Broker-centric

insurance solutions

2017 Annual Report

Echelon Financial
Holdings Inc.

echelon
Insurance

Letter to Shareholders

Establishing a foundation for sustainable growth and future profitability

While our financial results were not as good as we had expected for 2017, we made ample progress in moving our organization in the right direction during the year.

I would like to thank our fellow shareholders for your continued support during the continued evolution of our company. We have laid significant groundwork, and I am confident that we will begin to see profitability in 2018 and beyond.

During the year, we began to transform key areas of our organization, adding experienced new team members to our Actuarial, Information Technology, Underwriting, and Claims departments.

Under new leadership, we grew and strengthened our actuarial team, moving away from the outsourcing of this core function. Moving into 2018, we have the skills and expertise to implement new actuarial practices such as predictive modelling, which will help to ensure the ongoing profitability of our products.

On the technology front, we accelerated the migration of our various insurance products to our new Passport system. We are pleased to report that at year-end, 14 of our 17 products were being processed on Passport. Passport has been built to manage all facets of a policy's lifecycle, from pricing and underwriting, to billing and claims. It also supports improved connectivity and simplified processes for our brokers, from whom we've received positive feedback on our Passport system and broker portal.

In underwriting, we expanded our teams to better support both our brokers and customers, and the increase in business that we continue to see.

Echelon's growth continued in 2017, supported by our strong broker partnerships, and in-demand products.

Alongside top line growth of 31%, we narrowed our personal commercial lines split, moving from 71% Personal Lines and 29% Commercial Lines in 2016, to a more balanced 66% Personal Lines and 34% Commercial Lines at the close of 2017. A more balanced book will bring greater stability to our results, and, will support more consistent profitability for both Echelon and our brokers through a better spread of risk and lower dependence on regulated rates.

As noted last year, Canadian brokers continue to express a dire need for a broker-committed insurer partner, with larger insurers delving into a direct business model. With our expanded product offering, improved technology, and underwriting and actuarial expertise, Echelon is emerging as a viable alternative for brokers across the country. We are focused on forming strong partnerships with a smaller, more dedicated group of brokers, and are growing profitable books of business with mutually committed brokers.

I would also like to take this opportunity to thank our employees for their dedication and hard work, and our Board of Directors for their ongoing advice and support of our new strategy. We are excited for what the future holds for Echelon.

Serge Lavoie
President & CEO
Echelon Insurance

Chairman's Report

The year 2017 marked a watershed in the history and development of Echelon Insurance. The disposition of our European operations in 2017 removed any continuing underwriting risk from that sector of the business, and the successful realization of the loan to the purchaser closes that era of the company's history.

With the way clear for a focus on Canadian operations, your management team is working to implement our strategy of building a successful and profitable insurance enterprise in selected niche markets across Canada. The recruitment of key insurance professionals in underwriting, claims, information technology and actuarial capabilities has positioned the company with the ability to grow and prosper in selected lines of insurance over time.

Last May, your Board was strengthened by the addition of key insurance professionals Jim Falle, Gary Quon and David Thomson. These directors were joined in January 2018 by seasoned investment executive Lee Matheson, who filled the remaining Board vacancy.

Building and maintaining a profitable and growing property and casualty insurance enterprise is challenging, and a quest that takes time to develop. Results in any one quarter can be cyclical, and reorienting an enterprise in this business requires skill and patience. Your Board is fully supportive of the strategy and the capability of CEO Serge Lavoie and his leadership team. We look forward to continuing to work with them as we make progress toward our goals.

Murray Wallace
Chairman of the Board

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

For the period ending December 31, 2017

Echelon Financial Holdings Inc. ("EFH" or "the Company") prepares its financial statements in accordance with International Financial Reporting Standards (IFRS), issued and effective as of December 31, 2017, as set out in the Handbook of the Chartered Professional Accountants (CPA Handbook).

The financial data for 2017, 2016 and 2015 in this discussion has been prepared in accordance with IFRS.

References to "EFH" or "the Company" in this Management's Discussion and Analysis of Financial Condition and Results of Operations refer to Echelon Financial Holdings Inc. on a consolidated basis, both now and in its predecessor forms.

The following discussion should be read in conjunction with EFH's audited consolidated financial statements and the related notes. The following commentary is current as of February 15, 2018. Additional information relating to EFH is available on SEDAR at www.sedar.com. Certain totals, subtotals and percentages may not reconcile due to rounding.

The Company uses both IFRS and certain non-IFRS measures to assess performance. Securities regulators require that companies caution readers about non-IFRS measures that do not have a standardized meaning under IFRS and are unlikely to be comparable to similar measures used by other companies. EFH analyzes performance based on underwriting income and underwriting ratios such as combined, expense and loss ratios, which are non-IFRS measures. Net operating income is defined as underwriting income plus interest and dividend income, net of tax. Underwriting income is defined as net earned premiums less net claims incurred, net acquisition expenses, general expenses and reversing any impact of change in discount rate and foreign exchange on claims and excludes impact of change in claims discount rates, foreign exchange on unpaid claims and investments, and non-recurring items. Net investment income consists of interest income, dividend income and premium financing charges, less interest expense, as per note 6 of the Company's Financial Statements. Net operating income is adjusted to that attributable to shareholders for per share calculation.

The following discussion contains forward-looking information that involves risk and uncertainties based on current expectations. This information includes, but is not limited to, statements about the operations, business, financial condition, priorities, targets, ongoing objectives, strategies and outlook for the Company in 2017 and subsequent periods.

This information is based upon certain material factors or assumptions that were applied in drawing a conclusion or making a projection as reflected in the forward-looking information. By its nature, this information is subject to inherent risks and uncertainties that may be general or specific. A variety of material factors, many of which are beyond EFH's control, affect the operations, performance and results of the Company and its business and could cause actual results to differ materially from the expectations expressed in any of this forward-looking information (see "Risk Factors").

Forward-looking information is provided for the purpose of providing information about management's current expectations and plans relating to the future. Readers are cautioned that such information may not be appropriate for other purposes. Additional information about the risks and uncertainties about EFH's business is provided in its disclosure materials, including its annual information form, filed with the securities regulatory authorities in Canada, available at www.sedar.com. EFH does not expect to update any forward-looking information.

COMPANY OVERVIEW

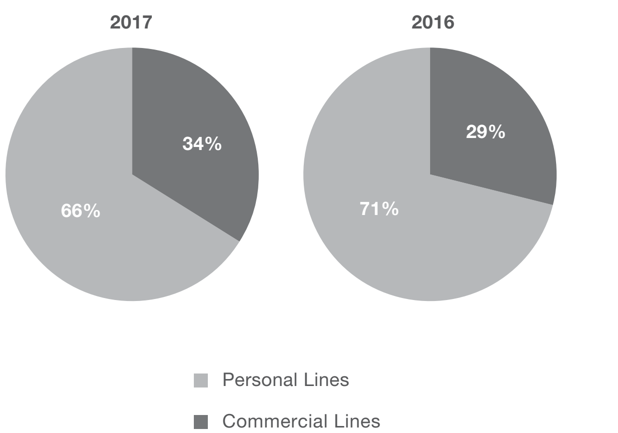
EFH operates in the property and casualty ("P&C") insurance industry in Canada through Echelon Insurance ("Echelon"), a federally regulated P&C insurance company and The Insurance Company of Prince Edward Island ("ICPEI"), a provincially regulated P&C insurance company. The Company underwrites automobile insurance and other specialty insurance products, with a focus on niche under served markets. It has two lines of insurance business – Personal Lines and Commercial Lines. Personal Lines focuses on the underwriting of non-standard automobile insurance and insurance for motorcycles, antique and classic vehicles, trailers, motor homes, recreational vehicles and personal property. Commercial Lines designs and underwrites Commercial Property, Commercial Automobile, Surety, Liability, and Specialty Programs.

On March 7, 2017, the Company completed the sale of its European operations. The European operation results are referred to as discontinued operations in this document.

EFH intends to grow its business profitably across Canada by offering a complete and diverse suite of products to its brokers, with an ability to transact efficiently through modern systems. EFH currently intends to use any excess capital in addition to capital generated from its operations to fund its growth.

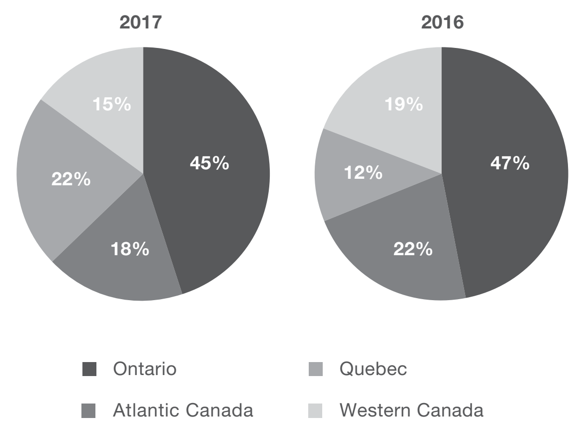
The breakdown of direct written premiums by category of business is shown below for 2017 and 2016:

DIRECT WRITTEN PREMIUMS BY LINE OF BUSINESS



The breakdown of direct written premiums by region is shown below for 2017 and 2016:

DIRECT WRITTEN PREMIUMS BY REGION



On a Consolidated basis, 66% of EFH's direct written premiums in 2017 were attributable to premiums from Personal Lines policies while Commercial Lines accounted for 34%.

FOURTH QUARTER HIGHLIGHTS

Net operating loss on continued operations of $0.51 per share compared to income of $0.40 per share in the fourth quarter of 2016.

A combined operating ratio of 115% compared to 90% in the fourth quarter of 2016, primarily due to increased severity of claims compared to the prior year quarter, especially in Atlantic Auto.

A 38% increase in direct written premiums over the same period in 2016 to $68.1 million as a result of organic growth in Personal Lines and growth in new Commercial Lines products launched in 2016.

A pre-tax gain on invested assets of $3.6 million in the quarter compared to a pre-tax loss of $0.6 million in the prior year quarter, attributable to positive returns on the fixed income portfolio driven by spread compression in provincial and corporate bonds, in addition to strong returns in the preferred share and equity portfolios.

Closing book value per share of $12.01, a decrease of 1% over the third quarter of 2017.

The following financial information compares three months ended December 31, 2017 results with the same period in 2016.

	3 months ended December 31		Change	
($ THOUSANDS, EXCEPT PER SHARE AMOUNTS)	**2017**	2016	$	%
Direct written and assumed premiums	**68,050**	49,403	18,647	38
Net written premiums	**65,235**	44,476	20,759	47
Net earned premiums	**64,906**	46,013	18,893	41
Net claims incurred	**52,825**	25,654	27,171	106
Net acquisition costs	**15,173**	10,680	4,493	42
Operating expenses	**8,116**	7,124	992	14
Underwriting (loss) income	**(11,208)**	2,555	(13,763)	(539)
Severance expense	**(87)**	(769)	682	89
Investment income	**3,316**	3,159	157	5
Impact of discount rate on claims	**1,220**	(1,370)	2,590	(189)
Net (loss) income before interest and income taxes	**(6,759)**	3,575	(10,334)	(289)
Interest expense	**—**	63	(63)	(100)
Income tax (recovery) expense	**(1,933)**	911	(2,844)	312
Net (loss) income	**(4,826)**	2,601	(7,427)	(286)
Net (loss) income attributable to shareholders	**(4,966)**	2,598	(7,564)	(291)
Net operating (loss) income attributable to shareholders	**(6,252)**	4,857	(11,109)	(229)
(Loss) Earnings per share				
Basic	**($0.42)**	$0.22	$(0.64)	(291)
Diluted	**($0.42)**	$0.22	$(0.64)	(291)
Net operating (loss) income per share – diluted (1)	**($0.51)**	$0.40	$(0.91)	(228)
Trailing twelve-month return on equity (ROE) – continuing operations (2)	**4.6%**	4.2%		

(1) Net operating income is defined as underwriting income plus interest and dividend income, net of tax. Underwriting income excludes impact of change in claims discount rates, and non-recurring items. Net investment income consists of interest income, dividend income and premium financing charges, less interest expense, as per note 6 of the Company's Consolidated Financial Statements. Net operating income is adjusted to that attributable to shareholders for per share calculation.

