7. INSURANCE CONTRACTS (Continued)

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 reinsurer's share requires the estimation of three major variables which are the development of claims, reinsurance recoveries and future investment income.

The Superintendent of the Financial Services Commission of Ontario has required that consideration of future investment income be disregarded except in the evaluation of automobile accident benefit claims.

Claim development

The estimation of claim development involves assessing the future behaviour 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 2007 to 2015. 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.

In 2011, the year of adoption of IFRS, only information from periods beginning on or after January 1, 2007 was required to be disclosed. This is being increased in each succeeding additional year, until ten years of information is included.

7. INSURANCE CONTRACTS (Continued)

Gross claims (000's)	2007	2008	2009	2010	2011	2012	2013	2014	2015	Total
Gross estimate of cumulative claims cost										
At the end year of claim	1,941	3,570	4,207	3,882	4,655	3,108	2,288	3,242	5,165	
One year later	1,782	3,500	3,402	3,218	4,366	2,709	2,343	3,557		
Two years later	1,874	3,113	4,472	2,812	4,261	2,359	2,380			
Three years later	1,811	2,712	4,274	3,796	4,582	2,301				
Four years later	1,744	2,648	4,335	3,774	4,341					
Five years later	1,703	2,644	4,300	3,751						
Six years later	1,683	2,587	4,356							
Seven years later	1,670	2,587								
Eight years later	1,670									
Current estimate of cumulative claims cost	1,670	2,587	4,356	3,751	4,341	2,301	2,380	3,557	5,165	30,108
Cumulative payments	1,670	2,587	3,121	3,721	3,905	1,842	2,011	2,453	2,089	23,399
Outstanding claims	-	-	1,235	30	436	459	369	1,104	3,076	6,709
Outstanding claims 2006 and prior										63
Provision for claims incurred but not reported										2,908
Total gross outstanding claims										9,680

CAYUGA MUTUAL INSURANCE COMPANY

7. INSURANCE CONTRACTS (Continued)

Net of reinsurance (000's)	2007	2008	2009	2010	2011	2012	2013	2014	2015	Total
Net estimate of cumulative claims cost										
At the end year of claim	1,869	3,372	3,552	3,109	3,895	2,832	2,288	3,037	4,485	
One year later	1,753	3,122	2,851	2,577	3,633	2,433	2,334	3,369		
Two years later	1,786	2,719	3,058	2,283	3,508	2,263	2,380			
Three years later	1,688	2,422	2,861	2,309	3,572	2,194				
Four years later	1,676	2,350	2,923	2,304	3,572					
Five years later	1,626	2,346	2,930	2,319						
Six years later	1,614	2,276	2,921							
Seven years later	1,614	2,276								
Eight years later	1,614									
Current estimate of cumulative claims cost	1,614	2,276	2,921	2,319	3,572	2,194	2,380	3,369	4,485	25,130
Cumulative payments	1,614	2,276	2,698	2,289	3,283	1,901	2,011	2,265	2,089	20,426
Outstanding claims	-	-	223	30	289	293	369	1,104	2,396	4,704
Outstanding claims 2006 and prior										66
Provision for claims incurred but not reported										1,162
Total net outstanding claims										5,932

CAYUGA MUTUAL INSURANCE COMPANY

8. OTHER PROVISIONS AND CONTINGENT LIABILITIES

In common with the insurance industry in general, the Company is subject to litigation arising in the normal course of conducting its insurance business which is taken into account in establishing the provision for unpaid claims and adjustment expenses.

The Company is a member of the Farm Mutual Reinsurance Plan Inc. ("the Plan"), which is a general reinsurer that shares in the insurance risks originally accepted by member insurance companies. As a member of the Plan, the Company may be required to contribute additional capital to the Plan in the form of subordinated debt should the Plan's capital fall below a prescribed minimum.

9. PENSION PLAN

The Company makes contributions on behalf of its employees to “The Retirement Annuity Plan for Employees of the Ontario Mutual Insurance Association and Member Companies”, which is a multi-employer plan. Each member company has signed an Ontario Mutual Insurance Association Pension Plan Agreement. Eligible employees participate in the defined benefit plan. The defined benefit plan specifies the amount of the retirement benefit to be received by the employee based on the number of years the employee has contributed and his/her final average earnings. The plan is accounted for as a defined contribution plan as insufficient information is available to account for the plan as a defined benefit plan. The Company is one of a number of employers that participates in the plan and the financial information provided to the Company on the basis of the contractual agreements is insufficient to reliably measure the Company’s proportionate share in the plan assets and liabilities on defined benefit accounting requirements.

