SOUTH EASTHOPE MUTUAL INSURANCE COMPANY

CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008

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AUDITORS' REPORT

To the Policyholders,
SOUTH EASTHOPE MUTUAL INSURANCE COMPANY

We have audited the consolidated balance sheet of **SOUTH EASTHOPE MUTUAL INSURANCE COMPANY** as at December 31, 2008 and the consolidated statements of operations, members' surplus, comprehensive (loss) income, accumulated other comprehensive income 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 misstatement. 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, 2008 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

BDO Dunwoody LLP

Chartered Accountants, Licensed Public Accountants

Woodstock, Ontario
January 16, 2009

SOUTH EASTHOPE MUTUAL INSURANCE COMPANY

CONSOLIDATED BALANCE SHEET
AS AT DECEMBER 31, 2008

		2008		2007
ASSETS				
Cash and short-term deposits	**$**	**2,384,235**	$	2,590,563
Due from policyholders		**2,698,107**		2,691,366
Investment income accrued		**90,383**		73,900
Other receivables		**770,687**		288,583
Deferred policy acquisition expenses		**430,897**		429,473
Reinsurer's share of provision for unpaid claims (Note 1)		**4,624,415**		2,995,083
Income taxes recoverable (Note 6)		**544,693**		94,176
Other assets		**33,083**		20,319
Developed software (net)		**243,919**		406,023
Capital assets (Note 3)		**1,063,971**		1,025,755
Customer list (Note 4)		**-**		60,628
Investments (Note 5)		**22,966,389**		23,254,611
	$	**35,850,779**	$	33,930,480
LIABILITIES				
Provision for unpaid claims (Note 1)	**$**	**12,698,545**	$	9,950,994
Unearned premiums		**5,494,109**		5,324,135
Accounts payable and accrued liabilities		**238,591**		216,370
Future income taxes		**40,640**		278,820
Other liabilities		**25,000**		25,000
		18,496,885		15,795,319
MEMBERS' SURPLUS				
Members' surplus		**17,272,369**		17,213,578
Accumulated other comprehensive income		**81,525**		921,583
	$	**35,850,779**	$	33,930,480

On behalf of the Board

______________________________, Director

______________________________, Director

The accompanying notes are an integral part of these financial statements

CONSOLIDATED STATEMENT OF OPERATIONS
FOR THE YEAR ENDED DECEMBER 31, 2008

	2008	2007
UNDERWRITING INCOME		
Gross premiums written	$ 11,398,614	$ 11,118,158
Less reinsurance ceded	2,011,938	1,774,256
Net premiums written	9,386,676	9,343,902
Change in unearned premiums	(169,974)	(195,767)
NET PREMIUMS EARNED	9,216,702	9,148,135
EXPENSES		
Net claims and adjusting expenses incurred	7,847,963	6,801,939
Policy acquisition cost	1,266,094	1,331,519
Salaries, benefits and directors' fees	542,667	555,306
Computer expense	9,038	6,491
Office premise expense	73,134	61,598
Professional fees	38,734	42,361
Premium tax	27,251	26,524
Telephone	44,299	39,781
Printing and stationery	36,631	30,688
Sundry and miscellaneous expense	331,235	314,238
Amortization of capital assets	114,265	146,491
TOTAL CLAIMS AND EXPENSES	10,331,311	9,356,936
NET UNDERWRITING LOSS	(1,114,609)	(208,801)
NET INCOME (LOSS) FROM SUBSIDIARY OPERATIONS (Note 8)	136,586	(172,340)
INVESTMENT INCOME		
Interest and dividends earned	1,102,238	847,689
Gain on disposal of securities	229,221	515,525
Investment expenses	(42,516)	(42,796)
Write down of investments (Note 5)	(273,066)	(82,918)
NET INVESTMENT INCOME	1,015,877	1,237,500
INCOME BEFORE PROVISION FOR INCOME TAXES	37,854	856,359
(RECOVERY OF) PROVISION FOR INCOME TAXES		
Current	(256,475)	207,854
Future	235,538	(88,420)
	(20,937)	119,434
NET INCOME FOR THE YEAR	$ 58,791	$ 736,925

