



2006 Annual Report





YOUR OWN COMPANY

Prince Edward Island Mutual Insurance Company

201 Water Street
Summerside, P.E.I.
C1N 1B4

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DIRECTORS

Percy Affleck Bedeque, P.E.I.	887-2507
Claude Dorgan Tignish, P.E.I.	882-3452
Jim Doyle Auburn, P.E.I.	676-2472
Allison Johnson Belmont, Lot 16, P.E.I.	436-5200
Stewart MacRae Ebenezer, P.E.I.	964-2979
Brian MacKinley Cornwall, P.E.I.	566-4163
George Matheson Albion Cross, P.E.I.	583-2340
Gordon Vessey York, P.E.I.	629-1332
Brian Annear Lower Montague, P.E.I.	838-3038

OFFICERS

President Percy Affleck Bedeque, P.E.I.	Secretary/Legal Counsel Blair Campbell Summerside, P.E.I.
Vice-President Gordon Vessey York, P.E.I.	Treasurer Rudy Smith Summerside, P.E.I.
General Manager Terrence Shea Summerside, P.E.I.	

NOTICE OF ANNUAL MEETING

P.E.I. Mutual Insurance Company will be holding its annual meeting on Tuesday, April 10, 2007, at 2:00 P.M. at the Royal Canadian Legion, 340 Notre Dame Street, Summerside, P.E.I.

The purpose of the meeting is to receive the financial statements and auditors report for 2006; to elect directors; to amend by-laws; to appoint auditors and to transact other business which may properly be brought before the meeting. Proposed amendments to our by-laws can be obtained by contacting the Corporate Secretary at 1-800-565-5441.

Blair Campbell, Corporate Secretary



PRESIDENT'S REPORT

2006 has been a very successful year for PEI Mutual to the extent that the Board of Directors has been able to declare a Special Mutual Rebate in the amount of \$1.3 million. This refund has been distributed to our 29,000 policyholders by way of cheque and is this is in addition to the 10% Mutual Rebate that will be repeated again in 2007 at time of policy renewals.

On a less positive note is the cost of continuing oil spill losses, which amounted to \$1.5 million during the past year. This in spite of past efforts by the Company and policyholders to lessen the risk by equipment upgrades and increased diligence. Outside oil tanks continue to be a large contributor to the problem and this must be addressed. To PEI Mutual's credit, our remedial cleanup procedure is stellar and endorsed by our Reinsurers but also very expensive. This has resulted in an unusual number of claims against our reinsurance coverage and as policyholders we realize this cannot continue without the consequence of higher reinsurance premiums in the future. While oil spill losses occur across the nation, Prince Edward Island is unique in that we have the highest population density per square kilometer and are among the largest users of home heating oil. The risks are great and in the end policyholders will have to be a big part of the solution.

Board governance is a major issue of review for organizations with public involvement and consumes a lot of time in this post Enron era. PEI Mutual is not immune to this fact and has felt the sting of change from other organizations with which we have dealings. The Board of Directors and our Management team have completed our own governance review that spanned approximately eighteen months and took a huge effort in gathering information and determining its relevance to our Company. In the process, both old and new governance systems were examined, some being very similar to ours and others vastly different. On occasion external expertise and advice was necessary to move the review along.

While change for the Maritime Mutual system of governance is likely inevitable, it seems inadvisable for our Company to venture into major overhaul in advance of proposals under consideration by the Maritime govern-



ments. It is evident from our review that a lot of our past application of governance principles are quite acceptable and even recommended in modern governance models. In the end, our consultant's advice was to fine tune our procedures, make some minor changes and stay the course for the time being.

Since the last annual meeting Blair Wood has tendered his resignation from the Board. I wish to acknowledge Blair's many years of service and thank him for his valued contribution to the governance process.

Further, I am pleased to advise that Brian Annear of Lower Montague has been nominated to fill the vacancy in Zone 9. Brian brings youth and business talent to the board table and will be a valued addition to the Board of Directors.

A successful year at PEI mutual is not by accident. Everyone plays an important part. I wish to express appreciation to our valued policyholders and acknowledge the diligent work of our office Staff, Agent force, Management team and fellow Directors. Thank you!

Percy Affleck,
President

MANAGER'S REPORT

Your rebate cheque is enclosed.

Most successful year in past 25 years.

Rebates to policyholders total \$2,700,000

PEI Mutual has just completed its best year financially for the past 25 years. Our policyholders will benefit from our success by sharing in the Company's profits through "Mutual Rebates" which are given in years when the Company has good financial results. I am pleased to advise that policyholders will receive a total of \$2,700,000 in mutual rebates:

- A "Mutual Rebate" of \$1,400,000 (10% of 2007 premium) will be deducted from our policyholders' invoice in 2007, and
- A "Special Mutual Rebate" of \$1,300,000 (10% of 2006 premium) is being paid out to our policyholders – your cheque is enclosed.