(2) ROE calculated on rolling twelve-month basis

INSURANCE OPERATIONS

Direct Written, Net Written and Net Earned Premiums

In the fourth quarter of 2017, direct written premiums increased by 38% while net earned premiums increased by 41% compared to the same period prior year. The increase in premium was driven by organic growth in Personal Lines and new Commercial Lines products launched in 2016.

Claims Incurred

For the quarter ended December 31, 2017, net claims expense increased by 106%, primarily due to increased severity of Personal Auto claims in the Atlantic provinces.

Net favourable development of prior year claims of $2.3 million was recorded in the fourth quarter of 2017 compared to net favourable development of $3.4 million in the same period in 2016. The favourable development primarily arose from the Commercial Lines segment and $1.2 million of the development related to a change in discount rate.

Acquisition Costs

Acquisition costs, which consist mainly of commissions, premium taxes and a portion of general expenses related to policy acquisitions, increased by 42%, in the quarter ended December 31, 2017, in line with the increase in net earned premiums.

Operating Expenses

Operating expenses increased by $1.0 million or 14%, to $8.1 million in the fourth quarter of 2017 compared to $7.1 million in the comparative quarter, driven by increased information technology and compensation expenses.

Underwriting Income

Underwriting loss of $11.2 million was recorded in the fourth quarter of 2017 compared to an underwriting income of $2.6 million in the same period in 2016 due to weak Personal Lines results in the quarter.

Investment Income

Investment income was $3.3 million comparable to $3.2 million in the fourth quarter of 2016.

Net Income before Income Taxes

For the quarter ended December 31, 2017, net loss before taxes was $6.8 million compared to income of $3.6 million in the fourth quarter of 2016 primarily due to a decrease in underwriting income.

Income Taxes

For the quarter ended December 31, 2017, the provision for income taxes reflects a recovery of $1.9 million compared to an expense of $0.9 million for the same period last year.

SEGMENTED FINANCIAL INFORMATION (CONTINUED OPERATIONS)

The segmented results below exclude corporate expenses.

TOTAL OPERATIONS

	Three months ended December 31				Twelve months ended December 31			
($THOUSANDS)	**2017**	2016	$ Change	% Change	**2017**	2016	$ Change	% Change
Direct written premiums	**68,050**	49,403	18,647	38	**285,718**	217,486	68,232	31
Net earned premiums	**64,906**	46,013	18,893	41	**227,396**	181,060	46,336	26
Net claims:								
Current year claims	**55,106**	29,096	26,010	89	**182,559**	128,015	54,544	43
Current year loss ratio	**84.9%**	63.2%			**80.3%**	70.7%		
Favourable prior year claims development	**2,281**	3,442	(1,161)	(34)	**25,745**	17,243	8,502	49
Total net claims	**52,825**	25,654	27,171	106	**156,814**	110,772	46,042	42
Loss ratio	**81.4%**	55.8%			**69.0%**	61.2%		
Expense ratio	**33.8%**	34.5%			**33.3%**	35.0%		
Combined ratio	**115.2%**	90.3%			**102.3%**	96.2%		
Underwriting income (loss)	**(9,844)**	4,326	(14,170)	(328)	**(5,183)**	6,814	(11,997)	(176)

PERSONAL LINES

	Three months ended December 31				Twelve months ended December 31			
($THOUSANDS)	**2017**	2016	$ Change	% Change	**2017**	2016	$ Change	% Change
Direct written premiums	**42,638**	31,171	11,467	37	**189,454**	154,992	34,462	22
Net earned premiums	**45,865**	35,285	10,580	30	**165,893**	139,616	26,277	19
Net claims:								
Current year claims	**43,527**	26,059	17,468	67	**144,467**	106,017	38,450	36
Current year loss ratio	**94.9%**	73.9%			**87.1%**	76.0%		
(Unfavourable) favourable prior year claims development	**(175)**	(1,560)	1,385	89	**19,582**	8,194	11,388	139
Total net claims	**43,702**	27,619	16,083	58	**124,885**	97,823	27,062	28
Loss ratio	**95.3%**	78.3%			**75.3%**	70.1%		
Expense ratio	**31.5%**	31.8%			**30.2%**	32.2%		
Combined ratio	**126.8%**	110.1%			**105.5%**	102.3%		
Underwriting income (loss)	**(12,265)**	(3,530)	(8,735)	247	**(9,186)**	(3,177)	(6,009)	(189)

Fourth quarter 2017

Personal Lines recorded an underwriting loss of $12.3 million compared to an underwriting loss of $3.5 million in the same period last year. Direct written premiums increased by 37% in the quarter due to organic growth in Personal Auto in Ontario and Quebec.

This segment's combined ratio increased to 127% in the quarter as a result of the following factors:

1. Increased severity of claims in Atlantic Auto, in addition to increased frequency in Ontario Auto.
2. Weak results in Ontario recreational vehicles.
3. This was partially offset by reduced adverse development compared to the prior quarter.

Year-to-date 2017

Personal Lines reported an underwriting loss of $9.2 million compared to an underwriting loss of $3.2 million in the same period last year. Direct written premiums increased by 22% for the year, primarily due to organic growth in Personal Auto across Canada, but especially in Ontario and Quebec.

This segment's combined ratio increased to 106% for the year as a result of the following factors:

1. Increased severity of claims in Atlantic Auto and Ontario motorcycle compared to prior year.
2. $2.0 million impact from BC wildfire losses on Personal Property.
3. These factors were partially offset by improved results in Ontario Auto.

COMMERCIAL LINES

($THOUSANDS)	Three months ended December 31 2017	2016	$ Change	% Change	Twelve months ended December 31 2017	2016	$ Change	% Change
Direct written premiums	**25,412**	18,232	7,180	39	**96,264**	62,494	33,770	54
Net earned premiums	**19,041**	10,728	8,313	77	**61,503**	41,444	20,059	48
Net claims:								
Current year claims	**11,579**	3,037	8,542	281	**38,092**	21,998	16,094	73
Current year loss ratio	**60.8%**	28.3%			**61.9%**	53.1%		
Favourable prior year claims development	**2,456**	5,002	(2,546)	(51)	**6,163**	9,049	(2,886)	(32)
Total net claims	**9,123**	(1,965)	11,088	564	**31,929**	12,949	18,980	147
Loss ratio	**47.9%**	(18.3)%			**51.9%**	31.2%		
Expense ratio	**39.4%**	45.2%			**41.6%**	44.7%		
Combined ratio	**87.3%**	26.9%			**93.5%**	75.9%		
Underwriting income (loss)	**2,421**	7,856	(5,435)	(69)	**4,003**	9,991	(5,988)	(60)

Fourth quarter 2017

Commercial Lines recorded an underwriting income of $2.4 million compared to $7.9 million in the same period last year. Direct written premiums increased by 39% in the quarter primarily due to the launch of Commercial Auto and Surety in 2016.

This segment's combined ratio increased to 87% in the quarter from an exceptional 27% in prior year quarter as a result of the following factors:

1. Higher frequency of losses on the warranty book compared to the same period last year.
2. Improved expense ratio due to start-up costs incurred in the prior year quarter primarily on the launch of new products.
3. Reduced redundancies on prior year claims of $2.5 million compared to $5.0 million in the same period last year.

Year-to-date 2017

Commercial Lines recorded an underwriting income of $4.0 million compared to $10.0 million in the same period last year. Direct written premiums increased by 54% for the year, primarily due to the launch of Commercial Auto and Surety in 2016.

This segment's combined ratio increased to 94% for the year from an exceptional level of 76% in the prior year as a result of the following factors:

1. Weaker results in Commercial Auto due to increased severity of claims.
2. Higher frequency of losses on the warranty book compared to the same period last year.
3. Reduced redundancies on prior year claims of $6.2 million compared to $9.0 million in the same period last year.

DISCONTINUED OPERATIONS

On August 4, 2016, Echelon entered into a definitive stock purchase agreement to sell its European insurance subsidiary, subject to regulatory approval. On February 28, 2017, regulatory approval was received from the Danish Financial Supervisory Authority, which completed the necessary approvals required for the sale. The Company completed the sale on March 7, 2017 and has retained no residual insurance risk or other financial risk other than credit risk associated with the loan receivable from the sale. The Company has received an aggregate of $16.7 million to date on closing and from the partial repayment of the loan, and is scheduled to receive an additional $6.6 million prior to March 31, 2018, which it has recognized as a loan receivable on its balance sheet. Interest payments on the loan are current.

SUMMARY OF QUARTERLY RESULTS

A summary of the Company's last eight quarters (after all corporate expenses) is as follows:

	2017				2016			
($ THOUSANDS, EXCEPT PER SHARE AMOUNTS)	**Q4**	**Q3**	**Q2**	**Q1**	Q4	Q3	Q2	Q1
Direct written and assumed premiums	**68,050**	**78,047**	**85,035**	**54,586**	49,403	58,171	67,791	42,121
Net earned premiums and other revenue	**64,906**	**60,017**	**53,448**	**49,025**	46,013	46,452	45,247	43,348
Underwriting income (loss)	**(11,208)**	**(3,428)**	**1,477**	**716**	2,555	(429)	(485)	(2,055)
Income before interest expense and income taxes	**(6,759)**	**936**	**4,365**	**9,203**	3,575	1,622	3,402	406
Net income	**(4,826)**	**810**	**3,193**	**7,466**	2,602	1,402	2,214	901
Net operating income	**(6,252)**	**1,211**	**3,338**	**2,316**	4,857	1,580	2,892	1,025
Earnings (loss) per adjusted share								
(a) Basic	**($0.42)**	**$0.07**	**$0.27**	**$0.63**	$0.22	$0.10	$0.15	$0.08
(b) Diluted	**($0.42)**	**$0.07**	**$0.26**	**$0.62**	$0.22	$0.10	$0.15	$0.08
Net operating income per share – diluted	**($0.51)**	**$0.10**	**$0.28**	**$0.19**	$0.40	$0.13	$0.24	$0.09
Selected financial ratios								
Loss ratio	**81.4%**	**72.2%**	**59.5%**	**58.9%**	55.8%	61.5%	62.4%	65.3%
Expense ratio	**35.8%**	**33.5%**	**37.7%**	**39.6%**	38.6%	39.4%	38.7%	39.4%
Combined ratio	**117.2%**	**105.7%**	**97.2%**	**98.5%**	94.4%	100.9%	101.1%	104.7%
Book value per share	**$12.01**	**$12.14**	**$12.25**	**$12.10**	$11.70	$12.90	$13.08	$15.16

The quarterly results reflect the seasonality of the Company's business. While net earned premiums are relatively stable from quarter to quarter, underwriting results may vary significantly by quarter as they are affected by seasonality, as described in note 5 of the financial statements.

NET OPERATING INCOME

($ THOUSANDS, EXCEPT PER SHARE AMOUNTS)	**Q4 2017**	**2017**	2016	2015	2014	2013
Net investment income	**2,821**	**10,416**	11,502	14,050	13,650	13,349
Underwriting income (loss)	**(11,208)**	**(12,443)**	(414)	(447)	8,106	(2,980)
Add: CAT losses	**—**	**2,604**	3,334	—	—	—
Pre-tax operating income	**(8,387)**	**577**	14,422	13,603	21,756	10,369
Income tax	**2,275**	**190**	(3,556)	(3,673)	(5,874)	(2,800)
Net operating income	**(6,112)**	**767**	10,866	9,930	15,882	7,569
Minority interest	**(140)**	**(154)**	(512)	(8)	(129)	—
Net operating income attributable to shareholders	**(6,252)**	**613**	10,354	9,922	15,753	7,569
Net operating income per share – diluted	**$(0.51)**	**$0.05**	$0.86	$0.83	$1.31	$0.63

2017 FINANCIAL OVERVIEW

REVENUE

Revenue reflected in the consolidated financial statements includes net earned premiums, investment income, realized gains and losses on the sale of investments, and other revenue.