The Company contributes 13% of employee earnings and funds the excess defined benefit based on the Company’s percentage of pensionable earnings as calculated by the Pension Plan actuaries. The Pension Plan agreement states that the Company is responsible for its share of any deficit as a result of any actuarial valuation or cost certificate. The minimum funding requirement is the solvency valuation amount determined by the Pension Plan actuary on the valuation dates prescribed by the Pensions Benefit Act. In the event of a wind-up, voluntary withdrawal or bankruptcy, either by the Company or the group as a whole, the Company is responsible for its portion of all expenses and deficit related to such.

The amount contributed to the plan for 2015 was $56,323 (2014 - $53,753). The contributions were made for current service and these have been recognized in comprehensive income. The Company had a 1.11% share of the total contributions to the Plan in 2015.

An actuarial valuation of the Pension Plan as of December 31, 2013 showed a going-concern surplus position. The next actuarial valuation to be filed under the Pension Benefit Act will be as of December 31, 2016.

9. PENSION PLAN (Continued)

In 2013 there was a contractual requirement to provide additional funding which resulted in a lump sum payment of $76,008 recognized in comprehensive income.

Expected contributions to the plan for the next annual reporting period amount to $47,293, which is based on payments made to the multi-employer plan during the current fiscal year.

The defined benefit plan has been closed to future eligible employees effective July 1, 2013. The Company and all current employees who are accruing benefits under the defined benefit plan continue to contribute to the defined benefit plan according to the existing terms of the agreement.

Future eligible employees are enrolled in the defined contribution plan. The Company's obligation with respect to this plan is to make specified monthly contributions based on a percentage of employee's eligible earnings. The amount contributed to the plan for 2015 was $62,335 (2014 - $46,646) and this has been recognized in comprehensive income.

10. INCOME TAXES

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

The significant components of tax expense included in net income are composed of:

	2015	2014
Current tax expenses		
Based on current year taxable income	-	496,854
Adjustments for over / under provision in prior periods	(12,155)	-
	(12,155)	496,854
Deferred tax expense		
Origination and reversal of temporary differences	(59,726)	13,576
Total income tax expense (recovery)	(71,881)	510,430

Reasons for the difference between tax expense for the year and the expected income taxes based on the statutory tax rate of 26.50% (2014 - 26.50%) are as follows:

	2015	2014
Income (Loss) for the year before income taxes	(116,461)	2,028,141
Expected taxes based on statutory rate of 26.50% (2014 - 26.50%)	(30,862)	537,457
Small business deduction	-	(9,810)
Non deductible portion of claims liabilities	26,482	(5,769)
Other non deductible expenses	1,739	1,225
Capital cost allowance in excess of depreciation	31,920	(8,539)
Over (under) provision in prior years	(12,155)	-
Other	(29,279)	(17,710)
Current income tax expense (recovery)	(12,155)	496,854

10. INCOME TAXES (Continued)

The movement in 2015 deferred tax liabilities and assets are:

	Opening balance at January 1, 2015	Recognized in net income	Closing balance at December 31, 2015
Deferred tax liabilities			
Property, plant and equipment	(40,133)	33,244	(6,889)
Deferred tax assets			
Claims liabilities	52,124	26,482	78,606
Other	-	-	-
2015 net deferred income tax	11,991	59,726	71,717

	Opening balance at January 1, 2014	Recognized in net income	Closing balance at December 31, 2014
Deferred tax liabilities			
Property, plant and equipment	(32,325)	(7,808)	(40,133)
Deferred tax assets			
Claims liabilities	57,892	(5,768)	52,124
2014 net deferred income tax	25,567	(13,576)	11,991

	2015	**2014**
Deferred tax liabilities		
Deferred tax liabilities to be settled within 12 months	(6,889)	(40,133)
Deferred tax liabilities to be settled after more than 12 months	-	-
	(6,889)	(40,133)

	2015	**2014**
Deferred tax assets		
Deferred tax assets to be settled within 12 months	78,606	52,124
Deferred tax asset to be settled after more than 12 months	-	-
	78,606	52,124

11. GROSS CLAIMS AND ADJUSTMENT EXPENSES

Included in claims expenses were wage and benefit costs of $306,869 (2014 - $133,171).

12. SALARIES, BENEFITS AND DIRECTORS FEES

	2015	2014
Underwriter salaries and benefits	234,687	140,176
Sales salaries and commissions	792,286	790,743
Other salaries, benefits and directors fees	631,863	894,988
	1,658,836	1,825,907

13. 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:

	2015	2014
Compensation		
Management salaries and director's fees	196,483	209,581
Total pension and other post-employment benefits	15,336	16,088
	211,819	225,669
Premiums	63,190	69,346
Claims paid	7,777	7,364

Amounts owing to and from key management personnel at December 31 are $nil (2014 - $nil) and $1,713 (2014 - $16,668) respectively. The amounts are included in due from policyholders and accounts payable and accrued liabilities on the statement of financial position.