The accompanying notes are an integral part of these financial statements

CONSOLIDATED STATEMENT OF MEMBERS' SURPLUS
FOR THE YEAR ENDED DECEMBER 31, 2008

	2008	2007
BALANCE AT BEGINNING OF YEAR	$ 17,213,578	$ 16,471,269
CHANGE IN ACCOUNTING POLICY	-	5,384
BALANCE AT THE BEGINNING OF YEAR, as restated	17,213,578	16,476,653
NET INCOME FOR THE YEAR	58,791	736,925
BALANCE AT END OF YEAR	$ 17,272,369	$ 17,213,578

NON-CONSOLIDATED STATEMENT OF COMPREHENSIVE (LOSS) INCOME
FOR THE YEAR ENDED DECEMBER 31, 2008

	2008	2007
NET INCOME	$ 58,791	$ 736,925
OTHER COMPREHENSIVE (LOSS) INCOME		
Change in unrealized (loss) gain on available-for-sale financial assets		
Debt securities	478,239	(72,416)
Common shares	(1,549,297)	284,066
Farm mutual pooled fund	(13,496)	993
	(1,084,554)	212,643
Reclassification adjustment for gain included in income		
Common shares	(229,221)	(515,525)
Net unrealized loss	(1,313,775)	(302,882)
Income tax effect	473,717	107,500
	(840,058)	(195,382)
COMPREHENSIVE (LOSS) INCOME	$ (781,267)	$ 541,543

CONSOLIDATED STATEMENT OF ACCUMULATED OTHER COMPREHENSIVE INCOME
FOR THE YEAR ENDED DECEMBER 31, 2008

	2008	2007
BALANCE AT BEGINNING OF YEAR	$ 921,583	$ -
CHANGE IN ACCOUNTING POLICY	-	1,116,965
OTHER COMPREHENSIVE LOSS	(840,058)	(195,382)
BALANCE AT END OF YEAR	$ 81,525	$ 921,583

The accompanying notes are an integral part of these financial statements

CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2008

	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income for the year	**$ 58,791**	$ 736,925
Adjustments for:		
Amortization of capital assets	**348,176**	360,224
Amortization of customer list	**60,628**	60,628
Realized gain from disposal of investments	**(229,221)**	(515,525)
Realized loss from disposal of capital assets	**21,116**	75,240
Write down of investments (Note 5)	**254,832**	82,918
Future income tax provision	**235,538**	(88,420)
	749,860	711,990
Changes in non-cash working capital items	**340,382**	331,781
Total cash from operating activities	**1,090,242**	1,043,771
CASH FLOWS FROM INVESTING ACTIVITIES		
Sale of investments	**1,288,676**	1,775,570
Purchase of investments	**(2,339,839)**	(2,523,469)
Proceeds on disposal of capital assets	**19,500**	9,200
Purchase of capital assets	**(264,907)**	(103,019)
Purchase of customer list	**-**	(4,280)
Total cash used for investing activities	**(1,296,570)**	(845,998)
(DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	**(206,328)**	197,773
CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR	**2,590,563**	2,392,790
CASH AND CASH EQUIVALENTS - END OF YEAR	**$ 2,384,235**	$ 2,590,563

	2008	2007
Income taxes paid during the year	**$ 143,429**	$ 654,502

South Easthope Mutual Insurance Company is incorporated under the laws of Ontario and is subject to the Ontario Insurance Act. It is licensed to write property, liability and automobile insurance in Ontario.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The preparation of financial statements is in accordance with Canadian generally accepted accounting principles, including the requirements of the Financial Services Commission of Ontario. Management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as at the date of the financial statements. Estimates also affect the reported amounts of income and expenses for the reporting period of the statement of operations. Actual results could differ from these estimates.

Basis of presentation of financial statements

These financial statements include the financial statements of South Easthope Mutual Insurance Company and those of its subsidiary company, SEH Computer Systems Inc.

Premiums earned and deferred policy acquisition expenses

(a) Premiums and unearned premiums

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.

Premiums receivable are recorded at amounts due less any required provision for doubtful amounts.