($ THOUSANDS)	**Q4 2017**	**2017**	2016
Gross premiums written	**68,050**	**285,718**	217,486
Net premiums written	**65,235**	**266,807**	199,601
Net earned premiums	**64,906**	**227,396**	181,060
Net interest and dividends	**2,821**	**10,416**	11,502
Realized and unrealized gains on investments	**483**	**2,151**	4,150
Foreign exchange gains	**12**	**4,629**	855
Total revenue	**68,222**	**244,592**	197,567

The Company's main source of revenue was earned premiums from the sale of insurance policies. Gross written premiums totaled $285.7 million, an increase of 31% compared to $217.5 million last year. The increase in gross premiums was primarily due to organic growth in Personal Auto and increased volumes from the newly launched products in 2016.

Personal Lines recorded $189.5 million of premiums in 2017 compared to $155.0 million in 2016, an increase of 22%. Commercial Lines recorded $96.3 million of premiums in 2017 compared to $62.5 million in 2016, an increase of 54%.

Net earned premiums increased $46.3 million, or 26% in 2017, to $227.4 million from $181.1 million in 2016.

Investment income constituted approximately 7% of EFH's total revenue in 2017. Market fluctuations in interest rates and equity markets affect EFH's returns on the market value of fixed income, preferred shares, equity markets and short-term investments. Net realized and unrealized gains including foreign exchange gains on invested assets totaled $6.8 million compared to net realized and unrealized gain of $5.0 million last year.

EXPENSES

EFH's expenses consist of incurred claims, acquisition costs and operating expenses.

($ THOUSANDS)	**Q4 2017**	**2017**	2016
Incurred claims[(1)]	**52,825**	**156,814**	110,772
Acquisition expense	**15,173**	**51,994**	41,545
Operating expense[(2)]	**8,116**	**31,031**	29,157
	76,114	**239,839**	181,474

Selected Underwriting Ratios	**Q4 2017**	**2017**	2016
Incurred claims ratio[(1)]	**81.4%**	**69.0%**	61.2%
Acquisition expense ratio	**23.4%**	**22.9%**	22.9%
Operating expense ratio	**12.4%**	**13.6%**	16.1%
Combined ratio[(1)]	**117.2%**	**105.5%**	100.2%

(1) Before impact of change in discount rate decreasing unpaid claims by $3.3 million in 2017 and increasing unpaid claims by $2.8 million in 2016.

(2) Operating expenses do not include severance costs of $0.3 million in 2017, $4.3 million in 2016.

Incurred claims, also referred to as losses, are the amounts payable under insurance policies relating to insured events. Loss adjustment expenses, also referred to as claims expenses, are the expenses of settling claims, including allocated (i.e. external) loss adjustment expenses and unallocated (i.e. internal) loss adjustment expenses (together, LAE). Achieving profitable results depends on EFH's ability to manage future claims and other costs through innovative product design, strict underwriting criteria and efficient claims management.

Acquisition costs consist mainly of commissions and premium taxes which are directly related to the acquisition of premiums. Commissions are the amounts paid to producers for selling insurance policies. The amount of commission is generally a percentage of the premium of the insurance policy sold or renewed. Contingent commissions are paid to brokers and Managing General Agents (MGAs) on an annual basis if they meet certain targets. In general, these producers have to meet or exceed certain criteria, including written premium targets and profitability to qualify for this compensation. Premium taxes are paid by EFH to provincial governments, calculated as a percentage of direct written premiums.

Operating expenses are the non-commission selling, underwriting and administrative expenses incurred to support EFH's business. A significant portion of these expenses is related to employee compensation and benefits. The effective control and management of these expenses can enhance the underwriting results from the operation.

YEAR ENDED DECEMBER 31, 2017 COMPARED TO 2016

2017 HIGHLIGHTS

- Net operating income decreased by 94% to $0.05 per share from $0.86 per share.
- A combined operating ratio of 102% compared to 96% due to increased severity in Atlantic Auto and Motorcycle in addition to higher technology expenses in 2017. This was partially offset by stronger results in Ontario Auto.
- A 31% increase in direct written premium in 2017, primarily due to growth in Commercial Lines products launched in 2016 and organic growth in Personal Lines.
- Total pre-tax return of invested assets of $7.8 million comparable to $7.5 million in 2016 due to stronger preferred share and equity returns in 2017.

The following financial information compares results for the full year 2017 and 2016.

($ THOUSANDS, EXCEPT PER SHARE AMOUNTS)	**2017**	2016	$ Change	% Change
Direct written and assumed premiums	**285,718**	217,486	68,232	31
Net written premiums	**266,807**	199,601	67,206	34
Net earned premiums	**227,396**	181,060	46,336	26
Net claims incurred	**156,814**	110,772	46,042	42
Net acquisition costs	**51,994**	41,545	10,449	25
Operating expenses	**31,031**	29,156	1,875	6
Underwriting (loss)	**(12,443)**	(414)	(12,029)	(2,906)
Severance expense	**(262)**	(4,266)	4,004	94
Investment income	**17,196**	16,507	689	4
Impact of discount rate	**3,254**	(2,822)	6,076	215
Net income before interest expense and income taxes	**7,745**	9,005	(1,260)	(14)
Interest expense	**155**	217	(62)	(29)
Income taxes expense	**947**	1,670	(723)	(43)
Net income	**6,643**	7,118	(475)	(7)
Net income attributable to shareholders	**6,489**	6,606	(117)	(2)
Net operating income attributable to shareholders	**613**	10,354	(9,741)	(94)
Earnings per share				
Basic	**$0.55**	$0.56	$(0.01)	(2)
Diluted	**$0.54**	$0.55	$(0.01)	(2)
Net operating income per share – diluted (1)	**$0.05**	$0.86	$(0.81)	(94)
Trailing twelve-month return on equity (ROE) – continuing operations (2)	**4.6%**	4.2%		

(1) Net operating income is defined as underwriting income plus interest and dividend income, net of tax. Underwriting income excludes impact of change in claims discount rates, and non-recurring items. Net investment income consists of interest income, dividend income and premium financing charges, less interest expense, as per note 6 of the Company's Financial Statements. Net operating income is adjusted to that attributable to shareholders for per share calculation.

(2) ROE calculated on rolling twelve-month basis

INSURANCE OPERATIONS

Direct Written and Net Earned Premiums

Direct written premiums increased by 31%, while net earned premiums increased 26%. The increase in premium was driven by organic growth in Personal Lines and new Commercial Lines products launched in 2016.

Claims Incurred

Net claims expense increased by 42% due to increased severity in Atlantic Auto, catastrophic losses from the British Columbia wild fires and increased Commercial Auto losses.

Net favourable development on prior year claims of $25.7 million was recorded in the year compared to $17.2 million in 2016. The favourable development arose from both the Personal Lines and Commercial Lines segments, with the majority (62%) arising from Ontario Auto within Personal Lines. $3.3 million of the aggregate development for the year related to a change in discount rate.

Acquisition Costs

Acquisition costs, which consist mainly of commissions, premium taxes and a portion of general expenses related to policy acquisitions, increased by 25% in line with the increase in net earned premiums.

Operating Expenses

Operating expenses increased $1.9 million or 6% to $31.0 million in 2017 compared to $29.2 million in the same period last year, primarily due to increased information technology and incremental headcount. The increase in operating expenses is lower than the growth rate of earned premiums, resulting in a decrease in the operating expense ratio.

Underwriting Income

Underwriting loss of $12.4 million was recorded in 2017 compared to an underwriting loss of $0.4 million in 2016. The underwriting loss was due to weak Personal Lines results.

Investment Income

Investment income increased by $0.7 million, to $17.2 million in 2017 compared to $16.5 million in 2016. Income from fair value changes on FVTPL investments of $3.5 million was comparable to an income of $3.9 million in the same period of 2016. The total fair value of the investment portfolio as at December 31, 2017, (including cash and short-term and premium financing receivables) was $469 million compared to $410 million as at December 31, 2016.

Net Income before Income Taxes

Income before taxes was $7.7 million in 2017, compared to $9.0 million in 2016, due to an increased underwriting loss and increase in discount rate on unpaid claims, which was offset by reduced severance expenses and slightly higher investment income.

Income Taxes

For the year ended December 31, 2017, the provision for income taxes reflects an expense of $0.9 million compared to an expense of $1.7 million for the same period last year. The approximate effective rate decreased to 13% for 2017 from 19% for the previous year.

BALANCE SHEET ANALYSIS

The Balance Sheet analysis that follows should be read in conjunction with the consolidated financial statements for the fourth quarter of 2017, and notes therein.

BALANCE SHEET HIGHLIGHTS

Selected balance sheet highlights and book value per share details are as follows:

($ THOUSANDS, EXCEPT PER SHARE AMOUNTS)	**2017**	2016	2015	2014	2013
Cash and short-term deposits	**44,459**	50,588	23,373	27,326	18,156
Investments	**370,933**	336,535	513,099	504,290	454,317
Total assets	**590,586**	800,219	923,795	740,299	619,928
Provision for unpaid claims	**262,966**	255,129	397,214	344,692	296,857
Unearned premiums	**160,577**	120,184	264,584	168,555	127,247
Total equity attributable to shareholders	**142,822**	137,414	180,935	183,616	172,360
Book value per share (1)	**$12.01**	$11.70	$15.75	$15.82	$14.57
MCT Ratio – Echelon Insurance	**212%**	237%	241%	211%	219%
– ICPEI	**355%**	340%	296%	229%	N/A

(1) Shareholders' equity divided by the number of shares issued and outstanding.

INVESTMENTS

EFH has an investment policy that seeks to provide a stable income base to support EFH's liabilities in line with its risk appetite and tolerance. In addition to this risk-return analysis, the chosen asset mix also considers the amount of regulatory capital that is required.

EFH's investment portfolio is invested in well-established, active and liquid markets in Canada. Fair value for most investments is determined by reference to observable market data.

FAIR VALUE OF INVESTMENTS

The following table sets forth EFH's invested assets as at December 31, 2017 and December 31, 2016.

($ THOUSANDS)	Fair values			
Available-for-sale	**As at December 31, 2017**	**% of Total**	As at December 31, 2016	% of Total
Fixed income				
Canadian				
Federal	**39,408**		67,826	
Provincial	**29,883**		44,147	
Municipal	**14**		519	
Corporate	**127,701**		136,984	
	197,006		249,476	
Fixed income lent through securities lending program				
Federal	**63,864**		15,390	
Provincial	**17,564**		998	
Municipal	**1,322**		845	
Corporate	**8,535**		1,885	
	91,285		19,118	
Total fixed income	**290,305**	**70%**	268,594	69%
Commercial mortgages pooled funds	**—**		17,423	
Money market pooled funds	**1,014**		200	
Short-term fixed income and mortgage pooled funds	**19,303**		17,229	
Specialty pooled fund	**8,240**		—	
Total pooled funds	**28,557**	**7%**	34,852	9%
Common shares				
Canadian	**889**		312	
Foreign	**8,428**		—	
Total common shares	**9,317**	**2%**	312	—%
Total available-for-sale	**328,179**		303,758	
Fair value through profit or loss				
Preferred shares	**42,754**		32,678	
Preferred shares lent through securities lending program	**—**		99	
Total preferred shares	**42,754**	**10%**	32,777	8%
Total investments	**370,933**	**89%**	336,535	86%
Cash and short-term deposits	**44,459**	**11%**	50,588	14%
Total investments including cash and short-term deposits	**415,392**	**100%**	387,123	100%

IMPAIRMENT ASSETS AND PROVISIONS FOR LOSSES

EFH has an established policy to write down or make a provision for any investment with objective evidence that the value of the investment is impaired.

There were no impairments recognized during the twelve months ended December 31, 2017 and 2016.

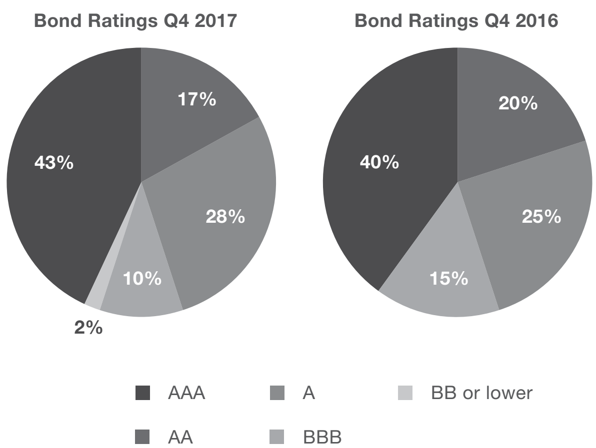
A gross unrealized loss of $3.3 million (December 31, 2016 – $1.7 million) on investments held as at December 31, 2017, is recorded, net of tax, in the amount of $2.4 million (December 31, 2016 – $1.2 million) in Accumulated Other Comprehensive Income. The Company has concluded, based on its review, that these fair value deficiencies do not meet the criteria for impairment and they will be monitored on an ongoing basis.

