Farm Mutual
Reinsurance
Plan Inc.

Contents

Directors and Officers

Seated, left to right: *Marie Byrne,* Recording Secretary/Office Manager; *John Harper,* President Emeritus; *Earl Harder,* Chairman, Director, Western Canada (2004); *Steve Smith,* President & C.E.O.; *Kathryn Adie,* First Vice Chair, Director, Group 5 (2005); *Joe Facey,* Director, Group 2 (2006).

Standing, left to right: *Michael O'Shea,* First Vice Chair, Canadian Director-at-large, (2005); Bruce Williams, Director, Eastern Canada (2006); *Terry Malcolm,* Ontario Director-at-large (2004); *Robert Forsythe,* Senior Vice President; *John Leeson,* Director, Group 1 (2005); *Doug Crockett,* Director, Group 4 (2005); *Bruce Caughey,* Director, Group 7 (2006); *Brian Bessey,* Director, Group 3 (2004); *Tom Smith,* Vice President & C.F.O.; *Philip Brett,* Past Chairman, Director, Group 6 (2004); *Serge Gauthier,* Director, Group 8 (2006).

Five Year Financial Highlights

	2003	restated 2002	2001	2000	1999
Revenue					
Premiums Earned	**$ 139,633**	$ 100,979	$ 78,153	$ 63,584	$ 58,045
Commission Earned	**212**	218	508	578	582
	139,845	101,197	78,661	64,162	58,627
Expenditures					
Gross Claims Incurred	**112,832**	77,324	50,783*	66,522*	58,006*
Reinsurance Recovery	**(6,901)**	(7,081)	(11,611)*	(14,443)*	(23,456)*
Premiums Ceded	**16,645**	16,235	13,888	12,999	10,736
Commission Expense	**17,561**	8,488	6,398	4,051	3,747
Operating Expenses	**5,809**	5,156	4,316	4,111	3,877
	145,946	100,122	63,774	73,240	52,910
Underwriting Gain (Loss)	**(6,101)**	1,075	14,887	(9,078)	5,717
Investment Income	**10,655**	(90)	11,981	29,544	8,834
Refund of Premiums	**–**	(6,800)	(5,500)	(5,100)	(4,700)
Taxes	**(385)**	1,764	(5,510)	(3,930)	(2,423)
Net Earnings (Loss) for the Year	**$ 4,169**	$ (4,051)	$ 15,858	$ 11,436	$ 7,428
Surplus and Reserves	**$ 130,877**	$ 126,708	$ 125,218	$ 109,360	$ 97,924

*Claims have not been discounted due to lack of historical data.

Operations and Staff

Seated, left to right: *Olivia Melo,* Claims; *Ursula Yetman,* Claims, *Kathleen Seemann,* Office Services; *Krista Guia Pereira,* Claims; *Cynthia White,* Underwriting; *Carol Homer,* Administrative Offices; *Krista Seiling,* Underwriting.

Standing, left to right: *George Mihailov,* Accounting; *Jackie Brouwers,* Claims; *Jane Williams,* Reinsurance; *Jack Black,* EDP Manager; *Shannon Simpson,* EDP; *Jessie Louks,* Claims; *Sandra Wiseman,* Accounting; *Jeff Consitt,* Assistant Claims Manager; *Angela Boost,* Underwriting; *Richard Soehner,* Underwriting; *Greg Hutchinson,* Co-op Student; *Robert Brenner,* Claims Manager; *Sharon Godden,* EDP; *Susan McDonald,* Claims; *Jeff Barnard,* Reinsurance Manager; *Tracey Schneider,* EDP; *John Knill,* Underwriting Manager; *Marie Gorman,* Office Services.

The Claims Department is pleased to announce the addition of Olivia Melo to our staff. Olivia is working in the capacity of Claims Technician.

The Underwriting and Reinsurance Departments welcome Krista Seiling as Underwriting/Reinsurance Assistant.

Chairman's Message

On behalf of the Board of Directors, it is a pleasure to present the 2003 Annual Financial Statement.

We are pleased to report a welcome improvement in our financial performance, with the Corporation posting a net gain of $4.1 million for the period. The significant increase in premiums written during the period reflects the continued growth of our expanding Class "A" membership base and our planned expansion in underwriting property business for mutual insurance companies in the United States.

Although we are reporting a net profit for the year, underwriting experience in our core business areas deteriorated during the period. Management reports will confirm our need to continue to examine and implement programs that focus on improving performance in the Property Excess of Loss and Automobile Reinsurance programs.

Our Succession Planning Committee completed their mandate of assisting the Board of Directors in selecting Steve Smith as President and CEO of the Corporation and we are pleased to welcome him into the organization. The support and assistance provided by our professional operational staff and management have been a key component in the successful transition into the leadership of the organization.

President Emeritus, John Harper, will retire from the Corporation in June of 2004, following three decades of service to FMRP and the mutual insurance industry. We look forward to celebrating and acknowledging his contributions with his many mutual friends and business colleagues in conjunction with our upcoming annual meeting in Toronto.