(b) Deferred policy acquisition costs

Acquisition costs are comprised of agents' commissions, premium taxes, and other expenses 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, after considering the related anticipated claims and expenses and investment income. Based on the above there was no premium deficiency for December 31, 2008 and 2007.

Furniture, equipment and automobiles

Furniture, equipment and automobiles are stated at cost less accumulated amortization. Amortization is provided using the straight-line method at rates reflecting the useful lives of the assets (building at 20 years, all others at 5 years).

Financial Instruments

The Company classifies its financial instruments into one of the following categories based on the purpose for which the asset was acquired. The Company's accounting policy for each category is as follows:

Held-for-trading

This category is comprised of cash and cash equivalents. They are carried on the balance sheet at fair value with changes in fair value recognized in the statement of operations. Transaction costs are expensed as incurred.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial Instruments (continued)

Loans and receivables

These assets are non-derivative financial assets resulting from the delivery of cash or other assets by a lender to a borrower in return for a promise to repay on a specified date or dates, or on demand. They arise principally through the provision of goods and services to customers (due from policyholders), but also incorporate other types of contractual monetary assets. They are recognized initially at fair value and subsequently carried at amortized cost, using the effective interest rate method, less any provision for impairment. Transaction costs are expensed as incurred.

Available-for-sale investments

This category is comprised of non-derivative financial assets not included in the above categories and includes investments in debt securities and equity, including the Company's investments in private companies. Investments that have a quoted market price in an active market are carried at fair value with changes in fair value recognized as a separate component of other comprehensive income. Investments that do not have a quoted market price in an active market are carried at cost. Any decline in the fair market value (loss) that is determined to be other than temporary, is removed from other comprehensive income and recognized in the statement of operations. Purchases and sales of these assets are accounted for at settlement date. Transaction costs are included in the amount initially recognized.

Other financial liabilities

Other financial liabilities includes all financial liabilities other than those classified as held-for-trading and comprises trade payables, and other short-term monetary liabilities. These liabilities are initially recognized at fair value and subsequently carried at amortized cost using the effective interest rate method. Transaction costs are expensed as incurred.

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

	Designated held-for-trading	Available-for-sale	Loans and receivables	Other financial liabilities	Total
Cash	$ 2,384,235	$ -	$ -	$ -	$ 2,384,235
Due from policyholders	-	-	2,698,107	-	2,698,107
Investment income accrued	-	-	90,383	-	90,383
Other receivables	-	-	770,687	-	770,687
Investments	-	22,966,389	-	-	22,966,389
Accounts payable and accrued liabilities	-	-	-	(238,591)	(238,591)
	$ 2,384,235	$ 22,966,389	$ 3,559,177	$ (238,591)	$ 28,671,210

Fair values

The fair value of a financial instrument is the amount of consideration that would be agreed upon in an arms length transaction between knowledgeable, willing parties who are under no compulsion to act. The initial value recognized is the transaction price being the fair value of the consideration given or received. Subsequent to initial recognition, the fair values of financial instruments that are quoted in active markets are based on bid prices for financial assets held and offer prices for financial liabilities. When independent prices are not available, fair values are determined by using valuation techniques that refer to observable market data.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial Instruments (continued)

Impaired investments

When the value of any debt security or equity is identified as impaired, the carried amounts are adjusted to estimated realizable amounts. Estimated realizable amounts are measured by discounting reasonably determinable expected future cash flows at the effective interest rate inherent in the investment or using the estimated fair values of underlying security less realization costs or observable market prices. Adjustments to carried amounts are included in investment income in the year the impairment is recognized.

Unpaid claims

The provision for unpaid claims represents an estimate for the full amount of all costs including investigation and the projected final settlements of claims incurred 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 year.

The table below details the provision for unpaid claims and adjustment expenses by risk categories.

	2008		2007	
	Gross	**Ceded**	Gross	Ceded
Long settlement term	**$ 9,802,036**	**$ 4,084,214**	$ 7,594,394	$ 2,986,082
Short settlement term	**2,449,773**	**540,201**	1,926,671	9,001
Facility Association and other residual pools	**446,736**	**-**	429,929	-
	$ 12,698,545	**$ 4,624,415**	$ 9,950,994	$ 2,995,083

Reinsurance ceded

Reinsurance premiums ceded and reinsurance recoveries on losses incurred are recorded as reductions of the respective income and expense accounts. Unearned premiums on business ceded and estimates of amounts recoverable from the reinsurer on unpaid claims and adjustment expenses are recorded on a gross basis.