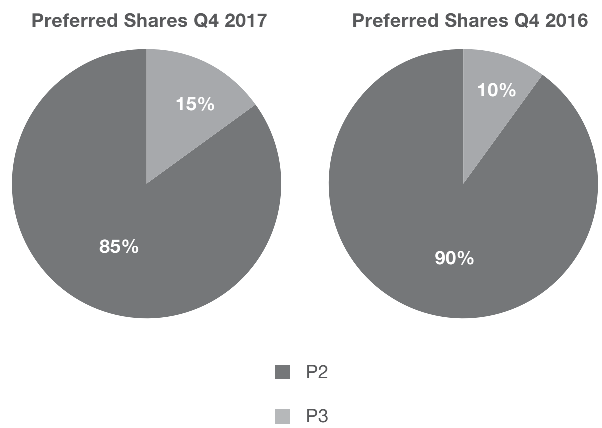
FIXED INCOME SECURITIES

EFH holds fixed income securities to provide a steady, predictable level of income with reasonable liquidity and minimal risk of loss and a fixed sum at maturity. EFH's portfolio is diversified by selecting various types of government and corporate bonds. Constraints on types of issuers take liquidity, diversification and risk into account by limiting the portfolio mix by issuer.

EFH's bond portfolio has a high overall credit quality with an average rating of AA. The preferred shares have an average rating of P2. The duration of the bond portfolio is 2.7 years.

The charts below show EFH's fixed income and preferred share portfolios by credit quality as at December 31, 2017 compared to December 31, 2016.





SECTOR MIX BY ASSET CLASS

The following table shows sector exposure by asset class as at December 31, 2017:

Sector	Fixed Income Securities & Pooled Funds [1]	Preferred Shares	Common Shares	Total
Government	51%	—%	—%	44%
Financial Services	26%	50%	17%	28%
Infrastructure	9%	—%	—%	8%
Industrial Products	4%	13%	18%	5%
Utilities	—%	31%	1%	4%
Energy	3%	—%	1%	3%
Pipelines	2%	6%	—%	2%
Telecommunication	2%	—%	4%	2%
Consumer Discretionary	—%	—%	32%	1%
Technology	—%	—%	17%	—%
Other	3%	—%	10%	3%
Total	100%	100%	100%	100%
Total	$317,699	$42,754	$9,317	$369,770

1) Fixed income securities and pooled funds do not include any cash being carried by the pooled funds, $1.2 million as at December 31, 2017.

COMMON SHARE PORTFOLIO

As at December 31, 2017, 10% of the common share portfolio was invested in Canadian equities.

RECOVERABLE FROM REINSURERS

($ THOUSANDS)	**As at December 31, 2017**	As at December 31, 2016
Reinsurers' share of unpaid claims	**23,471**	27,023
Reinsurers' share of unearned premiums	**9,957**	8,975
Total	**33,428**	35,998

As at December 31, 2017, the recoverable from reinsurers decreased by $2.6 million, or 7%, to $33.4 million from $36.0 million as at December 31, 2016. The increase in reinsurers share of unearned premium was due to growth while the decrease in reinsurers share of unpaid claims was due to an increase in the Company's retention on large claims in recent years. All reinsurers, with balances due, have a rating of A– or above as determined by Standard & Poor's and A.M. Best, except for several Specialty Programs distributors who share a portion of the risk with EFH, for whom the Company holds deposits as collateral.

ACCOUNTS RECEIVABLE

($ THOUSANDS)	**As at December 31, 2017**	As at December 31, 2016
Premium financing receivables	**53,538**	**32,216**
Agents and brokers	**17,215**	9,787
Other	**4,869**	4,702
Total	**75,622**	46,705

Premium financing receivables represent 71% of total receivables as at December 31, 2017. Premium financing receivables increased to $53.5 million at December 31, 2017, from $32.2 million at December 31, 2016, due to the growth in direct bill premiums. Agent and broker receivables increased from $9.8 million in 2016 to $17.2 million in 2017 due to growth in broker-billed premiums.

PROVISION FOR UNPAID CLAIMS

EFH establishes loss reserves to provide for future amounts required to pay claims related to insured events that have occurred and been reported but have not yet been settled, and related to events that have occurred but have not yet been reported to EFH. Provision for unpaid claims consists of the aggregate amount of individual case reserves established and management's estimate of claims incurred but not reported, based on the volume of business currently in force and historical claims experience and are determined by EFH's appointed actuary. Provisions for unpaid claims are discounted to present value. The Company determines the discount rate based on the expected return on its investment portfolio of assets with appropriate assumptions for interest rates relating to reinvestment of maturing investments. The investment portfolio has experienced an increase in yields compared to December 31, 2016. The discount rates used for December 31, 2017, and 2016 for the following entities are below:

Entity	**As at December 31, 2017**	As at December 31, 2016
Echelon Insurance	**2.65%**	1.90%
ICPEI	**2.80%**	1.75%

SHARE CAPITAL

As of February 15, 2018, there were 11,891,076 common shares issued and outstanding.

LIQUIDITY AND CAPITAL MANAGEMENT

The purpose of liquidity management is to ensure there is sufficient cash to meet all of EFH's financial commitments and obligations as they come due. EFH believes that it has the flexibility to obtain, from internal sources, the funds needed to fulfill its cash requirements, during the following financial year and to satisfy regulatory capital requirements.

Contractual obligations include operating leases, for which $1.8 million is due in less than a year and $9.1 million is due over the next eight years.

EFH is primarily a holding company and, as such, has limited direct operations of its own. EFH's principal assets are the shares of its insurance and reinsurance subsidiaries. Accordingly, its future cash flows depend in part upon the availability of dividends and other statutorily permissible distributions from its insurance subsidiaries. The ability to pay such dividends and to make such other distributions is limited by applicable laws and regulations of the jurisdictions in which the insurance subsidiaries are domiciled, which subject the insurance subsidiaries to significant regulatory restrictions. These laws and regulations require, among other things, that the insurance subsidiaries maintain minimum solvency requirements and may also limit the amount of dividends that the insurance subsidiaries can pay to EFH.

CAPITAL MANAGEMENT

The total capitalization of EFH at December 31, 2017, was $146.7 million compared to $141.4 million at December 31, 2016.

The Minimum Capital Test (MCT) ratio of the Company's subsidiary, Echelon Insurance, as at December 31, 2017, was 212%, which comfortably exceeds the supervisory regulatory capital level required by the Office of the Superintendent of Financial Institutions (OSFI). ICPEI's MCT ratio of 355% was in excess of provincial supervisory targets. As at December 31, 2017, the Company has approximately $29 million of excess deployable capital invested in equities and liquid assets in the holding company.

NORMAL COURSE ISSUER BID (NCIB)

No shares were repurchased in 2017. However, in the comparative period of 2016 there were 51,000 common shares repurchased and canceled at an average cost of $13.24 per share for a total consideration of $0.7 million.

YEAR ENDED DECEMBER 31, 2016 COMPARED TO 2015

The following chart compares results for the full year 2016 and 2015:

($ THOUSANDS, EXCEPT PER SHARE AMOUNTS)	2016	2015	$ Variance	% Variance
Direct written and assumed premiums	217,486	199,473	18,013	9%
Net written premiums	199,601	180,336	19,265	11%
Net earned premiums	181,060	176,468	4,592	3%
Net claims incurred	110,772	109,827	945	1%
Net acquisition costs	41,545	39,448	2,097	5%
Operating expenses	29,156	27,639	1,517	5%
Underwriting income (loss)	(414)	(447)	33	7%
Severance	(4,266)	—	(4,266)	N/A
Investment income	16,507	12,613	3,894	31%
Impact of discount rate – increase in claims	(2,822)	1,024	(3,846)	(376)%
Other income	—	748	(748)	(100)%
Net income before income taxes	9,005	13,938	(4,933)	(35)%
Interest expense	217	—	217	N/A
Income taxes expense	1,670	1,676	(6)	0%
Net income	7,118	12,262	(5,144)	(42)%
Net income attributable to shareholders	6,606	12,254	(5,648)	(46)%
Net operating income attributable to shareholders	10,354	9,922	432	4%
Earnings per share				
Basic	$0.56	$1.05	$(0.49)	(47)%
Diluted	$0.55	$1.02	$(0.47)	(46)%
Net operating income per share – diluted (1)	$0.86	$0.83	$0.03	4%
Trailing twelve-month return on equity (ROE) (2)	4.2%	6.7%		

(1) Net operating income is defined as underwriting income plus interest and dividend income, net of tax. Underwriting income excludes impact of change in claims discount rates, and non-recurring items. Net investment income consists of interest income, dividend income and premium financing charges, less interest expense, as per note 6 of the Company's Financial Statements. Net operating income is adjusted to that attributable to shareholders for per share calculation.

(2) ROE calculated on rolling twelve-month basis.

5 YEAR FINANCIAL HIGHLIGHTS

	Year ended December 31				
($ THOUSANDS, EXCEPT PER SHARE AMOUNTS)	**2017**	2016	2015	2014	2013
Revenue					
Direct written and assumed premiums					
Personal Lines	**189,454**	154,992	146,578	133,275	134,902
Commercial Lines	**96,264**	62,494	52,895	54,069	39,702
Total direct written premiums	**285,718**	217,486	199,473	187,344	174,604
Net written premiums	**266,807**	199,601	180,336	171,396	157,117
Net earned premiums	**227,396**	181,060	176,468	167,517	154,137
Underwriting expenses					
Incurred claims	**156,814**	110,772	109,827	92,966	101,363
Acquisition costs	**51,994**	41,545	39,448	40,824	36,799
Operating expenses	**31,031**	29,156	27,639	25,621	18,955
Total underwriting expense	**239,839**	181,474	176,915	159,411	157,117
Underwriting income (loss)	**(12,443)**	(414)	(447)	8,106	(2,980)
Impact of discount rate on claims	**3,254**	(2,822)	1,024	(2,391)	207
ICPEI Integration Cost	**—**	—	—	(1,347)	—
Severance expense	**(262)**	(4,266)	—	(1,166)	—
Investment income	**17,196**	16,507	12,613	22,019	17,474
Other income	**—**	—	748	—	—
Income before interest expense and income taxes	**7,745**	9,005	13,938	25,221	14,701
Interest expense	**155**	217	—	—	—
Income tax expense (recovery)					
Current	**921**	1,738	1,555	5,300	4,129
Deferred	**26**	(68)	121	209	(895)
	947	1,670	1,676	5,509	3,234
Net income on continued operations	**6,643**	7,118	12,262	19,712	11,467
Net income (loss) on discontinued operations attributable to shareholders of the Company	**(4,855)**	(36,646)	(5,677)	(980)	(7,742)
Net income	**1,788**	(29,528)	6,585	18,732	3,725
Attributed to:					
Shareholders of the Company	**6,489**	6,606	12,254	18,722	4,681
Non-controlling interest	**154**	512	8	10	(956)
	6,643	7,118	12,262	18,732	3,725
Earnings per share attributable to shareholders of the Company:					
Net income per share continued operations basic	**$0.55**	$0.56	$1.05	$1.72	$0.97
Net income per share continued operations diluted	**$0.54**	$0.55	$1.02	$1.67	$0.95
Book value per share	**$12.01**	$11.70	$15.75	$15.82	$14.57
Net operating income [1]	**613**	10,354	9,922	15,753	7,569
Net operating income per share – diluted [2]	**$0.05**	$0.86	$0.83	$1.31	$0.63

(1) Net operating income is defined as underwriting income plus interest and dividend income, net of tax. Net operating income is adjusted to that attributable to shareholders for per share calculation.
(2) Net operating income is adjusted to that attributable to shareholders for per share calculation.