During 2003, two Directors announced that they would not be seeking re-election to the Board of Directors. We want to acknowledge the contributions that Terry Malcolm, FMRP Ontario Director at Large (Director, Farmer's Mutual Insurance Company, Lindsay, Ontario) and Philip Brett, FMRP Director Group 6 (Director, Dufferin Mutual Insurance Company, Shelburne, Ontario) have made to the organization, both having served on the Board since their election in 1994. Terry and Phil have served as Chairmen of the Board and both have played a leadership role in the continuing development of the organization.

It has been my privilege and pleasure to serve as the Chairman of the FMRP over the last year. We could not have accomplished so much without the cooperation and dedication of your Board of Directors, management and staff, all of whom take a very active role in developing the programs that will "Empower our Members for Mutual Success".

We encourage you to attend and participate in our Annual General Meeting which will be held in the Sheraton Center Hotel, Toronto, Ontario, on Wednesday, March 24th, 2004 at 1:00 P.M.

Earl Harder
Chairman of the Board

Report to the Members

Despite the deterioration in our overall underwriting results, we are pleased to report a net profit for the year of $4.1 million. A significant improvement in the performance of our investment portfolio, combined with the implementation of accounting procedures related to the discounting of outstanding loss reserves, resulted in an increase to the earned surplus position of the company to over $130 million.

Our combined ratio was 105% for the year which produced an underwriting loss of $6.1 million for the period. We saw a significant increase in premiums written reflecting the continuing growth and expansion of our Class "A" membership base and the planned expansion of our underwriting activities involving mutual insurance companies in the United States.

Increases in overall operating expenses of over 72% are directly attributable to commissions paid by FMRP on Proportional Reinsurance programs. This reflects an increase in the use of proportional reinsurance products by Class "A" members combined with the expansion of our business in the United States, much of which is transacted on a proportional basis.

Results in property business improved with premiums assumed now exceeding $79 million. In total, the property portfolio produced an underwriting gain of over $1.8 million for the period. The Property Excess of Loss program continues to produce dismal results with gross excess of loss claims exceeding $25 million for the year. Large individual losses continue to impact the program and our reinsurance partners. The Property Excess of Loss line produced an

Report to the Members *(continued)*

underwriting loss of over $3.9 million. There was significant activity in the Catastrophe program across the country with the most significant and severe events being Hurricane Juan, affecting our members in the Maritime Provinces, and a hailstorm in Manitoba. A number of Class "A" members have incorporated proportional reinsurance (quota share) in their reinsurance programs which has increased our volume in this line of business. Proportional reinsurance programs, together with other ancillary lines such as Farmers Accident and individual facultative placements, combined to produce an underwriting loss of $1.7 million for the year.

In accordance with our strategic plan, we have increased our activities in underwriting business for mutual insurance companies in the United States. Annually, premiums assumed for Class "C" business now exceed over $28 million. This portion of our business includes the Crop Reinsurance programs in Ontario and Manitoba, both of which produced very good results for the year. Exceptionally good results on our expanded activities in the United States produced the bulk of the $5.5 million underwriting profit for this line of business. The profit produced by Class "C" business was sufficient to offset losses in the balance of our property portfolio and was the dominant factor in the overall improvement in performance.

Experience in our liability portfolio was much improved with the line producing an underwriting gain for the period of over $1 million. Claims frequency and severity appear to be returning to more historical norms following our erratic performance in recent years. Increases in premium volume reflect the increase in the use of proportional reinsurance products in Class "A" member reinsurance programs.

Experience in our automobile portfolio deteriorated in comparison to our exceptional performance in recent years. Premiums assumed increased to over $46 million for the year reflecting substantial growth in premiums written by Class "A" members and an increase in the use of proportional reinsurance products. The line produced an underwriting loss of over $3.2 million.

Incurred claims increased to over $40 million including provisions for outstanding claims that reflect increasing premium volume, frequency, severity and the absence of positive developments in our reserves for outstanding claims for prior periods. Political influence on retail pricing and the need for product reform create an uncertain future for this product line. These factors influence expectations for future claims development and result in significant increases in provisions for outstanding claims for the future. In response, we have filed retail rate increases on behalf of our members who participate in the group filing process and we continue to represent the interests of our members writing automobile insurance to regulators on a provincial and national basis.

Throughout the year, we responded to the individual needs of our members and continued the development of our programs related to fuel oil spills and the underwriting of large property risks. We will continue to enhance these programs in the future and develop new initiatives that respond to the evolving needs of our members.

John A. Harper, President Emeritus

Following a distinguished four decade career in the insurance industry, John A. Harper will retire from the Farm Mutual Reinsurance Plan Inc. effective June 30th, 2004.