Income taxes

The Company follows the asset/liability method of accounting for income taxes. Under this method, current income taxes are recognized for the estimated income taxes payable for the current year. Future income tax assets, that are likely to be recognized, and future income tax liabilities are recognized for temporary differences between the tax and accounting basis of assets and liabilities.

Future tax amounts are measured at enacted tax rates expected to be applied to taxable income in the years in which temporary differences are expected to be recovered or settled.

2. CHANGE IN ACCOUNTING POLICY

On January 1, 2008, the Company adopted three new Canadian Institute of Chartered Accountants (CICA) Handbook Sections: Section 1535, Capital Disclosures; Section 3862, Financial Instruments – Disclosures; and Section 3863, Financial Instruments – Presentation. Prior year financial statements have not been restated.

Section 1535 requires disclosure of any entity's objectives, policies, and processes for managing capital; information about what the entity regards as capital; whether the Company has complied with any external capital requirements; and the consequences of not complying with these capital requirements.

Sections 3862 and 3863 replace Handbook Section 3861, Financial Instruments – Disclosure and Presentation. Section 3863 carries forward unchanged the presentation requirements of Section 3861 while Section 3862 requires enhanced financial instrument disclosures focusing on disclosures related to the nature and extent of risks arising from financial instruments and how the entity manages those risks.

Since the purpose of these new standards is to enhance disclosure requirements, they do not have a financial impact on the Company.

3. CAPITAL ASSETS

	2008		2007	
	Cost	**Accumulated Amortization**	Cost	Accumulated Amortization
Land	**$ 413,509**	**$ -**	$ 413,509	$ -
Buildings	**967,032**	**717,493**	963,366	686,831
Land improvements	**42,565**	**42,565**	42,565	42,565
Computer software	**298,805**	**146,474**	167,678	122,495
Computer hardware	**595,152**	**493,384**	608,030	468,391
Automobiles	**158,479**	**70,573**	156,953	96,418
Furniture and fixtures	**273,977**	**215,059**	262,541	172,187
	$ 2,749,519	**$ 1,685,548**	$ 2,614,642	$ 1,588,887
Net book value		**$ 1,063,971**		$ 1,025,755

4. CUSTOMER LIST

A customer list was purchased in 2006 for $146,219. An additional amount of $4,280 was purchased in 2007. This asset was amortized over a two and a half year period which was its estimated useful life. The amount shown on the balance sheet is net of accumulated amortization of $150,499 (2007 - $89,871).

5. INVESTMENTS

The carrying value of bonds and equities by issuer and industry sector as at December 31 is shown in the following table.

	2008			2007		
	Cost	**Fair Value**	**Carrying Value**	Book Value	Fair Value	Carrying Value
Bonds issued by:						
Federal	**$ 1,881,959**	**$ 2,114,045**	**$ 2,114,045**	$ 1,884,181	$ 1,911,818	$ 1,911,818
Provincial	**2,604,712**	**2,678,369**	**2,678,369**	1,963,751	1,944,887	1,944,887
Corporate						
"AAA"	**3,249,984**	**3,368,157**	**3,368,157**	3,262,177	3,227,573	3,227,573
"AA"	**2,247,252**	**2,185,560**	**2,185,560**	2,390,133	2,311,695	2,311,695
"A"	**630,561**	**597,862**	**597,862**	632,626	588,181	588,181
	10,614,468	**10,943,993**	**10,943,993**	10,132,868	9,984,154	9,984,154
Farm Mutual Pooled Fund						
Canadian Fixed Income	**7,505,611**	**7,552,543**	**7,552,543**	7,112,175	7,172,603	7,172,603
Equity investments						
Canadian common						
Finance/Utility	**1,747,071**	**1,560,142**	**1,560,142**	1,513,528	2,033,110	2,033,110
Consumer	**602,051**	**535,038**	**535,038**	421,602	419,440	419,440
Mining/Energy/Industrials	**1,576,463**	**1,788,814**	**1,788,814**	1,772,171	2,929,902	2,929,902
U.S. common						
Finance/Utility	**149,528**	**42,736**	**42,736**	150,642	91,650	91,650
Consumer	**253,754**	**229,299**	**229,299**	267,177	179,058	179,058
Mining/Energy/Industrials	**133,163**	**90,003**	**90,003**	111,738	148,490	148,490
Technology	**237,123**	**192,273**	**192,273**	246,795	199,674	199,674
	4,699,153	**4,438,305**	**4,438,305**	4,483,653	6,001,324	6,001,324
Fire Mutuals Guarantee Fund	**31,548**	**N/A**	**31,548**	30,530	N/A	30,530
Other investments - FMFS	**-**	**N/A**	**-**	66,000	N/A	66,000
	$ 22,850,780	**$ 22,934,841**	**$ 22,966,389**	$ 21,825,226	$ 23,158,081	$ 23,254,611

