ 2,222,338	\$ -	\$ 2,222,338

Intangible assets		2021		
		Cost	Accumulated Depreciation	Net book value
	Useful life			
Computer software	-	\$ -	\$ -	\$ -

Included in intangible assets is the cost associated with the development of a new IT software system for PEI Mutual Insurance Company. As at December 31, 2022 this system was not yet available for use. As such, there has been no amortization expense incurred at December 31, 2022.

9. Insurance contracts

The following is a summary of the insurance contract provisions and related reinsurance assets on December 31.

	December 31, 2022			December 31, 2021		
	Gross	Reinsurance	Net	Gross	Reinsurance	Net
Outstanding claims provision						
Long settlement term	\$ 6,624,636	\$ 864,456	\$ 5,760,180	\$ 6,084,361	\$ 763,001	\$ 5,321,360
Short settlement term	89,298,529	86,720,739	2,577,790	7,199,015	969,533	6,229,482
	95,923,165	87,585,195	8,337,970	13,283,376	1,732,534	11,550,842
Provision for claims incurred but not reported	2,424,375	-	2,424,375	2,125,876	-	2,125,876
	<u>\$ 98,347,540</u>	<u>\$87,585,195</u>	<u>\$ 10,762,345</u>	<u>\$ 15,409,252</u>	<u>\$ 1,732,534</u>	<u>\$ 13,676,718</u>

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

9. Insurance contracts (cont'd)

Comments and assumptions for specific claims categories

The ultimate cost of long settlement general liability claims is difficult to predict for several reasons. Claims may not be reported until many years after a policy expires. Changes in the legal environment have created further complications. Court decisions and federal and provincial legislation may dramatically increase the liability between the time a policy is written and associated claims are ultimately resolved. For example, liability for exposure to toxic substances and environmental impairment, which did not appear likely or even exist when the policies were written, has been imposed by legislators and judicial interpretation. Tort liability has been expanded by some jurisdictions to cover defective workmanship. Provisions for such difficult-to-estimate-liabilities are established by examining the facts of tendered claims and adjusted in the aggregate for ultimate loss expectations based upon historical experience patterns and current socioeconomic trends.

Claims and adjustment expenses

Changes in claim liabilities recorded in the balance sheet for the years-ended December 31, 2022 and 2021 and their impact on claims and adjustment expenses for the two years follow:

	2022	2021
Unpaid claim - beginning of year – net of reinsurance	\$ 11,550,842	\$ 8,935,587
Increase (decrease) in estimated losses and expenses, for losses occurring in prior years	(827,845)	408,509
Provision for losses and expenses on claims occurring in the current year	15,942,449	12,129,012
Payment on claims:		
Current year	(13,569,712)	(6,574,132)
Prior years	(4,757,764)	(3,348,134)
Unpaid claims – end of year - net of reinsurance	\$ 8,337,970	\$ 11,550,842

The change in estimate of losses occurring in prior years is due to changes arising from new information received.

Provision for unpaid claims and adjustment expenses

The determination of the provision for unpaid claims and adjustment expenses and the related reinsurers' share requires the estimation of three major variables which are the development of claims, reinsurance recoveries, and future investment income. As the Company does not sell auto insurance, future investment income has been disregarded for this purpose.

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

9. Insurance contracts (cont'd)

Claim development

The estimation of claim development involves assessing the future behavior of claims, taking into consideration 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 the settlement of a group of claims the more variable the estimates. Short settlement term claims are those which are expected to be substantially paid within a year of being reported.

The tables that follow present the development of claims payments and the estimated ultimate cost of claims for the claim year 2013 to 2022. The upper half of the tables 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.

<i>Net Claims</i>	<i>(\$'000)</i>										
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Total
Net estimate of cumulative claims cost:											
At the end year of claim	12,918	13,670	13,945	10,575	12,522	15,753	14,123	11,352	11,462	16,830	
One year later	12,472	13,893	13,523	10,246	12,491	16,258	13,913	11,121	10,943		
Two years later	12,362	13,770	13,760	10,090	12,565	16,250	13,692	11,121			
Three years later	12,309	13,712	13,769	10,164	12,364	16,364	13,692				
Four years later	12,297	13,711	13,742	10,068	12,489	16,364					
Five years later	12,309	13,687	13,885	9,914	12,489						
Six years later	12,308	13,595	14,020	9,914							
Seven years later	12,302	13,671	14,020								
Eight years later	12,299	13,671									
Nine years later	12,299										
Current estimate of cumulative claims cost	12,299	13,671	14,020	9,914	12,489	16,364	13,692	11,121	10,943	16,830	
Cumulative payments	12,345	13,540	13,210	9,843	12,202	14,675	12,731	9,863	10,440	14,457	
Outstanding claims	(46)	131	810	71	287	1,689	961	1,258	503	2,373	8,037
Outstanding claims 2012 and prior											301
Net outstanding claims and handling expense											8,338