OUTLOOK

EFH's long-term target is to deliver a minimum 12% after-tax return on shareholder's equity and a 95% combined ratio on its underwriting operations. The Company has made significant progress in the past year focusing on its core business in Canada, building a strong management team, focusing on broker relationships and improved technology. The overarching goal is to create a broker-focused insurance operation that offers a wide suite of profitable and sustainable insurance solutions, aligned directly to the broker's needs.

In 2018, we will continue execution on the strategy outlined below with a focus on underwriting profitability and maximizing our return on equity. We have a strong balance sheet that will provide us with a solid launching pad for 2018 and beyond.

STRATEGY

EFH's purpose is to bring piece of mind to individuals and businesses by protecting their assets. To do this, the company provides a range of insurance solutions that meet the evolving needs of our broker partners. EFH is committed to doing so while operating responsibly and ethically, and delivering strong underwriting results and return on shareholders' equity.

EFH's products are distributed exclusively through insurance brokers and agents. With a growing number of insurers selling directly to consumers, EFH's commitment to the broker channel differentiates Echelon Insurance and ICPEI from competitors and forms a foundation for mutually beneficial relationships. On this commitment, the Company has built and maintained an effective network of distribution partners by:

FOCUS ON CANADA OFFERING DIVERSE PRODUCTS THAT SATISFY UNMET NEEDS

The bulk of EFH's products were designed to respond to the unmet needs of our distribution partners.

Echelon Insurance has excelled in the non-standard auto market by delivering expertly underwritten coverage for hard-to-insure drivers. ICPEI's nuanced understanding of Maritime families and businesses has shaped the products and coverages that meet the unique needs of Atlantic Canadians. Now, Echelon Insurance has identified new areas where brokers are unsatisfied with existing products and service, and is responding by launching Surety and Commercial Auto solutions.

INVESTING IN TALENT AND LEVERAGING RELATIONSHIPS

EFH's management and underwriting teams have the skillsets to understand and effectively underwrite risks. Echelon Insurance and ICPEI benefit from this seasoned expertise, but also from employee reputations and long-standing relationships in their industries. With the addition of Commercial Automobile and Surety teams in 2016, EFH gained a number of new broker relationships.

IMPROVING TECHNOLOGY AND CONNECTIVITY

EFH is committed to investing in technology to connect more seamlessly with its brokers and agents. In 2014, The Company acquired and launched a new policy management system that will be instrumental in streamlining how brokers and agents write business with Echelon Insurance. It has rolled out this system across Canada, and is working towards consolidating its systems into this sole policy management system to simplify broker system interactions.

The type and number of distributors that EFH partners with varies by business line. Property and Automobile products are marketed through a broad network of insurance brokers and agents across Canada. These distributors have both the expertise to underwrite good risks, and the volume of premium to support good loss ratios in these business lines.

LINES OF BUSINESS

Personal Lines

EFH offers standard and specialty private passenger vehicle coverage in the Maritime provinces through ICPEI, and non-standard and specialty private passenger vehicle coverage across the rest of Canada through Echelon Insurance.

In addition to automobile products which form the bulk of EFH's Personal Lines business, Property coverage is offered in select provinces.

Personal Automobile

Non-standard Automobile insurance is the largest single component of EFH's business, with approximately $130 million in direct premiums written over the 12 months ended December 31, 2017. Offered through Echelon Insurance, the non-standard automobile product targets drivers of private passenger and single commercial vehicles who are unable to obtain coverage from standard insurers.

The Company provides coverage for specialty automobiles and recreational vehicles through both Echelon Insurance and ICPEI. Coverage is available for motorcycles, antique and classic cars, trailers, motorhomes, snowmobiles and all-terrain vehicles. Standard Personal and Commercial Automobile insurance is offered across the Maritimes through ICPEI only.

Moving forward, the Company intends to increase focus on profitable automobile products, evaluating whether these could be successfully expanded into new regional markets within Canada.

Personal Property

The Company offers homeowners, condo and tenant packages through ICPEI in the Maritimes and through Echelon Insurance in Quebec and British Columbia.

Commercial Lines

The Company writes Commercial Property, Liability and Automobile coverage for small- to mid-sized businesses under the Echelon Insurance and ICPEI brands.

In addition to standard commercial policies, Echelon Insurance also excels in niche business lines, including Surety, Commercial Automobile, and Specialty Programs. Since 2016, the Company has grown its Commercial Lines Management and underwriting teams to include seasoned experts with proven track records and deep networks in their respective markets. Commercial Lines represents $96 million, and 34% of the Company's business.

With a now-profitable portfolio and an experienced and connected management team, steps are underway to expand the Company's commercial product offering into Ontario, Quebec and Alberta. Echelon Insurance will target underserved and specialty brokers, offering flexible, risk-underwritten coverage.

Commercial Property & Casualty

EFH offers Commercial Property coverage in the Maritimes, Quebec and British Columbia, differentiating from competitors by applying risk vs. class underwriting. Simple, low-touch packages target small- to mid-sized businesses like contractors and professional service providers. Coverages can be customized to meet the more unique needs of larger businesses.

Commercial Automobile

The Company offers Commercial Automobile coverage through Echelon Insurance in Alberta, Ontario and Quebec, and through ICPEI in the Maritimes. Coverage is available for single vehicles, cargo trailers, fleets, and owner operators. Packaged policies are also offered to fleets and owner operators, and can be customized to include Commercial Automobile, Motor Truck Cargo Liability, Commercial General Liability, and Garage coverages, as well as special endorsements.

Specialty Programs

EFH partners with MGAs across Canada to underwrite a range of specialty and warranty programs including new home and home system warranties. In 2018, EFH will continue to grow its warranty programs by building deeper expertise and operational infrastructure in home, product and equipment warranty.

Surety

In 2016, Echelon Insurance introduced a Surety division to meet growing demand for mid-market surety bonds. Echelon Insurance focuses on distributing contract and commercial bonds through the broker channel. Unlike an insurance product, a surety bond is a guarantee issued to minimize the risk of a contractor's financial failure and inability to complete a construction project.

Organizational Strategies

EFH's key to profitable growth is personalized service and sophisticated pricing, underwriting and claims management. EFH will invest in its business and its people. It will continue to develop a sophisticated and scalable operational platform to grow. EFH will continue to invest aggressively in technology, with a focus on service and financial analytics.

COMPETITIVE STRENGTHS

EFH believes that it is uniquely positioned to deliver peace of mind to our customers by being a meaningful and committed partner to Canadian brokers for the following reasons:

Wide range of products and underwriting expertise

EFH offers its distributors a comprehensive line of personal and commercial insurance products, enabling them to meet the varying needs of their clients. Our underwriting teams are experienced and specialized, allowing EFH to effectively assess risks that don't fit the fully-automated processes of larger, standard insurers.

Entrepreneurial culture

EFH fosters a responsive team environment which encourages experimentation and allows the flexibility to provide unique, tailor-made solutions. The Company's values are collaborative, dynamic, respectful and focused.

Commitment to the broker channel

EFH's products are distributed exclusively through the broker channel. The Company believes that the insurance needs of Canadian individuals and businesses are best served by independent insurance brokers, who can ensure that they have the right insurance protection in place.

Financial strength

EFH has a strong capital base with shareholder equity of $142.8 million. The Minimum Capital Test (MCT) ratio of Echelon Insurance as at December 31, 2017, was 212% comfortably in excess of the Office of the Superintendent of Financial Institutions' (OSFI) supervisory target. In addition to any excess capital at Echelon, the Company has approximately $29 million of excess deployable capital invested in liquid assets in the holding company as at December 31, 2017.

It has a high quality investment portfolio with 100% of its fixed income portfolio in investment grade, 88% rated A and above and the average rating of the fixed income portfolio is AA. It has no debt on its balance sheet, little goodwill and intangible assets consisting mostly of computer software. Echelon has an A.M. Best financial strength rating of B++ (Good). EFH intends to maintain its strong balance sheet through appropriate pricing, underwriting discipline, conservative accounting and loss reserving practices.

RISK FACTORS

Careful consideration should be given to the following factors, which must be read in conjunction with the detailed information appearing elsewhere in this report. Any of the matters highlighted in these risk factors could have a material adverse effect on EFH's results of operations, business prospects or financial condition.

NATURE OF THE INDUSTRY

The P&C insurance business in Canada is affected by many factors which can cause fluctuations in the results of operations of EFH. Many of these factors are beyond EFH's control. An economic downturn in those jurisdictions in which EFH writes business could result in less demand for insurance and lower policy amounts. As a P&C insurance company, EFH is subject to claims arising out of catastrophes, which may have a significant impact on its results of operations and financial condition. These factors, together with the industry's historically cyclical competitive pricing, could result in fluctuations in the underwriting results and net income of EFH. A significant portion of the earnings of insurance companies is derived from the income from their investment portfolios. EFH's investment income will fluctuate depending on the returns and values of securities in its investment portfolio.

REGULATION

EFH is subject to the laws and regulations of the jurisdictions in which it carries on business. These laws and regulations cover many aspects of its business, including premium rates for automobile insurance; the assets in which it may invest; the levels of capital and surplus and the standards of solvency that it must maintain; and the amount of dividends which it may declare and pay.

Changes to laws or regulations are impossible to predict and could materially adversely affect EFH's business, results of operations and financial condition. Should OSFI be concerned about an unsafe course of conduct or an unsound practice in conducting the business of a federally regulated insurance company, OSFI may direct the insurance company to refrain from a course of action or to perform acts necessary to remedy the situation. In certain circumstances, OSFI may take control of the assets of an insurance company or take control of the company itself. More restrictive laws, rules or regulations may be adopted in the future that could make compliance more difficult and/or expensive. Specifically, recently adopted legislation addressing privacy issues, among other matters, is expected to lead to additional regulation of the insurance industry in the coming years, which could result in increased expenses or restrictions on EFH's operations.

COMPETITION

The P&C insurance business is highly competitive with pricing being a primary means of competition. Other elements of competition include availability and quality of products, quality and speed of service, financial strength, distribution systems and technical expertise.

EFH competes with many other insurance companies. Certain of these competitors are larger and have greater financial resources than EFH has. In addition, certain competitors have from time to time decreased their prices in an apparent attempt to gain market share.

As competitors introduce new products and as new competitors enter the market, the Company and its insurance subsidiaries may encounter additional and more intense competition. There can be no assurance that EFH will continue to increase revenues or be profitable. To a large degree, future revenues of EFH are dependent upon its ability to continue to develop and market its products and to enhance the capabilities of its products to meet changes in customer needs.

CYCLICALITY

Historically, the results of companies in the P&C insurance industry have been subject to significant fluctuations and uncertainties. The profitability of P&C insurers can be affected significantly by many factors, including regulatory regimes, developing trends in tort and class action litigation, adoption of consumer initiatives regarding rates or claims handling procedures, and privacy and consumer protection laws that prevent insurers from assessing risk, or factors that have a high correlation with risks considered, such as credit scoring.

The financial performance of the P&C insurance industry has historically tended to fluctuate in cyclical patterns of "soft" markets characterized generally by increased competition, resulting in lower premium rates and underwriting standards, followed by "hard" markets characterized generally by lessening competition, stricter underwriting standards and increasing premium rates. EFH's profitability tends to follow this cyclical market pattern with profitability generally increasing in hard markets and decreasing in soft markets. These fluctuations in demand and competition could produce underwriting results that would have a negative impact on EFH's results of operations and financial condition.

UNPREDICTABLE CATASTROPHIC EVENTS

Catastrophes can be caused by various natural and unnatural events. Natural catastrophic events include hurricanes, windstorms, earthquakes, hailstorms, explosions, severe winter weather and fires. Unnatural catastrophic events include hostilities, terrorist acts, riots, crashes and derailments. The incidence and severity of catastrophes are inherently unpredictable. The extent of losses from a catastrophe is a function of both the total amount of insured exposure in the area affected by the event and the severity of the event. Most catastrophes are restricted to small geographic areas; however, hurricanes, windstorms and earthquakes may produce significant damage in large, heavily populated areas. Catastrophes can cause losses in a variety of P&C insurance lines. Claims resulting from natural or unnatural catastrophic events could cause substantial volatility in EFH's financial results for any fiscal quarter or year and could materially reduce EFH's profitability or harm EFH's financial condition. EFH's ability to write new business also could be affected. EFH may experience an abrupt interruption of activities caused by unforeseeable and/or catastrophic events. EFH's operations may be subject to losses resulting from such disruptions. Losses can relate to property, financial assets, trading positions and also to key personnel. If EFH's business continuity plans cannot be put into action or do not take such events into account, losses may further increase.