The maximum exposure to credit risk would be the fair value as shown above.

The estimated fair value of bonds and pooled funds are based on quoted market values. The estimated fair value of equities are determined using last bid price.

Investments in the Fire Mutuals Guarantee Fund and Farm Mutual Financial Services Inc. (FMFS) do not have quoted market values. These investments have been recorded at cost for accounting purposes.

5. INVESTMENTS (continued)

Based on the analysis by the equity portfolio investment managers, equities that have declined from their cost value at December 31, 2008 and are anticipated to have a prolonged or doubtful prospect of recovery to cost due to economic uncertainty in their respective sectors were deemed as other than temporary impaired and written down. While these equities have potential for values to improve, it is considered unlikely these stock values will recover to the point of their initial purchase price. During the year, the Company determined that an other than temporary impairments occurred in specific equity investments. As a result, a writedown of $188,832 has been recognized in the statement of operations.

Equities that have declined from their purchase price at December 31, 2008 in sectors where improvement is probable within the a timeframe consistent to the investment managers conservative strategy were deemed as temporarily impaired and not written down.

In August 2008, Farm Mutual Financial Services Inc. (FMFS) entered into bankruptcy protection. Due to this development, the Company's investment of $66,000 in this corporation was written off.

During the year, the Company advanced Mutual Financial Solutions Inc. $18,233 to equalize shareholder ownership. The advance was determined to be uncollectible and written off.

Liquidity

Maturity profile as at December 31, 2008

	2008		2007	
	Cost	**Fair Value**	Cost	Fair Value
Maturing within one year	**$ 853,205**	**$ 862,803**	$ 784,985	$ 781,593
Maturing between one and five years	**4,154,721**	**4,191,583**	3,678,492	3,595,526
Maturing over five years	**5,606,542**	**5,889,607**	5,669,391	5,607,035
	$ 10,614,468	**$ 10,943,993**	$ 10,132,868	$ 9,984,154

The effective interest rate at December 31, 2008 for debt securities is 4.22%.

6. INCOME TAXES

The Company is subject to income taxes on that portion of its income derived from insuring other than farm related risks.

7. PENSION PLAN

The Company makes contributions to the Ontario Mutual Insurance Association Pension Plan, which is a multi-employer plan, on behalf of its staff. The plan is the greater of a defined benefit plan or a money purchase plan. A defined benefit plan specifies the amount of the retirement benefit to be received by the employees based on length of service and rates of pay. A money purchase plan is the amount to be received by the employees based on the investing of the pension assets and the return they have received during the length of service.

The amount contributed to the plan in 2008 was $115,183 (2007 - $108,384) for current service.

8. SUBSIDIARY OPERATIONS

REVENUE	**$**	**1,163,804**	$	760,904
EXPENSES				
Salaries and benefits		**566,508**		522,455
Amortization		**213,392**		213,733
General and administrative		**162,815**		84,833
Premise expenses		**67,723**		45,351
Loss on disposal of assets		**16,780**		66,872
		1,027,218		933,244
NET INCOME (LOSS) FROM SUBSIDIARY OPERATIONS	**$**	**136,586**	$	(172,340)

Intercompany revenue and expenses have been removed from the above statement of subsidiary operations.