10. Pension plan

The Company has a defined contribution plan providing pension benefits to eligible employees. The total plan expense for the Company's defined contribution plan for 2022 was \$345,121 (2021 - \$394,676).

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

11. Income taxes

Income tax expense is comprised of current and deferred tax. The significant components of tax expense included in net income and comprehensive income are as follows:

	2022	2021
Current tax expense		
Based on current year taxable income	\$ 2,510,984	\$ 4,981,602
Deferred tax expense		
Origination and reversal of temporary differences	166,726	(93,373)
Total income tax expense	\$ 2,677,710	\$ 4,888,229

Reasons for the difference between tax expense for the year and the expected income taxes based on the statutory tax rates are as follows:

	2022	2021
Income before income taxes	\$ 9,396,065	\$ 16,347,008
Combined basic Canadian Federal and provincial income tax rate	31%	31%
Income taxes at statutory rates	2,912,780	5,067,572
Non deductible portion of claims liabilities	(144,054)	87,514
Depreciation in excess of capital cost allowance	(18,515)	2,378
Other non deductible expenses	(350)	5,347
Deduction for CCPC dividends	(238,877)	(181,209)
Origination and reversal of temporary timing differences	166,726	(93,373)
Total income tax expense	\$ 2,677,710	\$ 4,888,229

The significant components of deferred tax assets are:

Deferred tax assets	2022	2021
Provision for unpaid claims	\$ 333,633	\$ 477,686
Unpaid pension liability	4,251	9,057
Property, plant & equipment	11,734	29,601
	\$ 349,618	\$ 516,344

Prince Edward Island Mutual Insurance Company
Notes to the Financial Statements
December 31, 2022

12. Gross claims and adjustment expenses

Included in claims expenses were wage costs of \$1,606,238 (2021 - \$451,375).

13. Fees, commissions and other acquisition expenses

	2022	2021
Commissions	\$ 2,403,256	\$ 2,278,812
Sales salaries	625,010	564,823
Other	249,943	242,205
	<u>\$ 3,278,209</u>	<u>\$ 3,085,840</u>

14. Other operating and administrative expenses

	2022	2021
Advertising and promotions	\$ 233,608	\$ 232,043
Computer costs	565,327	-
Conventions, courses and travel	60,048	50,940
Depreciation	265,561	232,303
Directors fees	305,754	298,396
Donations and sponsorships	195,682	111,950
Loss Prevention	28,899	35,425
Office supplies	244,244	197,213
Other administration costs	552,882	506,341
Postage	175,105	223,420
Premium tax	450,961	369,377
Professional fees	479,997	223,117
Salaries and benefits	3,076,043	3,151,175
Taxes, dues and licences	117,538	125,217
Telephone	70,489	64,950
	<u>\$ 6,822,138</u>	<u>\$ 5,821,867</u>

15. Salaries, benefits and directors fees

	2022	2021
Claims handling - Salaries, adjusting fees & benefits (Note 12)	\$ 1,606,238	\$ 451,375
Sales salaries, commissions and benefits (Note 13)	3,028,266	2,843,635
Director fees (Note 14)	305,754	298,396
Other salaries and benefits (Note 14)	3,076,043	3,151,175
	<u>\$ 8,016,302</u>	<u>\$ 6,744,581</u>

Prince Edward Island Mutual Insurance Company
Notes to the Financial Statements
December 31, 2022

16. Investment and other income

	2022	2021
Interest income	\$ 2,382,047	\$ 2,087,142
Dividend income	903,368	713,136
Gains on disposal of investments	551,545	342,864
Unrealized gains (losses) on investments	173,284	4,688,312
Investment expenses	(131,048)	(108,681)
(Loss) gain on disposal of property, plant and equipment	(2,094)	17,985
Other income	367,536	210,359
	<u>\$ 4,244,638</u>	<u>\$ 7,951,117</u>