Mutual rebates have been paid to our policyholders for 18 of the past 24 years. The total amount refunded to

our policyholders in these 18 years is approximately \$20,000,000.

In 2006, we continued our struggle to reduce the occurrence and cost of oil escape claims. Unfortunately, they continue to occur and the clean up costs are significant. There were 20 new oil escape claims reported in 2006 at an estimated total cost of \$1.5 million dollars. On a positive note, in 2006 we did have some success in recovering some of our costs from installers and manufacturers who were deemed to be at fault.

In 2006, Philip MacDonald, our service agent for Summerside and area, retired after 27 years of service to the Company. Philip experienced many changes over these years and was a significant contributor to the Company's success. On behalf of everyone at PEI Mutual, I thank Philip for his long term service with the Company.

Mark MacDonald from Cornwall, was hired in 2006 as our service agent for part of central Queens County. Mark is a graduate of Nova Scotia Agricultural College and has been employed in the agriculture industry for the past 18 years. I welcome Mark to our team.

I am pleased to advise that PEI Mutual was once again recognized in 2006 by Progress Corp as a "Top 101 Company in Atlantic Canada". PEI Mutual has received this award for each of the past nine years. In 2006, there were seven other companies in PEI that received this award.

PEI Mutual is an Island company owned by its policyholders with its head office located on PEI. Decisions are made promptly on PEI. We are in the business of providing service to our policyholders and it's our goal to give excellent service in an efficient manner. I thank our agents and staff for their hard work in achieving this goal.

Thank you for choosing PEI Mutual as your insurance provider.

Terry Shea
General Manager



AUDITOR'S REPORT

To the Policyholders of Prince Edward Island Mutual Insurance Company. We have audited the balance sheet of Prince Edward Island Mutual Insurance Company as at December 31, 2006 and the statements of earnings and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2006 and the results of its operations and cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Summerside, P.E.I.
February 5, 2007

Grant Thornton LLP
Chartered Accountants



PROTECTING EACH OTHER
SINCE 1885



STATEMENT OF EARNINGS

Year Ended December 31

	2006	2005
Underwriting Income		
Gross premiums written	\$ 12,526,543	\$ 12,359,769
Reinsurance premiums assumed (Note 8)	29,012	34,144
Reinsurance premiums ceded (Note 8)	<u>(1,672,008)</u>	<u>(1,678,911)</u>
Net premiums written	10,883,547	10,715,002
Less: increase in unearned premiums	11,596	675,162
Net premiums earned	<u>10,871,951</u>	<u>10,039,840</u>
Claims and expenses		
Gross claims incurred	6,259,864	5,418,353
Adjusting, legal and appraisals	599,262	604,015
Less: reinsurance recoveries	<u>1,117,643</u>	<u>459,218</u>
Net claims and adjusting	5,741,483	5,563,150
Advertising	93,986	118,408
Canada pension plan	67,068	65,357
Conventions, courses and travel	77,530	69,965
Depreciation	63,928	72,537
Directors fee	189,880	178,773
Donations	67,600	65,300
Employment insurance	34,293	35,625
Fire prevention tax	125,265	123,598
Group insurance	92,008	84,846
Loss prevention	121,045	110,046
Office supplies	87,800	89,550
Other administration costs	186,454	154,776
Postage	102,224	100,766
Premium acquisition expenses	1,553,327	1,559,018
Professional fees	26,507	32,313
Salaries	1,020,262	979,752
Taxes, dues and licences	32,051	37,272
Telephone	43,715	45,683
	<u>9,726,426</u>	<u>9,486,735</u>
Net underwriting earnings	<u>1,145,525</u>	<u>553,105</u>
Other income		
Net investment income (Note 6)	2,703,307	2,395,575
Gain (loss) on sale of property and equipment	809	(18,017)
Miscellaneous	38,730	38,966
	<u>2,742,846</u>	<u>2,416,524</u>
Earnings before income taxes	3,888,371	2,969,629
Income taxes (Note 9) - Current	858,654	698,125
- Future	<u>(61,654)</u>	<u>(114,216)</u>
Net earnings	<u>\$ 3,091,371</u>	<u>\$ 2,385,720</u>

See accompanying notes to the financial statements.