9. 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.

The regulators measure the financial strength of property and casualty insurers using a minimum capital test (MCT). The regulators generally expect property and casualty companies to comply with capital adequacy requirements. This test compares a Company's capital against the risk profile of the organization. The risk-based capital adequacy framework assesses the risk of assets, policy liabilities and other exposures by applying various factors. The regulator indicates that the Company should produce a minimum MCT of 150%. The regulator has the authority to request more extensive reporting and can place restrictions on the Company's operations if deemed necessary.

In an actuarial study done, the Net Risk Ratio was shown to have a high correlation to the MCT. As a result of these findings the Company uses Net Risk Ratio (surplus to gross premiums written) to monitor capital adequacy.

The minimum net risk ratio set out by the regulators is 1:2 (50%). The ratio that the board of directors desires for the Company is more conservative at 3:2 (150%) with a minimum not less than a 2:2 (100%). The risk ratio for the Company at December 31, 2008 was 152%.

The Company's objective is to maintain this ratio by increasing surplus in proportion to written premium. Accordingly, this ratio is the primary consideration in determining the amount of new business written, allocating new business budgets for agents and brokers and policyholder premium refunds in years the Company realizes an underwriting profit.

For the purpose of capital management, the Company considers capital as policyholders' equity excluding accumulated other comprehensive income.

Reinsurance

The Company purchases excess of loss reinsurance which limits the liability of the Company on property, liability and automobile insurance contracts to a maximum amount on any one claim of $200,000 plus 10% of the excess up to $1,000,000. 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 100% of gross net earned premium for liability and automobile.

In 2008 Catastrophe reinsurance was purchased to protect capital from catastrophic losses as the frequency and severity of these losses are inherently unpredictable. To limit the potential impact of a catastrophic event, catastrophe reinsurance limits the Company's exposure to $600,000 plus 5% of the remaining loss in one event. The $600,000 net retained amount represents approximately 3% of Company's capital.

10. CONTINGENT LIABILITIES

Pursuant to an agreement effective January 1, 1976, the Company is a member of the Fire Mutuals Guarantee Fund ("the Fund"). The Fund was established to provide payment of outstanding policyholders' claims if a member company becomes bankrupt. As a result, the Company may be required to contribute assets to their proportionate share in meeting this objective.

11. FINANCIAL INSTRUMENT RISK MANAGEMENT

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.

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. The bond portfolio remains very high quality with 100% of the bonds rated A or better. All fixed income portfolios are measured for performance on a quarterly basis and monitored by management on a monthly basis.

Reinsurance is placed with Farm Mutual Reinsurance Plan Inc. (FMRP), a Canadian registered reinsurer. Management monitors the creditworthiness of FMRP 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 receivables are short-term in nature and are not subject to material credit risk.

The maximum exposure to investment credit risk and concentration of this risk is outlined in note 5.

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. The Policy limits the investment in any one corporate issuer rated "AAA/AA" to a maximum of 5% and "A" to a maximum of 2.5% of the Company's fixed income portfolio. There is no single issuer limit on securities of the Government of Canada or of Provinces and guaranteed Crown Corporations rated A- or better.

The Company's investment policy limits investment in the Farm Mutual Canadian Fixed Income Pool Fund to a maximum of 50% of assets available to be invested. Funds are invested in bonds and debentures of Federal, Provincial or Municipal Government and Canadian companies rated BBB or better. The fund is monitored by the Farm Mutual Pooled Fund Investment Committee appointed by the Ontario Mutual Insurance Association.

Derivative instruments are not used in any investment activity.

11. FINANCIAL INSTRUMENT RISK MANAGEMENT (continued)

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 15% of the equity portfolio 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 $5,500 which would be reflected in other 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 exposed to this risk through its interest bearing investments (T-Bills, GICs, Bonds).