INTEREST RATES

An increase in interest rates may result in lower values for EFH's bond portfolio and increased costs of borrowing for EFH on future debt instruments, preferred shares or credit facilities. Such increased costs would negatively affect EFH's operating results.

NEGATIVE PUBLICITY IN THE INDUSTRY

EFH's products and services are ultimately distributed to individual consumers. From time to time, consumer advocacy groups or the media may focus attention on EFH's products and services, thereby subjecting its industry to periodic negative publicity. EFH also may be negatively impacted if its industry engages in practices resulting in increased public attention to its business. Negative publicity may also result in increased regulation and legislative scrutiny of practices in the P&C insurance industry as well as increased litigation. Such consequences may increase EFH's costs of doing business and adversely affect EFH's profitability by impeding its ability to market its products and services or increasing the regulatory burdens under which EFH operates.

RELIANCE ON BROKERS

EFH distributes its products primarily through a network of brokers. These brokers sell EFH's competitors' products and may stop selling EFH products altogether. Strong competition exists among insurers for brokers with demonstrated ability to sell insurance products. Premium volume and profitability could be materially adversely affected if there is a material decrease in the number of brokers that choose to sell EFH products.

PRODUCT AND PRICING

EFH prices its products taking into account numerous factors, including claims frequency and severity trends, product line expense ratios, special risk factors, the capital required to support the product line, and the investment income earned on that capital. EFH's pricing process is designed to ensure an appropriate return on capital and long-term rate stability, avoiding wide fluctuations in rate unless necessary. These factors are reviewed and adjusted periodically to ensure they reflect the current environment.

However, pricing for automobile insurance must be submitted to each provincial government regulator and in certain Provinces pre-approved by the regulator. It is possible that, in spite of EFH's best efforts, regulator decisions may impede automobile rate increases or other actions that EFH may wish to take. Also, during periods of intense competition for any product line to gain market share, EFH's competitors may price their products below the rates EFH considers acceptable. Although EFH may adjust its pricing up or down to maintain EFH's competitive position, EFH strives to ensure its pricing will produce an appropriate return on invested capital. There is no assurance that EFH will not lose market share during periods of intense pricing competition.

UNDERWRITING AND CLAIMS

EFH is exposed to losses resulting from the underwriting of risks being insured and the exposure to financial loss resulting from greater than anticipated adjudication, settlement and claims costs. EFH's success depends upon its ability to accurately assess the risks associated with the insurance policies that EFH writes.

EFH's underwriting objectives are to develop business within EFH's target markets on a prudent and diversified basis and to achieve profitable underwriting results (i.e. a combined operating ratio below 100%). There can be no assurances that EFH will properly assess the risks associated with the insurance policies that it writes and may, therefore, experience increased adjudication, settlement and claims costs.

LOSS RESERVES AND CLAIMS MANAGEMENT

The amounts established and to be established by EFH for loss and loss adjustment expense reserves are estimates of future costs based on various assumptions, including actuarial projections of the cost of settlement and the administration of claims, estimates of future trends in claims severity and frequency, and the level of insurance fraud. Most or all of these factors are not directly quantifiable, particularly on a prospective basis, and the effects of these, and unforeseen factors could negatively impact EFH's ability to accurately assess the risks of the policies that it writes. In addition, future adjustments to loss reserves and loss adjustment expenses that are unanticipated by management could have an adverse impact upon the financial condition and results of operations of EFH. Although EFH's management believes its overall reserve levels as at December 31, 2017, are adequate to meet its obligations under existing policies, actual losses may deviate, perhaps substantially, from the reserves reflected in EFH's financial statements. To the extent reserves prove to be inadequate, EFH would have to increase such reserves and incur a charge to earnings.

ERRORS AND OMISSIONS CLAIMS

Where the Company acts as a licensed insurance agency, it is subject to claims and litigation in the ordinary course of business resulting from alleged errors and omissions in placing insurance. The placement of insurance and the handling of claims involve substantial amounts of money. Since errors and omissions claims against the Company may allege the Company's potential liability for all or part of the amounts in question, claimants may seek large damage awards and these claims can involve significant defense costs. Errors and omissions could include, for example, the Company's employees or sub-agents failing, whether negligently or intentionally, to place coverage or file claims on behalf of customers, to appropriately and adequately disclose insurer fee arrangements to its customers, to provide insurance providers with complete and accurate information relating to the risks being insured or to appropriately apply funds that it holds for its customers on a fiduciary basis. It is not always possible to prevent or detect errors and omissions, and the precautions the Company takes may not be effective in all cases.

EFH's business, financial condition and/or results may be negatively affected if its errors and omissions insurance coverage proves to be inadequate or unavailable. In addition, errors and omissions claims may harm EFH's reputation or divert management resources away from operating the business.

The Company maintains liability insurance covering errors or omissions that may occur while acting in its role as an insurance consultant. This coverage has an aggregate limit of liability of $2 million.

INVESTMENTS

EFH's investment assets are exposed to any combination of risks related to interest rates, foreign exchange rates and changing market values.

EFH's investment portfolio consists of diversified investments in fixed-income securities and preferred and common stocks. Investment returns and market values of investments fluctuate from time to time. A decline in returns could reduce the overall profitability of EFH. A change in interest rates, market values or foreign exchange rates may affect Echelon's regulatory strength tests.

REINSURANCE

Consistent with industry practice, EFH utilizes reinsurance to manage its claims exposure and diversifies its business by types of insurance and geographic area. The availability and cost of reinsurance are subject to prevailing market conditions that are generally beyond the control of EFH and may affect EFH's level of business and profitability. There can be no assurance that developments may not occur in the future which might cause a shortage of reinsurance capacity in those classes of business which EFH underwrites, which could result in the curtailment of issuing of policies in a certain line of business or containing limits above a certain size.

REINSURER CREDIT RISK

EFH's reinsurance arrangements are with a limited number of reinsurers. This reinsurance may cause an adverse effect on EFH's results of operations if one or more of its reinsurers are unable to meet its financial obligations. Although all of its reinsurers were rated A or higher by A.M. Best at the time of entering into the reinsurance arrangements, these ratings are subject to change and may be lowered.

Although reinsurance makes the assuming reinsurers liable to EFH to the extent of the risk each reinsurer assumes, EFH is not relieved of its primary liability to its insureds as the direct insurer. As a result, EFH bears credit risk with respect to its reinsurers. EFH cannot ensure that its reinsurers will pay all reinsurance claims on a timely basis or at all. EFH evaluates each reinsurance claim based on the facts of the case, historical experience with the reinsurer on similar claims, and existing law and includes in its reserve for uncollectible reinsurance any amounts deemed uncollectible. The inability to collect amounts due to EFH under reinsurance arrangements would reduce EFH's net income and cash flow.

TECHNOLOGY AND CYBER SECURITY RISK

EFH is heavily dependent on systems technology to process large volumes of transactions and there would be a risk if the technology employed is inadequate or inappropriate to support current and future business needs and objectives. EFH continues to implement new computer applications as part of a comprehensive approach to improve systems technology. EFH regularly tests and improves its Disaster Recovery and Business Continuity Plan to protect itself, its producers and policyholders in the event of a technology failure; however, there is no assurance that EFH will be able to respond to technology failures effectively and with minimal disruption.

The threat of cyber attacks is a major Infrastructure risk. As with all financial services, EFH faces continual challenges to protect its data and customer information. These attacks can come through hacking security controls and identity theft, including installing ransomware technology within our network. To ensure the Company is protected from these attacks, EFH has implemented cyber security programs to respond and manage through immediate detection of such threats, using sound best practices software and notification technologies.

LIQUIDITY

EFH manages its cash and liquid assets in an effort to ensure there is sufficient cash to meet all of EFH's financial obligations as they fall due. As a federally regulated insurance company, Echelon is required to maintain an asset base comprised of liquid securities that can be used to satisfy its ongoing commitments. EFH believes that internally generated funds provide the financial flexibility needed to fulfill cash commitments on an ongoing basis. EFH has no material commitments for capital expenditures; however, there can be no assurances that EFH's cash on hand and liquid assets will be sufficient to meet any future obligations that may come due.

FUTURE CAPITAL REQUIREMENTS

EFH's future capital requirements will depend upon many factors, including the expansion of EFH's sales and marketing efforts and the status of competition. There can be no assurance that financing will be available to EFH on acceptable terms, or at all. If additional funds are raised by issuing equity securities, further dilution to the existing stockholders will result. If adequate funds are not available, EFH may be required to delay, scale back or eliminate its programs. Accordingly, the inability to obtain such financing could have a material adverse effect on EFH's business, financial condition and results of operations.

RISK MANAGEMENT

EFH has developed a comprehensive process of risk management and internal control which emphasizes the proactive identification of risks facing the organization and the effective management and control of these risks. The foundation of the process is an ongoing thorough operational analysis by senior management committees and a structured oversight process undertaken by the Board of Directors and appointed committees. Underlying this structure are internal control procedures which are designed to safeguard EFH's assets and protect the organization and its stakeholders from potential risk.

As a provider of insurance products, effective risk management is fundamental to EFH's ability to protect the interests of EFH's customers and shareholders. The Company is exposed to risks of loss pertaining to insurance products. EFH is exposed to potential loss from various market risks, including interest rate and equity market fluctuation risk, credit risk, liquidity risk and, to a lesser extent, foreign currency risk.

MARKET RISK

Market risk is the risk of loss arising from adverse changes in market rates and prices, such as interest rates, foreign currency exchange rates, and other relevant market rate or price changes. Market risk is directly influenced by the volatility and liquidity in the markets in which the related underlying assets are traded. This risk is mitigated by matching liabilities and assets.

The primary market risk to the investment portfolio is the interest rate risk associated with investments in fixed income securities. EFH's exposure to unhedged foreign exchange risk is not significant. The investment policy is capital efficient and minimizes interest rate mismatch risk. Management does not currently anticipate significant changes in EFH's primary market risk exposures or in how those exposures are managed in future reporting periods based upon what is known or expected to be in effect in future reporting periods.

INTEREST RATE AND EQUITY MARKET FLUCTUATION

Movements in short- and long-term interest rates, as well as fluctuations in the value of equity securities, affect the level and timing of recognition of gains and losses on securities that EFH holds, and cause changes in realized and unrealized gains and losses. Generally, EFH's investment income will be reduced during sustained periods of lower interest rates as higher yielding fixed income securities are called, mature, or are sold and the proceeds are reinvested at lower rates. During periods of rising interest rates, the market value of EFH's existing fixed income securities will generally decrease and the realized gains on fixed income securities will likely be reduced. These will be partially offset by changes on the Company's discounted actuarial liabilities. General economic conditions, political conditions and many other factors can also adversely affect the stock markets and, consequently, the value of the equity securities EFH owns.

CREDIT RISK

Credit risk is the possibility that counterparties may not be able to meet payment obligations when they become due. The credit risk exposure is concentrated primarily in the fixed income and preferred share investment portfolios and, to a lesser extent, in reinsurance recoverables.

EFH's risk management strategy and investment policy is to invest in debt instruments of high credit quality issuers and to limit the amount of credit exposure with respect to any one issuer. The Company attempts to limit its credit exposure by imposing fixed income portfolio limits on individual corporate issuers based upon credit quality (see "Investments" – "Fixed Income Securities" and "Reinsurance" sections).

FOREIGN EXCHANGE RISK

Foreign exchange risk is the possibility that changes in exchange rates may produce an unintended effect on earnings and equity when measured in domestic currency.

EFH is exposed to foreign exchange risk on its receivable from the sale of its International segment's operations in Europe. The Company has entered into derivative contract with a major Canadian bank to hedge the principal repayment from the loan receivable from New Nordic Odin Guernsey Limited. The total notional value of the derivative contracts is $6.6 million.