BALANCE SHEET
December 31

Assets	2006	2005
Cash and short term deposits	\$ 1,027,063	\$ 1,534,440
Receivables (Note 3)	1,112,703	1,136,863
Prepaid items	16,746	23,279
Deferred premium acquisition expenses	936,577	806,665
Reinsurers' share of provision for unpaid claims and adjustment expenses	1,200,829	1,555,285
Investments (Note 4)	37,324,057	34,131,853
Property and equipment (Note 5)	504,904	512,314
Future income taxes	290,386	228,732
	<u>\$42,413,265</u>	<u>\$39,929,431</u>
<hr/>		
Liabilities		
Payables and accruals	\$ 245,810	\$ 253,810
Income tax payable	160,530	426,541
Provision for unpaid claims and adjusting expenses	4,685,128	5,030,250
Unearned premiums	6,969,939	6,958,343
	<u>12,061,407</u>	<u>12,668,944</u>
Equity		
Policyholders' security fund, beginning of year	27,260,487	24,874,767
Net earnings	3,091,371	2,385,720
Policyholders' security fund, end of year	30,351,858	27,260,487
	<u>\$42,413,265</u>	<u>\$39,929,431</u>

See accompanying notes to the financial statements.



STATEMENT OF CASH FLOWS
Year ended December 31

	2006	2005
Increase (decrease) in cash and cash equivalents		
Operating		
Net earnings	\$ 3,091,371	\$ 2,385,720
Depreciation	85,059	86,401
Bond premium amortized	83,205	50,907
Gain on sale of investments	(781,175)	(500,367)
(Gain) loss on sale of equipment	(348)	18,017
Future income taxes	(61,654)	(114,216)
	<u>2,416,458</u>	<u>1,926,462</u>
Change in non-cash operating working capital (Note 7)	(352,300)	1,322,576
	<u>2,064,158</u>	<u>3,249,038</u>
Investing		
Purchase of property and equipment	(81,846)	(120,254)
Proceeds on disposal of bonds & equities	5,389,933	4,997,780
Purchase of bonds and equities	(7,884,168)	(7,434,332)
Proceeds on disposal of property and equipment	4,546	8,980
	<u>(2,571,535)</u>	<u>(2,547,826)</u>
Net decrease (increase) in cash and cash equivalents	(507,377)	701,212
Cash and cash equivalents, beginning of year	1,534,440	833,228
Cash and cash equivalents, end of year	\$ 1,027,063	\$ 1,534,440

See accompanying notes to the financial statements.

NOTES TO THE FINANCIAL STATEMENTS
December 31, 2006

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.

2. Summary of significant accounting policies
Depreciation

Depreciation of fixed assets is recorded on the diminishing balance method at the rates indicated in Note 5.

Unearned premiums

The unearned premium reserve is based on the unexpired term of all policies of the Company in force as at December 31.



Deferred premium acquisition expenses

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

Investments

Investments in bonds and debentures are carried at amortized cost. Premiums or discounts incurred on the purchase of bonds and debentures are amortized over the remaining life of the investment. Equities are carried at cost. Gains or losses arising from the disposition of bonds and debentures sold prior to maturity are recognized at the time of sale.

Provision for unpaid claims and adjusting expenses

The provision for unpaid claims represents an estimate for the full amount of all costs including investigation and the projected final settlements of reported claims and for claims incurred but not reported prior to the balance sheet date. These estimates of future loss activity are necessarily subject to uncertainty and are selected from a wide range of possible outcomes. These provisions are adjusted up or down as additional information affecting the estimated amounts become known during the course of claims settlement. All changes in estimates are recorded as incurred claims in the current period.

Premium revenues

Premiums are recognized as earned over the term of the policy on a pro rata basis.

Income taxes accounting policy

The Company uses the tax liability method for determining income taxes. Under this method, future tax assets and liabilities are determined according to differences between their respective carrying amounts and tax basis. Future tax assets and liabilities are measured based on enacted or substantively enacted tax rates and laws at the date of the financial statements for the years in which these temporary differences are expected to reverse. Adjustments to these balances are recognized in earnings as they occur.

Reinsurance

The Company reflects reinsurance balances on the balance sheet on a gross basis to indicate the extent of credit risk related to reinsurance and its obligations to policyholders.

Cash and cash equivalents

Cash and cash equivalents include cash on hand, balances with banks and short term deposits with original maturities of one year or less.

3. Receivables

	2006	2005
Policyholders for premiums	\$ 644,062	\$ 742,567
Accrued interest	450,425	378,336
Other	18,216	15,960
	<u>\$ 1,112,703</u>	<u>\$ 1,136,863</u>

4. Investments

	2006		2005	
	Cost	Market Value	Cost	Market Value
Term deposits and GIC's	<u>\$2,700,000</u>	<u>\$2,700,000</u>	<u>\$1,800,000</u>	<u>\$1,800,000</u>
Bonds at par less unamortized purchase discounts and premiums				
Federal	800,678	851,679	1,101,473	1,184,319
Provincial	15,688,749	17,473,648	15,813,606	17,908,175
Municipal	3,260,277	3,439,824	2,666,017	2,882,581
Corporate	8,338,254	8,438,896	7,027,751	7,306,638
Total bonds	<u>28,087,958</u>	<u>30,204,047</u>	<u>26,608,847</u>	<u>29,281,713</u>
Equities - Canadian				
Common stock	4,959,692	5,996,652	4,328,705	5,414,619
Equities - US				
Common stock	1,576,407	1,782,764	1,394,301	1,307,117
Total	<u>\$37,324,057</u>	<u>\$40,683,463</u>	<u>\$34,131,853</u>	<u>\$37,803,449</u>