14. CAPITAL MANAGEMENT

The Company's objectives in managing its capital are to maintain financial stability for policyholders and meet regulatory requirements. Mutual insurance companies are regulated by the provisions of the Insurance Companies Act (ICA) and the Financial Services Commission of Ontario (FSCO).

The Company has a capital management process in place to monitor its capital. Reinsurance placed with Farm Mutual Reinsurance Plan and the Farm Mutual Guarantee Fund serve to protect capital and limit losses on any one claim (see Note 15). The Company meets its objectives for managing capital through management and Board monitoring and oversight of regulatory capital measures.

The Company's capital consists of unappropriated members' surplus. The Company's capital structure at December 31 was as follows:

	2015	**2014**
Unappropriated members' surplus	16,663,171	16,707,751
Total Capital	16,663,171	16,707,751

The Company is subject to an annual examination by the Financial Examination Committee, the results of which are reported to the Superintendent of Financial Institutions for Ontario. In its most recent examination report, the Company was in compliance with regulatory expectations. 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.

15. FINANCIAL INSTRUMENT AND INSURANCE RISK MANAGEMENT

Insurance risk management

The principal risk that 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 risks mitigation program. Retention limits for the excess-of-loss and quota share 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 its reinsurer is unable to meet its obligations assumed under such reinsurance agreements.

15. FINANCIAL INSTRUMENT AND INSURANCE RISK MANAGEMENT (Continued)

Insurance risk management (Continued)

The Company writes insurance primarily over a 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 Ontario.

The Company manages this risk via its underwriting and reinsurance strategy with 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. Automobile premiums are subject to approval by the Financial Services Commission of Ontario and therefore may result in a delay in adjusting the pricing to exposed risk; in this case the Company has policies regarding renewal and new business accepted. Reinsurance is purchased to mitigate the effect of the potential loss to the Company. Reinsurance is placed with Farm Mutual Reinsurance Plan Inc. (FMRP), a Canadian registered reinsurer.

The Company follows the policy of underwriting and reinsuring contracts of insurance which, in the main, limit the liability of the Company to a maximum amount on any one claim of $350,000 (2014 - $350,000) in the event of a property claim, an amount of $350,000 (2014 - $350,000) in the event of a liability claim, and an amount of $350,000 (2014 - $350,000) in the event of an automobile claim. For claims occurring prior to 2013, for amounts over the respective limits there is a 10% retention to a specified maximum. The Company also obtained reinsurance which limits the Company's liability 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 100% of gross net earned premiums for automobile and liability.

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 at December 31, 2015 and December 31, 2014.

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 7.

15. FINANCIAL INSTRUMENT AND INSURANCE RISK MANAGEMENT (Continued)

Insurance risk management (Continued)

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		Auto Claims		Liability Claims	
	2015	**2014**	**2015**	**2014**	**2015**	**2014**
5% increase in loss ratios						
Gross	181,995	165,213	201,231	195,725	30,257	28,516
Net	160,129	150,594	161,141	158,756	22,241	20,970
5% decrease in loss ratios						
Gross	(181,995)	(165,213)	(201,231)	(195,725)	(30,257)	(28,516)
Net	(160,129)	(150,594)	(161,141)	(158,756)	(22,241)	(20,970)

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.

The Company's investment policy puts limits on the bond portfolio including portfolio composition limits, and bond quality limits. Funds should be invested in bonds and debentures of Federal, Provincial or Municipal Government and corporations initially 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 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 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.

15. FINANCIAL INSTRUMENT AND INSURANCE RISK MANAGEMENT (Continued)

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 its stock holdings. Foreign currency changes are monitored by the board of directors.

A 1% change in the value of the United States dollar would affect the fair value of stocks and cash by approximately $60,977 (2013 - $21,124), which would be reflected in the statement of comprehensive income.

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 (GICs and 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. 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.

In order to manage interest rate risk, the Company varies the maturity dates of bonds to avoid a significant number of bond maturities occurring at the same date. In addition, the Company avoids placing a significant amount of investments with a specific bond issuer.

The impact of an assumed 1% (100 basis point) decrease in interest rates on renewal of fixed rate investments maturing within the next twelve months would decrease investment income in the next twelve month period by approximately $3,000 (2014 - $3,000).

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

15. FINANCIAL INSTRUMENT AND INSURANCE RISK MANAGEMENT (Continued)

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. At December 31, 2015, a 10% movement in the stock market with all other variables held constant would have an estimated effect on the fair values of the Company's equity fund of $673,835 (2014 - $687,207). This change would be recognized in investment income.

The Company's investment policy limits investment in pooled funds, preferred and common shares to a maximum of 25% of assets.

Equities are monitored by the board of directors and holdings are adjusted following each quarter when the investments are offside of 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.

The Company holds a portion of its investment portfolio in cash and short-term investments.

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.