John's long affiliation with the Farm Mutual system began in 1975 when he joined a young and emerging FMRP as Assistant Treasurer. Within a year he moved to the Oxford Mutual Insurance Company as their new Manager and was subsequently elected to serve on the FMRP Board of Directors in 1977.

Over three decades, John has been a dominant figure in the development of the Canadian Farm Mutual Insurance industry. Following his service as a Director and past Chairman of the Board of FMRP, he returned to lead the organization holding numerous titles, culminating in his role as President and Chief Executive Officer. He has served as a Director of many related organizations including CAMIC, NAMICO, Canadian Institute for Climatic Studies and Vehicle Information Center of Canada.

John has been the recipient of the OMIA Presidential Merit Award and NAMIC Service Award and he has enhanced the reputation of the organization internationally. We offer our best wishes to John, Helen and family for a healthy, enjoyable and well deserved retirement.

Management Statement on Responsibility for Financial Reporting

The accompanying financial statements of Farm Mutual Reinsurance Plan Inc. are the responsibility of management and have been prepared in conformity with accounting principles generally accepted in Canada, and include some amounts based upon management's best estimates and judgments.

In meeting its responsibility for the reliability of financial information, management maintains and relies on a comprehensive system of internal control including organizational and procedural controls and internal accounting controls.

The Board of Directors is responsible for approving the financial statements. It establishes an Audit Committee, comprised of directors who are not employees of the Corporation who meet with management and external auditors, who have unrestricted access and the opportunity to have private meetings with the Audit Committee, to review the financial statements. The Audit Committee then submits its report to the Board of Directors prior to its approval of the financial statements.

The members' auditors, BDO Dunwoody LLP, conduct an independent audit of the financial statements and report to the members thereon.

The Financial Services Commission of Ontario makes an annual examination and inquiry into the affairs of the Corporation as deemed necessary to ensure that the Corporation is in sound financial condition and in compliance with the provisions of the Ontario Insurance Act.

G. S. Smith
President and C.E.O.

T. Smith
Vice-President and
Chief Financial Officer

Cambridge, Ontario
February 13, 2004

AUDITORS' REPORT

To the Members of Farm Mutual Reinsurance Plan Inc.

We have audited the balance sheet of Farm Mutual Reinsurance Plan Inc. as at December 31, 2003 and the statements of earnings, unappropriated surplus and cash flows for the year then ended. These financial statements are the responsibility of the Corporation'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 Corporation as at December 31, 2003 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Mississauga, Ontario
February 13, 2004

BDO Dunwoody LLP
Chartered Accountants

Farm Mutual Reinsurance Plan Inc.
Balance Sheet

As at December 31 (in thousands of dollars)

	2003	2002
Assets		(Note 17)
Cash	**$ 878**	$ 4,059
Receivables (Note 2)	**24,146**	18,175
Prepaids	**166**	122
Income taxes recoverable	**–**	4,830
Investments (Note 3)	**304,819**	253,014
Unpaid claims recoverable from reinsurers (Note 7)	**35,685**	33,905
Property and equipment (Note 4)	**5,127**	5,182
Future tax asset (Note 13)	**3,375**	–
Deferred acquisition expenditures	**6,983**	2,949
	$ 381,179	$ 322,236
Liabilities		
Payables and accruals (Note 5)	**$ 5,123**	$ 3,272
Income tax payable	**7,049**	–
Provision for unpaid claims (Note 7)	**217,035**	179,499
Unearned premiums	**21,095**	8,338
Future income tax liability (Note 13)	**–**	4,419
	250,302	195,528
Contingencies (Notes 1, 7, 8 and 9)		
Surplus and reserves		
Reserves required by the Financial Services Commission of Ontario (Note 10)	**–**	6,328
Unappropriated surplus	**130,877**	120,380
	130,877	126,708
	$ 381,179	$ 322,236

On behalf of the Board:

Serge Gauthier
Director

Michael O'Shea
Director

The accompanying summary of significant accounting policies and notes are an integral part of these financial statements.

Farm Mutual Reinsurance Plan Inc.
Statement of Unappropriated Surplus

For the year ended December 31 (in thousands of dollars)

	2003	2002
		(Note 17)
Unappropriated surplus, beginning of year (as previously reported)	**$ 120,380**	$ 118,504
Change in accounting policy (Note 17)	**–**	5,542
Unappropriated surplus, beginning of year	**120,380**	124,046
Change in reserves required by the Financial Services Commission of Ontario (Note 10)	**6,328**	385
Net earnings (loss) for the year	**4,169**	(4,051)
Unappropriated surplus, end of year	**$ 130,877**	$ 120,380

Statement of Earnings

For the year ended December 31 (in thousands of dollars)