17. Related party transactions

The Company entered into the following transactions with key management personnel, which are defined by IAS 24, Related Party-Disclosures, as those persons having authority and responsibility for planning, directing and controlling the activities of the Company, including directors and management:

	2022	2021
Compensation		
Short term employee benefits and director's fees	\$ 1,466,637	\$ 1,125,732
Total pension and other post-employment benefits	97,941	80,724
	<u>\$ 1,564,578</u>	<u>\$ 1,206,456</u>

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

18. Capital management

The Company's objectives with respect to capital management are to maintain a capital base that is structured to exceed regulatory requirements and to best utilize capital allocations. Reinsurance is utilized to protect capital from catastrophic losses as the frequency and severity of these losses are inherently unpredictable. To limit their potential impact, catastrophe coverage limits the Company's exposure to \$1.8 million. The \$1.8 million net retained amount represents approximately 2.25% of Company's capital. For the purpose of capital management, the Company has defined capital as members' surplus.

Section 317. (1) of the Insurance Act of Prince Edward Island requires insurers to maintain a reserve fund equal to the sum of \$500 for every \$100,000 of the first \$1 million of insurance in force, and \$3,000 for each additional \$1 million or part thereof insurance in force. The Company's reserve fund as of December 31, 2022 was 1.41 times that which is required by S317. (1) of the Insurance Act.

20. Financial instrument and Insurance risk management

Insurance risk management

The principal risk the Company faces under insurance contracts is that the actual claims and benefit payments or the timing thereof, differ from expectations. This is influenced by the frequency of claims, severity of claims, actual benefits 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 above risk exposure is mitigated by diversification across a large portfolio of insurance. The variability of risks is also improved by careful selection and implementation of underwriting strategy guidelines, as well as the use of reinsurance arrangements.

The Company purchases reinsurance as part of its risk mitigation program. Retention limits for the excess-of-loss reinsurance vary by product line.

Amounts recoverable from reinsurers are estimated in a manner consistent with the outstanding claims provision and are in accordance with the reinsurance contracts. Although the Company has reinsurance arrangements, it is not relieved of its direct obligations to its policyholders and thus a credit exposure exists with respect to ceded insurance, to the extent that any reinsurer is unable to meet its obligations assumed under such reinsurance agreements.

The Company writes insurance primarily over twelve-month duration. The most significant risks arise through high severity, low frequency events such as natural disasters or catastrophes. A concentration of risk may arise from insurance contracts issued in a specific geographic location since all insurance contracts are written in Prince Edward Island.

The Company manages this risk via its underwriting and reinsurance strategy within an overall risk management framework. Exposures are limited by having documented underwriting limits and criteria. Pricing of property and liability policies are based on assumptions in regard to trends and past experience, in an attempt to correctly match policy revenue with exposed risk.

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

20. Financial instrument and Insurance risk management (cont'd)

Reinsurance is purchased to mitigate the effect of the potential loss to the company. Reinsurance is placed with Farm Mutual Re, a Canadian registered reinsurer.

The Company follows a policy of underwriting and reinsuring contracts of insurance which, in the main, limit the liability of the Company to an amount on any one claim of \$600,000 in the event of a property claim, and \$600,000 in the event of a liability claim. The Company also obtained reinsurance which limits the Company's liability to \$1.8 million in the event of a series of claims arising out of a single occurrence. In addition, the Company has obtained stop loss reinsurance which limits the liability of all claims in a specific year to 80% of gross net earned premiums for property and liability combined.

The Company is exposed to a pricing risk to the extent that unearned premiums are insufficient to meet the related future policy costs. Evaluation is performed regularly to estimate future claims costs, related expenses, and expected profit in relation to unearned premiums. There was no premium deficiency on December 31, 2022 and 2021.

The risks associated with insurance contracts are complex and subject to a number of variables which complicate quantitative sensitivity analysis. The company uses various techniques based on past claims development experience to quantify these sensitivities. This includes indicators such as average claim cost, amount of claims occurrence, expected loss ratios and claims development as described in Note 9.

Results of sensitivity testing based on expected loss ratios are as follows, shown gross and net of reinsurance as impact on pre-tax income.