Historical data and current information is used to profile the ultimate claims settlement pattern by class of insurance, which is then used in a broad sense to develop an investment policy and strategy. However, because a significant portion of the Company's assets relate to its capital rather than liabilities, the value of its interest rate based assets exceeds its interest rate based liabilities. As a result, generally, the Company's investment income will move with interest rates over the medium to long-term with short term interest rate fluctuations creating unrealized gains or losses in other comprehensive income. There are no occurrences where interest would be charged on liabilities; therefore, little protection is needed to ensure the fair market value of assets will be offset by a similar change in liabilities due to an interest rate change.

The objective of the policies and procedures for managing interest rate risk is to diversify the bond portfolio in such a way that the bonds are a portfolio laddered over 10 years. One tenth of the bond portfolio would come due each year and be reinvested. This protects the Company from fluctuations in the interest rates.

At December 31, 2008, a 1% move in interest rates, with all other variables held constant, could impact the market value of bonds by $500,000. This change in market value would impact other comprehensive income.

At December 31, 2008, a 1% move in interest rates, with all other variables held constant, could impact the market value of the pooled funds by $500,000. This change in market value would impact other 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.

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 affect on the fair values of the Company's Canadian common and United States common of $ 450,000. This change in fair values would impact other comprehensive income.

11. FINANCIAL INSTRUMENT RISK MANAGEMENT (continued)

The Company's investment policy limits equity investments to 25% of total assets in accordance with the Insurance Act. Investment managers are mandated to follow the same conservative strategy that they have demonstrated to the Company since 1992. All stocks must be freely tradable and listed on a recognized stock exchange in Canada or the US. The Company investment policy limits the investment in any single issuer to a maximum of 15% by market value of the equity portfolio. In the 10 global classification sectors, sector weights are limited to a maximum of 35%. Holdings in four sectors (Technology, Consumer, Energy/Industrials and Financial/Utilities) are maintained within 50% to 150% of the BMO/TSX CAP 10% index. The Investment Manager must suspend further sales when net realized losses in one quarter exceed $40,000.

Equities are monitored by the board of directors and holdings are adjusted following each quarter when they are out of balance with the investment policy.

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. Applicable reinsurance recoveries in excess of the Company's retention are submitted immediately upon confirmation of the claim.

The Company's investment policy requires that 2.5% to 7.5% of assets available for investments to be held in cash in an interest bearing bank demand account which includes a pre-approved line of credit to meet immediate cash flow requirements.

The administrator of the Farm Mutual Pooled Funds held by the Company entered into bankruptcy protection during the year. Due to the uncertainty surrounding the bankruptcy, the custodian of these funds has frozen any contributions or withdrawals by the unit holders. The funds continue to be managed according to the investment mandate, but no purchase or sale of these units will be allowed until the uncertainty is resolved.

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.

12. GOVERNMENT REGULATION OF AUTOMOBILE INSURANCE

The Company's automobile insurance rates are subject to approval by the Financial Services Commission of Ontario (FSCO). Application for automobile rate changes are presented to FSCO by the Farm Mutual Reinsurance Plan (FMRP) on behalf of some members of Ontario Mutual Insurance Association (OMIA). The rate filings include actuarial justification for the rate increases or decreases. All rate filings must be approved by FSCO prior to implementation.

13. NEW ACCOUNTING PRONOUNCEMENTS

Recent accounting pronouncements that have been issued but are not yet effective, and have a potential implication for the Company, are as follows:

Financial Statement Concepts

CICA Handbook Section 1000, Financial Statement Concepts has been amended to focus on the capitalization of costs that truly meet the definition of an asset and de-emphasizes the matching principle. The revised requirements are effective for annual and interim financial statements related to fiscal years beginning on or after October 1, 2008. The Company is currently evaluating the impact of the adoption of this change on the disclosure within its financial statements.

Goodwill and Intangible Assets

Section 3064 incorporates guidance to clarify the recognition of intangible assets and address and recognition and measurement of internally developed intangible assets. The new standards are effective for interim and annual financial statements beginning on or after October 1, 2008. The Company is currently evaluating the impact of this new standard.

International financial reporting standards

The Accounting Standards Board has confirmed that all publicly accountable enterprises will have to comply with IFRS for fiscal years beginning on or after January 1, 2011. The Company understands there to be differences between current Canadian GAAP and IFRS, and have undertaken a project to understand the possible future effects on the financial statements.