	2003	2002
		(Note 17)
Net premiums earned (Note 8)		
Property	**$ 69,233**	$ 46,365
Liability	**11,189**	9,180
Automobile	**42,566**	29,199
	122,988	84,744
Net claims incurred (Note 8)		
Property	**55,615**	46,734
Liability	**9,523**	13,366
Automobile	**40,793**	10,143
	105,931	70,243
Underwriting gain before expenses	**17,057**	14,501
Expenses		
Commissions	**17,349**	8,270
Operating	**5,809**	5,156
	23,158	13,426
Net underwriting (loss) gain	**(6,101)**	1,075
Net investment income (loss)	**10,655**	(90)
Earnings before the following	**4,554**	985
Refund of premiums (Note 12)	**–**	6,800
Income (loss) before income taxes	**4,554**	(5,815)
Income taxes (Note 13)		
Current	**8,179**	(2,748)
Future	**(7,794)**	984
	385	(1,764)
Net income (loss) for the year	**$ 4,169**	$ (4,051)

The accompanying summary of significant accounting policies and notes are an integral part of these financial statements.

FARM MUTUAL REINSURANCE PLAN INC.
STATEMENT OF CASH FLOW

For the year ended December 31 (in thousands of dollars)

CASH PROVIDED FOR (USED IN):	2003	2002
		(Note 17)
OPERATING ACTIVITIES		
Net income (loss) for the year	**$ 4,169**	$ (4,051)
Adjustments required to reconcile net earnings to net cash provided by operating activities		
Amortization	**409**	442
Bond amortization	**1,138**	952
Future income taxes	**(7,794)**	984
Gain on sale of investments	**(482)**	(2,095)
Loss on sale of property and equipment	**34**	–
Write down of investments	**–**	11,900
Changes in non-cash working capital components (Note 14)	**52,194**	(3,669)
	49,668	4,463
INVESTING ACTIVITIES		
Proceeds on disposal of property and equipment	**20**	–
Purchase of property and equipment	**(408)**	(217)
Net purchase of investments (Note 14)	**(52,461)**	(10,160)
	(52,849)	(10,377)
NET DECREASE IN CASH	**(3,181)**	(5,914)
CASH, BEGINNING OF YEAR	**4,059**	9,973
CASH, END OF YEAR	**$ 878**	$ 4,059

SUPPLEMENTARY CASH FLOW INFORMATION		
Income tax (recovered) paid	**$ (3,721)**	$ 4,259

The accompanying summary of significant accounting policies and notes are an integral part of these financial statements.

Farm Mutual Reinsurance Plan Inc.
Summary of Significant Accounting Policies

December 31, 2003

Basis of Presentation

These financial statements have been prepared in accordance with accounting policies generally accepted in Canada. The preparation of financial statements requires management to make estimates and assumptions that affect reported assets and liabilities and disclosure of contingencies. These estimates also affect the reported amounts of income and expenses for the reporting period of the statement of earnings. Actual results could vary from these estimates.

Investments

Investments in bonds and debentures are carried at amortized cost less amounts written off for other than temporary declines in value. Premiums or discounts incurred on the purchase of bonds and debentures are amortized on a straight-line basis over the remaining life of the investment.

Investments in short-term securities and common shares are carried at cost less amounts written off for other than temporary declines in value. Real estate is carried at the lower of cost and estimated fair value.

Gains or losses on investments are included in investment income when realized and are calculated on the basis of average cost.

Property and Equipment

Property and equipment are recorded at cost less accumulated amortization and are amortized from the date of acquisition at the following annual rates:

Building	– 4% straight-line
Office furniture and equipment	– 20% declining balance
Computer hardware and software	– 20% straight-line
Automobiles	– 30% declining balance

Premiums Earned and Deferred Acquisition Expenditures

Premiums are included in income on a daily pro-rata basis over the term of the contracts. Acquisition costs related to unearned premiums, comprising commissions paid on proportional reinsurance, are deferred and amortized to income over the periods in which the premiums are earned. The method followed in determining the deferred acquisition expenditures limits the amount of the deferral to its realizable value by giving consideration to claims and expenses expected to be incurred as the premiums are earned.

Unpaid Claims

The provision for unpaid claims includes individual claim estimates for the full amount of all costs including the investigation and the projected final settlements for losses which occurred prior to the end of the year. In addition, a further provision is made in respect of incurred but not reported claims and development of losses on all outstanding claims. The initial estimate of unpaid claims is discounted for financial statement reporting purposes to give recognition to the time value of money. The interest rate used to discount the liabilities is based upon the rate of return of the Corporation's investment portfolio. The valuation incorporates assumptions made concerning future investment income and cash flows and a provision for adverse deviation. Estimates subject to uncertainty, are selected from a wide range of possible outcomes and are adjusted up or down as additional information becomes known. All changes in estimates are recorded as incurred claims in the current period.

Reinsurance Recoverable

Premiums earned and claims incurred are recorded net of amounts ceded to, and recoverable from, reinsurers. Amounts recoverable from reinsurers, which are estimated in a manner consistent with the associated claim liability, are recorded separately from the provision for unpaid claims.

Income Taxes

Income taxes are accounted for using the liability method. Future income taxes arise from temporary differences between the tax basis of the Corporation's assets and liabilities and their reported amounts in the financial statements. These assets and liabilities include investments and provision for unpaid claims.