	Property claims		Liability claims	
	2022	2021	2022	2021
5% increase in loss ratios				
Gross	1,604,593	1,501,984	199,250	202,216
Net	1,444,441	1,369,890	178,213	184,602
5% decrease in loss ratios				
Gross	(1,604,593)	(1,501,984)	(199,250)	(202,216)
Net	(1,444,441)	(1,369,890)	(178,213)	(184,602)

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.

Credit Risk

Credit risk is the risk of financial loss to the Company if a debtor fails to make payments of interest and principal when due. The Company is exposed to this risk relating to its debt holdings in its investment portfolio and the reliance on reinsurers to make payment when certain loss conditions are met.

All of the Company's investments in bonds and debentures are measured at amortized cost and are considered to have low credit risk. Based on Management's assessment of past events, current conditions and expected collectability of future cash flows from these instruments, there is no expected credit loss allowance to be recognized in the financial statements.

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

20. Financial instrument and Insurance risk management (cont'd)

The Company's investment policy includes guidelines on the bond portfolio relating to portfolio composition, issuer type, bond quality ratings (at time of acquisition – rated as "BBB" or better) and general guidelines for geographic exposure. All fixed income portfolios are monitored by management on a monthly basis.

Reinsurance is placed with Farm Mutual Re, a Canadian registered reinsurer. Management monitors the creditworthiness of Farm Mutual Re by reviewing their annual financial statements and through ongoing communications. Reinsurance treaties are reviewed annually by management prior to renewal of the reinsurance contract.

Accounts receivable are short-term in nature consisting of a large number of policyholders and are not subject to material credit risk. Regular review of outstanding receivables is performed to ensure credit worthiness.

The maximum exposure to investment credit risk is outlined in Note 7.

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.

Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate as a result of market factors. Market factors include three types of risk: currency risk, interest rate risk and equity risk.

The Company's investment policy operates within the guidelines of the Insurance Act. An investment policy is in place and its application is monitored by the Investment Committee and the Board of Directors. Diversification techniques are utilized to minimize risk.

Currency risk

Currency risk relates to the Company operating in different currencies and converting non-Canadian earnings at different points in time at different foreign exchange levels when adverse changes in foreign currency exchange rates occur.

The Company's foreign exchange risk is related to stock holdings which are limited to United States equities in sectors which are not readily available in Canada. The Company limits its holdings in foreign equity to 25% of its total equity holdings in accordance with its investment policy. Foreign currency changes are monitored by the investment committee and holdings are adjusted when offside of the investment policy. A 1% change in the value of the United States dollar would affect the fair value of stocks by \$56,272 which would be reflected in the statement of comprehensive income.

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 potential for financial loss caused by fluctuations in fair value or future cash flows of financial instruments because of changes in market interest rates.

The Company is not exposed to this risk as its interest-bearing investments are being held to maturity.

Prince Edward Island Mutual Insurance Company

Notes to the Financial Statements

December 31, 2022

20. Financial instrument and Insurance risk management (cont'd)

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

Equity risk is the uncertainty associated with the valuation of assets arising from changes in equity markets. The Company is exposed to this risk through its equity holdings within its investment portfolio.

The Company's portfolio includes Canadian stocks with fair values that move with the Toronto Stock Exchange Composite Index and United States stocks with fair values that move with the S&P 500 Index. A 10% movement in the stock markets with all other variables held constant would have an estimated effect on the fair values of the Company's Canadian common stock and United States common stock of \$2.53 million (2021 - \$2.39 million), which would be recognized in the statement of comprehensive income.

The Company's investment policy limits investment in common shares to a maximum of 25% of the adjusted cost base of the portfolio.

Equities are monitored by the board of directors on a semi-annual basis. Holdings are adjusted by the Investment Committee, as required.

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet all cash outflow obligations as they come due. The Company mitigates this risk by monitoring cash activities and expected outflows. The Company's current liabilities arise as claims are made. The Company does not have material liabilities that can be called unexpectedly at the demand of a lender or client. The Company has no material commitments for capital expenditures and there is no need for such expenditures in the normal course of business. Claim payments are funded by current operating cash flow including investment income.

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.

21. Commitment

In December 2021, the Company entered into an agreement to implement a new information technology system. As at December 31, 2022, the implementation of the new information technology system is still in progress. The implementation fee is estimated at \$2.86M with ongoing annual subscription fees of \$565,000 for the next five years ending in December of 2026. To date \$2,222,338 in capital costs and \$565,327 in operating costs have been incurred relating to this commitment.