CORPORATE GOVERNANCE

Active oversight remains a priority for the Board of Directors. The board is directly involved, through its committees, in overseeing all aspects of EFH's operation. The objective of the board is to meet or exceed best practices in corporate governance. There is independent oversight from the board and the respective committees to key corporate functions such as financial reporting, compliance, risk assessment and management, as well as human resources and succession planning.

EFH's Board of Directors has established the following committees to ensure that risks are effectively identified, monitored, controlled and reported on:

AUDIT AND RISK COMMITTEE

The Audit and Risk Committee reviews all financial information, monitors internal controls and provides oversight of management's risk-control processes, specifically focusing on financial related risks. Echelon also has an Audit and Risk Committee of its directors in accordance with the requirements of the Insurance Companies Act (Canada).

GOVERNANCE COMMITTEE

The Governance Committee is responsible for director nominations, monitoring related party transactions, officer compensation, benefit plans and the monitoring of regulatory compliance and market conduct programs put in place by management to ensure their effectiveness.

INVESTMENT COMMITTEE

The Investment Committee ensures that risks associated with the investment of corporate and policyholder funds are effectively managed to accomplish EFH's investment objectives of prudent, conservative management of funds and compliance with regulatory restrictions while achieving competitive rates of return.

In addition to these board committees, management has formed a number of working committees which have been assigned the responsibility of identifying and managing specific corporate risks, including (i) Underwriting and Claims committees to manage the risks associated with the development and pricing of EFH's products, claims adjudication and reserving; (ii) a Technology committee and a system prioritization committee to ensure the prioritization and implementation of effective technology solutions; (iii) an Enterprise Risk Management committee to instill a consistent approach to risk management and appropriate processes and procedures are in place to ensure compliance with all applicable regulatory requirements; (iv) a Reinsurance committee that works closely with EFH's reinsurance brokers to ensure that effective reinsurance programs are in place that provide EFH with protection against the occurrence of significant and unusual claims risk and development.

EFH has established a Disaster Recovery Plan and a Business Continuity Plan with the objectives of protecting critical Company information and infrastructure and resuming business operations in a timely effective manner in the event of a business interruption.

FUTURE CHANGES IN ACCOUNTING POLICIES AND DISCLOSURE

STANDARDS, AMENDMENTS AND INTERPRETATIONS NOT YET ADOPTED OR EFFECTIVE

IFRS 9, Financial Instruments

In July 2014, the IASB published the complete version of IFRS 9 which is effective for annual periods beginning on or after January 1, 2018, with retrospective application. The new standard includes requirements on the classification and measurement of financial assets and liabilities, an expected credit loss model that replaces the existing incurred loss impairment model and new hedge accounting guidance. The Company has evaluated and meets the requirements to defer the adoption of IFRS 9 until the new insurance contracts standard is adopted effective January 1, 2021.

IFRS 15, Revenue from contracts with customers

IFRS 15, Revenue from contracts with customers deals with revenue recognition and establishes principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. The standard replaces IAS 18 'Revenue' and IAS 11 'Construction contracts' and related interpretations. The standard is effective for annual periods beginning on or after January 1, 2018. Revenue arising from insurance contracts and from financial instruments is outside the scope of IFRS 15. There are no other revenues arising from other sources of income.

IFRS 16, Leases

In January 2016, the IASB published IFRS 16 which is effective January 1, 2019. The new standard requires the capitalization of all leases by recognizing the present value of the lease payments and showing them as lease assets, and recognizing a financial liability representing an obligation to make future lease payments. The Company has evaluated the impact of IFRS 16 on its Consolidated Financial Statements and based on its workings, the impact will be minimal.

IFRS 17, Insurance Contracts

In May 2017, the IASB published IFRS 17 which is effective January 1, 2021, with retrospective application. The standard replaces IFRS 4. The standard is comprehensive in scope and addresses recognition, measurement, presentation and disclosure for insurance contracts. The standard requires the entity to recognize a group of insurance contracts it issues from the earliest of the following: (a) the beginning of the coverage period of the group of contracts; (b) the date when the first payment from a policyholder in the group becomes due; and (c) for a group of onerous contracts, when the group becomes onerous. The measurement approach is based on the following building blocks: (i) a current, unbiased probability-weighted estimate of future cash flows expected to arise as the insurer fulfills the contract; (ii) the effect of the time value of money; (iii) a risk adjustment that measures the effects of uncertainty about the amount and timing of future cash flows; and (iv) a contractual service margin which represents the unearned profit in a contract (that is recognized in net earnings as the insurer fulfills its performance obligations under the contract). Estimates are required to be re-measured each reporting period. In addition, a simplified measurement approach is permitted for short-duration contracts in which the coverage period is approximately one year or less. The Company is currently evaluating the impacts of IFRS 17 on its consolidated financial statements.

CONTROLS AND PROCEDURES

DISCLOSURE CONTROLS AND PROCEDURES

The Company's disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed by EFH is recorded, processed, summarized and reported in a timely manner. This includes controls and procedures that are designed to ensure that information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

As of December 31, 2017, an evaluation was carried out, under the supervision of the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures as defined under Multilateral Instrument 52-109. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the design of these disclosure controls and procedures was effective.

INTERNAL CONTROLS OVER FINANCIAL REPORTING

As at the quarter ended December 31, 2017, the Chief Executive Officer and the Chief Financial Officer evaluated the design of the Company's internal control over financial reporting. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the design of internal controls as at December 31, 2017, was effective to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

A new policy management system is being rolled out across the country and management is satisfied that sufficient internal controls over financial reporting are in place during the transition and partial completion of the project.

CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The Company's significant accounting policies are disclosed in note 3 to the consolidated financial statements for the years ended December 31, 2017 and 2016.

The preparation of the Company's consolidated financial statements requires management to use estimates that affect the amounts reported in the financial statements. These estimates principally relate to the establishment of reserves for claims and expenses, impairments of investment securities, amounts recoverable from reinsurers and income taxes. As more information becomes known, these estimates could change and impact future results.

POLICY LIABILITIES

Policy liabilities consist of provisions for unpaid claims.

Provision for unpaid claims are maintained to cover the Company's estimated ultimate liability for unpaid losses and loss adjustment expenses with respect to reported and unreported claims incurred as of the end of each accounting period. The provision for unpaid claims and adjustment expenses is first determined on a case-by-case basis as claims are reported and then reassessed as additional information becomes known. The provision also accounts for the future development of these claims, including claims incurred but not reported (IBNR). Provisions for unpaid claims do not represent an exact calculation of liability, but instead represent estimates developed using projection techniques in accordance with Canadian accepted actuarial practice. These estimates are expectations of the ultimate cost of settlement and administration of claims based on the Company's assessment of facts and circumstances then known, its review of historical settlement patterns, estimates of trends in claims severity and frequency, legal theories of liability and other factors. The appointed actuary of EFH's subsidiaries, using appropriate actuarial techniques, evaluates the adequacy of the policy liabilities at the end of each reporting period.

Variables in the reserve estimation process can be affected by both internal and external events, such as changes in claims handling procedures, economic inflation, legal trends and legislative changes. Many of these items are not directly quantifiable, particularly on a prospective basis. Additionally, there may be significant reporting lags between the occurrence of the insured event and the time it is actually reported to the insurer. These estimates are refined in a systematic ongoing process as historical loss experience develops and additional claims are reported and settled. Because the establishment of reserves is an inherently uncertain process involving estimates, current reserves may not be sufficient. Adjustments to reserves, both positive and negative, are reflected in the consolidated statements of income for the period in which such estimates are updated.

The provision for unpaid claims and adjustment expenses is discounted to take into account the time value of money. Changes in market interest rates and investment portfolio yield are the primary factors influencing the discount rate. Based on the net provision for unpaid claims and adjustment expenses as at December 31, 2017, a 1% increase in the discount rate would result in a decrease in the net provision of $5.1 million and a 1% decrease in the discount rate would increase the net provision by $5.3 million. It also includes a provision for adverse deviation, as required by Canadian accepted actuarial practice.

IMPAIRMENT OF FINANCIAL ASSETS

The Company considers an impairment if there is objective evidence that an available-for-sale financial asset is impaired, including in the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its carrying value. The Company considers an impairment if there is objective evidence that a loan or receivable collectability is impaired at which time the Company will write down the loan or receivable to the expected recoverable cost.

Factors considered by the Company include but are not limited to:

a) significant financial difficulty of the issuer or obligor;

b) a breach of contract, such as a default or delinquency in interest or principal payments;

c) the lender, for economic or legal reasons relating to the borrower's financial difficulty, granting to the borrower a concession that the lender would not otherwise consider;

d) it becoming probable that the borrower will enter bankruptcy or other financial reorganization;

e) the disappearance of an active market for that financial asset because of financial difficulties; or

f) observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group, including:

   (i) adverse changes in the payment status of borrowers in the group (e.g., an increased number of delayed payments or an increased number of credit card borrowers who have reached their credit limit and are paying the minimum monthly amount); or

   (ii) national or local economic conditions that correlate with defaults on the assets in the group (e.g., an increase in the unemployment rate in the geographical area of the borrowers, a decrease in property prices for mortgages in the relevant area, a decrease in oil prices for loan assets to oil producers, or adverse changes in industry conditions that affect the borrowers in the group).

REINSURANCE

Reinsurer's share of the provision for unpaid claims include amounts for expected recoveries related to provision for unpaid claims. Amounts recoverable from reinsurers are estimated in a manner consistent with claim and claim adjustment expense reserves. The ceding of an insurance liability to a reinsurer does not discharge EFH's primary liability to the policyholders. The Company's policy is to record an estimated allowance for doubtful accounts on the basis of periodic evaluations of balances due from reinsurers, reinsurer solvency, credit ratings of reinsurers, collateral held by the Company, management's experience and current economic conditions.

The Company is exposed to disputes on, and defects in, contracts with reinsurers and the possibility of default by reinsurers.

INCOME TAXES

Deferred income taxes, accumulated as a result of temporary differences, which are probable to reverse, are included in the consolidated balance sheet. In addition, the consolidated statements of income contains items that are non-taxable or non-deductible for income tax purposes, which cause the income tax provision to differ from what it would be if based on statutory rates. Recoverability of deferred tax assets is primarily based on current and expected profitability applicable to the Company and its ability to utilize any recorded tax assets taking into consideration tax planning strategies and the expiry date of tax losses.

DEFERRED POLICY ACQUISITION COST

Portion of the deferred policy acquisition costs include general expenses that are capitalized based on management judgement.

GLOSSARY OF SELECTED INSURANCE TERMS

"Acquisition costs" commissions, premium taxes and a portion of general expenses related to policy acquisitions.

"Acquisition Expense ratio" for any period means the sum of the acquisition costs divided by Net earned premiums.

"Assumed written premiums" of an insurer for any period means the total insurance premiums written by the insurer while acting as a reinsurer during such period.

"Broker" an intermediary who negotiates policies of insurance or reinsurance with insurers on behalf of the insured or reinsured, receiving a commission from the insurer or the reinsurer for placement and other services rendered.

"Catastrophe event" or **"CAT event"** refers to a group of claims from a specific event considered to be non-recurring and therefore not reflective of normal operating performance.

"Catastrophe reinsurance" a form of insurance, which subject to specified limits, indemnifies the ceding company for the amount of loss in excess of a specified retention amount with respect to an accumulation of losses resulting from a CAT event.

"Cede" means the act of an insurer transferring or assigning part or all of the risk of an insurance policy written by it to a reinsurer by purchasing insurance from such reinsurer to cover the risk or part thereof.

"Ceded earned premiums" means ceded written premium during the period, plus the ceded unearned premiums reserve at the beginning of the period, less the ceded unearned premiums reserve at the end of the period.

"Ceded written premiums" of an insurer for any period means the total insurance premiums written transferred by the insurer to a reinsurer during such period.

"Claim" the amount owed by an insurer or reinsurer pursuant to a policy of insurance or reinsurance arising from the loss relating to an insured event.

"Claims development" a non-IFRS measure representing the change in reserve balance on unpaid claims through the process of adjudication from the initial estimate to the ultimate amount paid. The difference between prior year end estimates of ultimate undiscounted claim costs and the current estimates for the same block of claims. A favourable development represents a reduction in the estimated ultimate claim costs during the period for that block of claims. An unfavourable development represents an increase in the estimated ultimate claims costs during the period.