Foreign Currency Translation

Foreign currency accounts are translated into Canadian dollars as follows:

At the transaction date, each asset, liability, premium, claim and expense is translated into Canadian dollars by the use of the exchange rate in effect at that date. At the year end date, monetary assets and liabilities are translated into Canadian dollars by using the exchange rate in effect at that date. The resulting foreign exchange gains and losses are included in income in the current period.

Farm Mutual Reinsurance Plan Inc.
Notes to Financial Statements

December 31, 2003 (in thousands of dollars)

1. Nature of Business

The Corporation is incorporated without share capital under the laws of the Province of Ontario. It provides reinsurance to member mutual insurance companies across Canada.

The Corporation is a reinsurer and therefore shares in risks originally accepted by its members. These risks are generally assumed by line of business at premiums established under the terms of agreements (treaties) with individual members. The premiums charged in aggregate, together with investment income attributable to unpaid claims, are expected to cover underwriting costs and claims, which may take a number of years to settle. The business risks of reinsurance reside in determining the premiums, settlement of claims, management of invested funds, and maintaining an appropriate net underwriting exposure.

The Corporation in turn purchases reinsurance to limit its exposure to loss. This reinsurance, however, does not relieve the Corporation of its obligation to members. If any reinsurers are unable to meet their obligations under the related agreements, the Corporation would be liable for unrecoverable amounts.

2. Receivables

	2003	2002
Accrued investment income	**$ 2,362**	$ 2,320
Ceding member companies	**19,842**	14,355
Reinsurers	**1,828**	1,423
Miscellaneous	**114**	77
	$ 24,146	$ 18,175

3. Investments

The book values and estimated fair values of investments as at December 31 were:

	2003		2002	
	Book Value	**Estimated Fair Value**	Book Value	Estimated Fair Value
Short-term securities	**$ 7,103**	**$ 7,103**	$ 8,515	$ 8,515
Bonds and debentures				
Government and guaranteed	**160,896**	**163,424**	119,378	123,202
Corporate	**64,036**	**67,309**	58,682	60,923
Common shares	**72,034**	**85,932**	65,689	59,084
Real estate	**750**	**750**	750	750
	$ 304,819	**$ 324,518**	$ 253,014	$ 252,474

The estimated fair values of common shares and bonds and debentures are based on quoted market values. The estimated fair market value of real estate is based on appraised value.

Included in investments are bonds totalling $8,317 (2002 - $Nil) and common shares totalling $12,096 (2002 - $Nil) which are part of a pooled fund. The pooled fund is administered by Farm Mutual Financial Services, a company which has members in common with the Corporation.

Virtually all investments are denominated in Canadian dollars. Details of significant terms and conditions, exposure to interest rate and credit risks on debt instruments are as follows:

It is the company's policy to diversify all investment portfolios. Diversification within each asset class is provided by limiting to 10% or less the percentage of the market value of fund assets invested in a single security not guaranteed by a Canadian federal or provincial government.

Short-term Securities

These are comprised of Canadian Treasury Bills with effective interest rates of 2.6%.

Bonds and Debentures

Maturity profile of the portfolio as at December 31, 2003

Within 1 Year	1-3 Years	3-5 Years	5-10 Years	Over 10 Years	Total
$ 4,692	$ 38,778	$ 37,106	$ 89,205	$ 55,151	$ 224,932
2%	17%	16%	40%	25%	100%

The effective interest rate at December 31, 2003 for bonds and debentures is 5.37% based on book value.

Investment grade bonds are those rated BBB and above. At December 31, 2003 virtually all of the company's bond portfolio is investment grade.

Impaired Assets

The corporation establishes specific writedowns on any investment which is impaired where that impairment is considered other than temporary. In determining the amount of the writedown, management considers the current market value of the security and the financial strength of the issuer or borrower. Changes to these provisions are reflected in net investment income in the period when the impairment is recognized. These provisions are netted against the carrying value of the specific investment.

Specific writedowns for common shares during the year amounted to $Nil (2002 - $11,900). Included in common shares are specific provisions totalling $8,534 (2002 - $11,900).

4. Property and Equipment

	Cost	Accumulated Amortization	2003 Net Book Value	2002 Net Book Value
Land	**$ 1,086**	**$ –**	**$ 1,086**	$ 1,086
Building	**4,987**	**1,684**	**3,303**	3,428
Office furniture and equipment	**1,104**	**749**	**355**	289
Computer				
– hardware	**624**	**331**	**293**	223
– software	**383**	**305**	**78**	117
Automobiles	**41**	**29**	**12**	39
	$ 8,225	**$ 3,098**	**$ 5,127**	$ 5,182

5. Payables and Accruals

	2003	2002
Expenses payable and accrued	**$ 384**	$ 451
Ceding member companies	**2,801**	1,268
Reinsurers	**1,938**	1,553
	$ 5,123	$ 3,272

6. Role of the Actuary and Auditors

The actuary is mandated by the members of the Corporation to review the Corporation's claims liabilities. The actuary's responsibility is to carry out an annual valuation of the Corporation's provision for unpaid claims in accordance with accepted actuarial practice and report thereon to the members. In performing the valuation, the actuary makes assumptions as to the future loss ratios, trends, future rates of claims frequency and severity, inflation and both internal and external adjustments expenses, taking into consideration the circumstances of the Corporation. The actuary also makes use of the work of the external auditor in his verification of the underlying data used in the valuation. The actuary's report outlines the scope of his work and opinion.