Bonds and term deposits - maturity profile

	Within 1 Year	1 to 5 Years	5 to 10 Years	10 to 20 Years	Book Value
Bonds	\$ 2,061,440	\$8,192,012	\$12,508,490	\$5,326,016	\$28,087,958
Term deposits	560,000	2,140,000			2,700,000
Total	<u>\$2,621,440</u>	<u>\$10,332,012</u>	<u>\$12,508,490</u>	<u>\$5,326,016</u>	<u>\$30,787,958</u>
Percent of total	9%	33%	41%	17%	100%

5. Property and equipment

	2006		2005		
	Rate	Cost	Accumulated Depreciation	Net Book Value	Net Book Value
Land		\$132,097	-	\$132,097	\$132,097
Building	5%	456,603	\$258,466	198,137	207,915
Office equipment	20%	175,546	122,019	53,527	55,018
Computer equipment	30%, 45%	184,663	138,808	45,855	59,576
Motor vehicle	30%	143,648	72,718	70,930	52,971
Parking lot	8%	13,715	9,357	4,358	4,737
		<u>\$1,106,272</u>	<u>\$601,368</u>	<u>\$504,904</u>	<u>\$512,314</u>

6. Investment income

	2006	2005
Interest from bonds and short term deposits	\$1,677,890	\$1,673,340
Dividend income	244,242	221,868
Gain on sale of investments	781,175	500,367
	<u>\$2,703,307</u>	<u>\$2,395,575</u>

7. Change in non-cash operating working capital

	2006	2005
Receivables	\$ 24,160	\$ (147,886)
Prepaid expenses	6,533	(6,465)
Deferred premium acquisition expenses	(129,912)	(70,886)
Reinsurers' share of provision for unpaid claims	354,456	707,128
Payables and accruals	(8,000)	(34,758)
Income tax receivable/payable	(266,011)	642,488
Unpaid claims	(345,122)	(442,207)
Unearned premiums	11,596	675,162
	<u>\$ (352,300)</u>	<u>\$ 1,322,576</u>
Income taxes paid	<u>\$ 1,124,665</u>	<u>\$ 271,584</u>

8. Reinsurance

All reinsurance is ceded and assumed from Farm Mutual Reinsurance Plan Inc., a mutual reinsurer incorporated without share capital, of which the Company is a member.

Reinsurance ceded

The Company follows the policy of underwriting and reinsuring contracts of insurance which, in the main limits the liability of



the Company to a maximum amount on any one property loss to \$415,000 and liability loss to \$199,000. The reinsurance contracts also limit the Company's liability on the sum of all individual losses arising out of one event to \$1,200,000. In addition, the Company has obtained reinsurance which limits the Company's overall liability on losses to a maximum of 100% of the Company's earned premium.

Reinsurance assumed

The Company is participating as a reinsurer of losses from catastrophe suffered by members of the Farm Mutual Reinsurance Plan Inc. to the extent of \$150,000 for a single catastrophe loss. The Company's participation commences if a catastrophe loss exceeds \$10 million and reaches the limit of \$150,000 if the loss is \$100 million or greater.

The Company is also participating with a group of Canadian mutual insurance companies as a reinsurer of Agricorp, a crown corporation in Ontario that provides crop insurance to Ontario farmers. The Company's maximum exposure in any one year is \$150,000.

9. Income taxes

Forty two percent (42%) of premiums are from farming and fishing producers. The Company is taxable on the portion of its income that is attributed to non-farming/fishing premiums.

10. Pensions

The Company has a defined contribution plan providing pension, to all of its employees. The total plan expense for the Company's defined contribution plan for all of 2006 was \$113,698 (2005: \$78,892).

11. Financial instruments

The Company's financial instruments consist of cash, receivables, long-term investments, and payables. It is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from these financial instruments. The fair value of these financial instruments approximate their carrying values, unless otherwise noted.

CLAIMS MANAGER

Blair Campbell

Summerside

SAFETY SURVEYOR

Franklin Sanderson

Warren Grove

AGENTS

Cam Trail

Tignish

Jane MacLaurin

Grand River

Paul Power

Summerside

Myles Grady

South Freetown

Bruce Simpson

Bayview

Darren Baglole

Kinkora

Mark MacDonald

Cornwall

Tom Kickham

Souris

David MacAdam

Morell

Peter Johnston

Kinlock

David Walsh

Summerville

Janice Taylor

Montague