The external auditors have been appointed by the members of the Corporation to conduct an independent and objective audit of the financial statements of the Corporation in accordance with Canadian generally accepted auditing standards and report thereon to the members. In carrying out their audit, the auditors also make use of the work of the actuary and his report on the Corporation's provision for unpaid claims. The auditors' report outlines the scope of their audit and their opinion.

7. Provision for Unpaid Claims

The determination of the provision for unpaid claims and the related reinsurers' share requires the estimation of claims development and reinsurance recoveries. These estimates are subject to variability which could be material. The variability arises because all events affecting the ultimate settlement of claims have not taken place and may not take place for some time. Variability can be caused by receipt of additional claim information, changes in judicial interpretation, or significant changes in severity or frequency of claims from historical trends. The estimates are principally based on the Corporation's historical experience but incorporate expectations as to future developments arising out of actuarial studies, changes in the regulatory environment, inflationary trends and economic conditions. Methods of estimation have been used which the Corporation believes produce reasonable results given current information.

Catastrophes are an inherent risk of property and casualty insurance and may contribute to material year-to-year fluctuations in the Corporation's results of operations and financial condition when they occur. The level of catastrophe loss experienced in any one year cannot be predicted and could be material to results of operations and financial position.

The table below details the provision for unpaid claims by line of business:

	2003		2002	
	Gross	**Recoverable**	Gross	Recoverable
Property	**$ 43,289**	**$ 5,533**	$ 33,774	$ 3,285
Liability	**54,810**	**12,156**	55,321	13,483
Automobile	**118,936**	**17,996**	90,404	17,137
	$ 217,035	**$ 35,685**	$ 179,499	$ 33,905

The Corporation generally assumes risks from members on an excess of loss treaty basis. On the basis of historical experience, property claims are usually settled on a short-term basis, whereas claims on liability and automobile risks normally have a long settlement term.

Changes in the provision for unpaid claims recorded in the balance sheet and their impact on claims incurred reported in the statement of earnings are set out below:

	2003	2002
Provision for unpaid claims, beginning of year, net	**$ 145,594**	$ 138,403
Net Claims Activity		
Net decrease in estimated claims for losses that occurred in prior years	**(5,882)**	(16,518)
Net claims incurred on current year losses	**111,812**	86,760
Paid on claims incurred in		
– Current year	**(37,323)**	(27,708)
– Prior years	**(32,851)**	(35,343)
Provision for unpaid claims, end of year, net	**181,350**	145,594
Reinsurers' share	**35,685**	33,905
Provision for unpaid claims, gross	**$ 217,035**	$ 179,499

8. Reinsurance

The Corporation assumes risks from its members and cedes reinsurance to other insurers in order to limit the maximum loss through the spreading of risks. Reinsurance ceded does not relieve the corporation of liability as the originating reinsurer and accordingly it has a contingent liability for reinsurance recoverable should any of the assuming reinsurers be unable to meet their obligations.

The following table sets out the impact of ceded reinsurance on the statement of earnings:

	2003	2002
Net premiums earned		
Premiums assumed	**$ 139,633**	$ 100,979
Premiums ceded	**(16,645)**	(16,235)
	$ 122,988	$ 84,744
Net claims incurred		
Claims incurred	**$ 112,832**	$ 77,324
Reinsurance portion	**(6,901)**	(7,081)
	$ 105,931	$ 70,243

The Corporation reinsures assumed risks to limit its maximum loss to the following:

	In Excess of		**To a Maximum of**	
	2003	2002	**2003**	2002
Catastrophe – 95%	**$ 12,500**	$ 10,000	**$ 100,000**	$ 100,000
Excess reinsurance				
Property – 100%	**1,000**	750	**6,000**	1,750
Property – 95%	**–**	1,750	**–**	6,000
Liability – 90%	**1,500**	1,500	**3,000**	3,000
Liability – 100%	**3,000**	3,000	**18,000**	18,000
Automobile – 90%	**1,500**	1,500	**3,000**	3,000
Automobile – 100%	**3,000**	3,000	**18,000**	18,000

9. Contingencies

The Corporation has outstanding stand-by letters of credit at December 31, 2003 totalling $13,616 denominated in CND dollars. ($10,540, USD) These stand-by letters of credit are put in place to cover claims reserves as required.

The maximum available facility available to the Corporation is $40,000. The facility is secured by a general hypothecation of stocks and bonds.

10. Requirements Under the Ontario Insurance Act

Prior to 2003 the Act in its measurement of the Corporation's solvency position required the appropriation of members' surplus in respect of assets not admitted, investment valuation reserve and other statutory requirements. These appropriations were not considered part of surplus by the Financial Services Commission of Ontario.

As a result of changes to the Act, these reserves are not required for 2003 and subsequent years and have therefore been transferred to unappropriated surplus.

	2003	2002
Investment valuation reserve	**$ –**	$ 292
Non-admitted assets reserve	**–**	1,168
Unregistered reinsurers reserve	**–**	4,868
	$ –	$ 6,328

11. Pension Plan

The Corporation participates in a multiple employer pension plan through the Ontario Mutual Insurance Association. The plan is a contributory defined benefit pension plan which covers substantially all of its employees. The plan provides pension based on length of service and final average earnings.

The pension expense of $190 (2002 - $108) includes no charges for past service costs.

Based on the last actuarial valuation as at December 31, 2000, the Corporation's portion of the plan's position was as follows:

Assets	$ 1,646
Liabilities	$ 1,564

12. Refund of Premiums

Refunds of premiums are determined by the Board and are refundable to Class A members on a pro-rata basis based on premiums written over the last five years. The Board did not authorize the payment of any refund of premiums during the year.

13. Income Taxes

The provision for income taxes reflects an effective tax rate which differs from the corporate tax rate for the following reasons:

	2003	2002
Income taxes based on combined basic Canadian federal and provincial tax rate of 37% (2002 – 39%)	**$ 1,686**	$ (2,268)
Increase (decrease) resulting from permanent differences		
Non-taxable dividend income	**(405)**	(362)
Exempt income from insuring farm risks	**(324)**	591
Increase (decrease) resulting from change in future tax rate	**(622)**	–
Large Corporations Tax	**50**	275
Total taxes – current and future	**$ 385**	$ (1,764)

Future income tax assets (liabilities) are comprised of the following:

	2003	2002
Provision for unpaid claims	**$ 2,303**	$ (410)
Invested assets	**1,072**	(4,009)
	$ 3,375	$ (4,419)

14. Statement of Cash Flows

Changes in non-cash working capital

	2003	2002
Receivables	**$ (5,971)**	$ (3,340)
Prepaids	**(44)**	(83)
Deferred acquisition costs	**(4,034)**	(264)
Payables and accruals	**1,851**	(764)
Income taxes	**11,879**	563
Provision for unpaid claims, net of recoveries	**35,756**	(400)
Unearned premiums	**12,757**	619
	$ 52,194	$ (3,669)

Investing activities

The investing activities included in the statement of cash flow are comprised of the following:

2003	**Purchases**	**Sales**	**Net**	2002	Purchases	Sales	Net
Bonds	**$ 333,835**	**$ 291,437**	**$ (42,398)**	Bonds	$ 191,540	$ 185,382	$ (6,158)
Short-term	**239,425**	**241,718**	**2,293**	Short-term	78,114	75,917	(2,197)
Common shares	**27,649**	**15,293**	**(12,356)**	Common shares	21,253	19,448	(1,805)
			$ (52,461)				$ (10,160)

15. Facility Association

The Facility Association is comprised of various risk sharing pools where most companies in the auto insurance industry share resources to provide insurance for high risks.

The Corporation is not a direct writer of automobile insurance policies and as a result does not participate directly in the Facility Association.

The Corporation acts as an administrator on behalf of its members participating in the Facility Association.

16. Fair Value of Financial Instruments

The estimated fair value of investments is set out in Note 3.

The fair values of cash, receivables and payables and accruals approximate their carrying values because of the short maturity of these instruments.

Unpaid claims and reinsurance recoverables are recorded at their discounted present value which approximates fair value.

Included in the balance sheet are the following amounts denominated in foreign currencies:

	Currency	**2003**	2002
Cash	U.S. dollars	**$ 206**	$ 56
Accounts receivable	U.S. dollars	**2,822**	1,318
Provision for unpaid claims	U.S. dollars	**6,173**	4,142

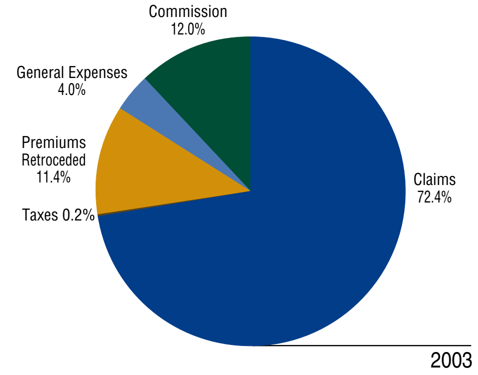
17. Change in Accounting Policy

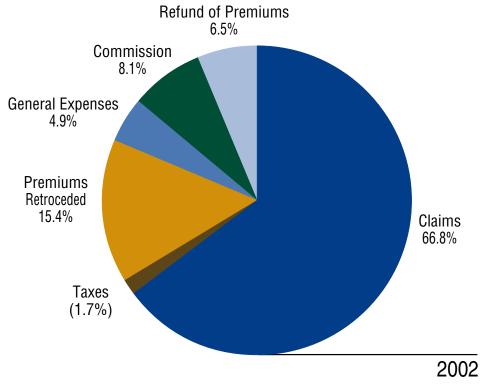
Effective January 1, 2003, the company changed the method of calculating the provision for unpaid claims from an undiscounted basis to a discounted basis. This change in accounting policy has been applied on a retroactive basis.

The following table outlines the impact of this change on the financial statements:

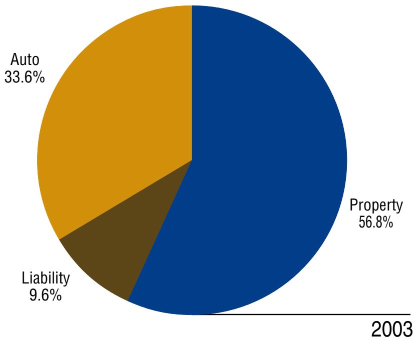
	2003	2002
Reduction in provision for unpaid claims	**$ 15,614**	$ 11,605
Reduction in unpaid claims recoverable from reinsurers	**5,454**	3,934
Increase in future taxes payable	**622**	2,071
Increase in opening unappropriated surplus (net of $2,050 future taxes)	**–**	5,542
Reduction in claims incurred	**2,489**	79
Increase in provision for income taxes	**622**	21
Increase in net income for the year	**1,867**	58

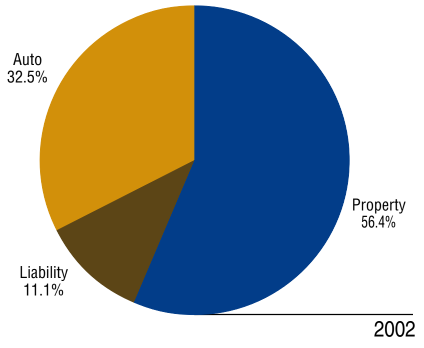
Distribution of expenses



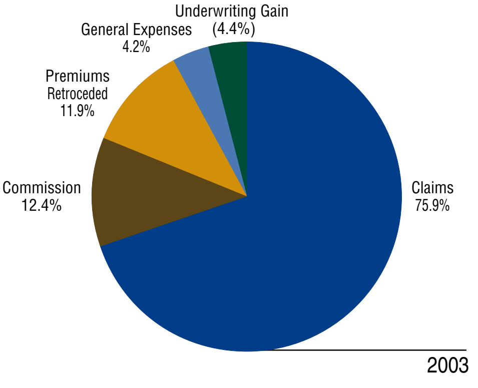


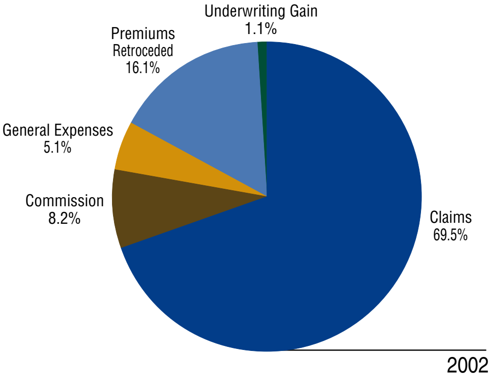
Sources of Gross Premium Income





Distribution of Gross Premium Dollar





Past Presidents and Chairmen of the Board

President	*from*	*to*
Fred M. Fletcher	1959	1965
J. Stan Mitchell	1965	1973
Delmar Cobban	1973	1975
Willard Shaw	1975	1977
K. Max Forsythe	1977	1979
William Weir	1979	1981
Emory Knill	1981	1983
John Harper	1983	1985
Fred Legg	1985	1987
Albert McArthur	1987	1989
Donald Mylrea	1989	1991
Gordon Johnson	1991	1992
Vern Inglis	1992	1993
Edward Pellow	1993	1994
Brian Fisher	1994	1995

Chairmen	*from*	*to*
James Pinnock	1995	1996
Carl Turnbull	1996	1997
Ronald Perry	1997	1998
Douglas Winer	1998	1999
Gerald Brown	1999	2000
John McIntosh	2000	2001
Terry Malcolm	2001	2002
Philip Brett	2002	2003
Earl Harder	2003	Present

Staff

General Manager	*from*	*to*
H.H. McFadden	1959	1973
Bruce Bird	1974	1979
Gerald M. Snyder	1980	1986
John A. Harper	1987	1995

President		
John A. Harper	1995	2003
Steve Smith	2003	Present
John A. Harper (President Emeritus)	2003	Present