"Combined ratio" of an insurer for any period means the sum of the loss ratio and the expense ratio of the insurer for such period.

"Deferred policy acquisition expenses (DPAC)" means the portion of acquisition costs within a policy term which have not yet earned.

"Direct written premiums" of an insurer for any period means the total insurance premiums written by the insurer during such period.

"Expense ratio" for any period means the sum of the acquisition expense ratio and the general expense ratio.

"Facility Association" is an unincorporated non-profit organization established by the automobile insurance industry to ensure that automobile insurance is available to all owners and licensed drivers of motor vehicles where such owners or drivers are unable to obtain automobile insurance through the voluntary insurance market

"Frequency of claims" the ratio of the number of claims files opened in a period to the total number of policies in force. A measure of how often a claim is reported as a function of policies in force.

"General Expense ratio" for any period means the sum of all general expenses divided by Net earned premiums.

"Gross CASE Loss ratio" for any period means the sum of gross claims and gross claims adjustment expenses incurred expressed as a percentage of gross earned premiums.

"Gross earned premiums" means written premium during the period, plus the unearned premiums reserve at the beginning of the period, less the unearned premiums reserve at the end of the period.

"Gross Ultimate Loss ratio" for any period means the sum of claims, claims adjustment expenses and IBNR incurred expressed as a percentage of gross earned premiums.

"Incurred but not reported (IBNR)" the estimate of claims incurred but not yet reported by policyholders and not enough case reserve.

"Industry pools" consist of the "residual market" as well as mandatory risk-sharing pools (RSP) in Alberta, Ontario, Quebec, New Brunswick and Nova Scotia. These pools provide automobile insurance to individuals who are otherwise unable to purchase such coverage from private insurers acting voluntarily. All insurance companies share in the results of the pool according to their market share.

"Large Loss" a single claim in excess of $100,000.

"Line of business" the major product groupings offered to the public.

"Loss adjustment expenses" or **"LAE"** means the expense of settling claims, including certain legal and other fees and the expense of administering the claims adjustment process.

"Market yield adjustment (MYA)" a non-IFRS measure representing the impact of changes in the discount rate on claims liabilities, the provision for adverse deviation (PFADs) and other discounting assumptions based on the change in the market-based yield of the underlying assets.

"Managing General Agent (MGA)" is an individual or business entity appointed by an insurer to solicit applications from agents for insurance contracts or to negotiate insurance contracts on behalf of an insurer and, if authorized to do so by an insurer, to effectuate and countersign insurance contracts.

"Minimum Capital Test" means the regulatory guideline under which a federally regulated insurer is measured for the adequacy of its capital.

"Net CASE Loss ratio" for any period means the sum of claims and claims adjustment expenses incurred less any ceded claims and claim expenses incurred expressed as a percentage of net earned premiums.

“Net earned premiums” of an insurer is the gross earned premiums less the ceded earned premiums.

“Net Operating Income” means net income plus or minus the after-tax impact of change in market yield adjustment, realized losses or gains on sale of investments, discontinued operations, unrealized fair value changes on FVTPL investments and one-time non-recurring charges.

“Net Ultimate Loss ratio” for any period means the sum of claims, claims adjustment expenses and IBNR incurred less any ceded claims, claim expenses and IBNR incurred expressed as a percentage of net earned premiums.

“Net written premiums” of an insurer for any period means direct written premiums less ceded written premiums.

“Producers” refers to, collectively, insurance brokers, agents and managing general agencies.

“Property and casualty (P&C) insurance” all insurance excluding life insurance and governmental insurance. Also known as general insurance.

“Provision for adverse deviation (PFAD)” margins that are added to loss reserves to provide for adverse deviation from claims reserve estimates; this includes provisions covering claims development variability and risks associated with interest rate and reinsurance recoveries.

“Reinsurance” means an arrangement in which an insurance company agrees to indemnify another insurance or reinsurance company against all or a portion of the insurance or reinsurance risks underwritten by the ceding company under one or more policies.

“Retention” has two meanings: (1) in respect of reinsurance, the amount of risk not ceded to reinsurers; (2) in respect to policies in force, the number of policyholders who renew for a subsequent term.

“Return on equity” or **“ROE”** for a period means net income expressed as a percentage of the average total shareholder equity in that period.

“Salvage recoverable” is the estimated value of damaged property that may be retrieved, reconditioned, and sold to reduce the amount of an insured loss.

“Severity of claims” the average cost of each claim, based on the total claims cost and number of claims opened in a period.

“Subrogation recoverable” is the estimate of the amount the insurer will collect from a negligent third party or their insurer after assuming the insured’s legal right to collect damages.

“Underwriting” means the assumption of risk for designated loss or damage by issuing a policy of insurance in respect thereof.

“Underwriting income or loss” a non-IFRS measure calculating the profit or loss from the activity of taking on insurance risks, excluding the impact of the market yield adjustment.

“Unearned Commissions” means the portion of reinsurance commissions within a policy term which have not yet earned.

“Unearned premiums” means the portion of premiums within a policy term which have not yet earned.

“Unearned premiums recoverable” means the portion of ceded written premiums within a policy term which have not yet earned.

“Unpaid claims and adjustment expenses” the liability to cover the estimated remaining cost of settling claims, including IBNR.

“Unpaid claims and adjustment expenses recoverable” the portion of the unpaid claims and adjustment expense that will be reimbursed by reinsurers.’

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

ROLES OF MANAGEMENT, BOARD OF DIRECTORS AND AUDIT AND RISK COMMITTEE

Management is responsible for the preparation and fair presentation of the financial statements, Management's Discussion and Analysis and other information in the annual report. The financial statements of Echelon Financial Holdings Inc. ("the Company") were prepared in accordance with International Financial Reporting Standards. Where necessary, these financial statements reflect amounts based on the best estimates and judgement of management.

In meeting its responsibility for the reliability of the consolidated financial statements, management maintains the necessary system of internal controls. These controls are designed to provide management with reasonable assurance that the financial records are reliable for preparing financial statements and other financial information, assets are safeguarded against unauthorized use or disposition and liabilities are recognized. The Audit and Risk Committee, composed of directors who are not officers or employees of the Company, meets, as required, with management, the Appointed Actuary and the external auditor to review actuarial, accounting, reporting and internal control matters. The Audit and Risk Committee is responsible for reviewing the financial statements and Management's Discussion and Analysis and recommending them to the Board of Directors for approval.

ROLE OF APPOINTED ACTUARY

The Actuary is appointed by the Board of Directors, pursuant to the Insurance Companies Act. The Appointed Actuary is responsible for ensuring that the assumptions and methods used in the valuation of policy liabilities are in accordance with accepted actuarial practice, applicable legislation and associated regulations or directives. The Appointed Actuary is also required to provide an opinion regarding the appropriateness of the policy liabilities to meet all policyholder obligations of the Company at the balance sheet date. Examination of supporting data for accuracy and completeness and consideration of the Company's assets are important elements of the work required to form this opinion. The Appointed Actuary uses the work of the external auditor in verifying data used for valuation purposes. Policy liabilities include unearned premiums, provision for unpaid claims, reinsurers' share of unearned premiums and provision for unpaid claims and deferred policy acquisition costs.

ROLE OF EXTERNAL AUDITOR

PricewaterhouseCoopers LLP, external auditor, has been appointed by the shareholders to conduct an independent audit of the consolidated financial statements of the Company in accordance with Canadian generally accepted auditing standards and report to the shareholders regarding the fairness of the annual financial statements. The external auditor considers the work of the Appointed Actuary in respect of policy liabilities included in the financial statements, on which the Appointed Actuary has rendered an opinion.

Serge Lavoie
Chief Executive Officer

Alvin Sharma
Chief Financial Officer

Toronto, Ontario
February 15, 2018

INDEPENDENT AUDITOR'S REPORT

February 15, 2018

pwc

TO THE SHAREHOLDERS OF ECHELON FINANCIAL HOLDINGS INC.

We have audited the accompanying consolidated financial statements of Echelon Financial Holdings Inc. and its subsidiaries, which comprise the consolidated balance sheets as at December 31, 2017 and the consolidated statements of income and comprehensive income, changes in equity and cash flows for the year then ended, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

MANAGEMENT'S RESPONSIBILITY FOR THE CONSOLIDATED FINANCIAL STATEMENTS

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

OPINION

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Echelon Financial Holdings Inc. and its subsidiaries as at December 31, 2017 and 2016 and their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers LLP

Chartered Professional Accountants,
Licensed Public Accountants

PricewaterhouseCoopers LLP
PwC Tower, 18 York Street, Suite 2600, Toronto, Ontario, Canada, M5J 0B2
T: +1 416 863 1133, F: +1 416 365 8215

APPOINTED ACTUARY'S REPORT

WillisTowersWatson

TO THE SHAREHOLDER OF ECHELON FINANCIAL HOLDINGS INC.

I have valued the policy liabilities and reinsurance recoverables of the following subsidiary insurance operations of Echelon Financial Holdings Inc.: Echelon Insurance, Insurance Company of Prince Edward Island and the Warranty business of Echelon Financial Holdings Inc., for their statement of financial position at December 31, 2017 and their changes in the statements of income and comprehensive income for the year then ended in accordance with accepted actuarial practice in Canada including selection of appropriate assumptions and methods. In my opinion, the amount of policy liabilities for Echelon Insurance, Insurance Company of Prince Edward Island and the Warranty business of Echelon Financial Holdings Inc. make appropriate provision for all their policy obligations. The financial statements of Echelon Insurance, Insurance Company of Prince Edward Island and the Warranty business of Echelon Financial Holdings Inc. fairly present the results of those companies. The consolidated financial statements are the sum of my valuation for Echelon Insurance, Insurance Company of Prince Edward Island and the Warranty business of Echelon Financial Holdings Inc.

Nicolas Beaudoin
Fellow, Canadian Institute of Actuaries

Toronto, Ontario
February 15, 2018

175 Bloor Street East
South Tower
Suite 1701
Toronto, Ontario
M4W 3T6

T +1 416 960.2700
F +1 416 960 2819
W willistowerswatson.com

Towers Watson Canada Inc.

CONSOLIDATED BALANCE SHEETS

(in thousands of Canadian dollars)

	Note	Dec. 31, 2017	Dec. 31, 2016
Assets			
Cash and short–term deposits	6	**44,459**	50,588
Accounts receivable		**75,622**	46,705
Loan receivable	7	**6,553**	—
Investments (including securities on loan)	6	**370,933**	336,535
Due from insurance companies		**510**	1,587
Deferred policy acquisition costs	10	**40,888**	30,689
Income taxes recoverable		**1,001**	867
Prepaid expenses and other assets		**2,462**	2,270
Reinsurers' share – unearned premiums	11	**9,957**	8,975
– provision for unpaid claims	12	**23,471**	27,023
Property and equipment		**859**	881
Intangible assets	15	**8,037**	8,197
Deferred income taxes	16	**5,834**	5,860
Assets of the disposal group held for sale	27	**—**	280,042
Total assets		**590,586**	800,219
Liabilities			
Derivative financial instruments	8	**—**	268
Accounts payable and accrued liabilities		**18,116**	17,332
Payable to insurance companies		**610**	450
Unearned premiums	11	**160,577**	120,184
Unearned commission	10	**1,667**	2,288
Provision for unpaid claims	12	**262,966**	255,129
Liabilities of the disposal group held for sale	27	**—**	263,194
Total liabilities		**443,936**	658,845
Equity			
Share capital	17	**71,520**	70,227
Contributed surplus		**248**	322
Retained earnings		**73,887**	71,935
Accumulated other comprehensive income	25	**(2,833)**	(5,070)
Equity attributed to shareholders of the Company		**142,822**	137,414
Non-controlling interest	28	**3,828**	3,960
Total equity		**146,650**	141,374
Total liabilities and equity		**590,586**	800,219

The accompanying notes are an integral part of these consolidated financial statements approved on February 15, 2018.

On behalf of the Board of Directors:

Serge Lavoie
Chief Executive Officer

Murray Wallace
Chairman of the Board

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

(in thousands of Canadian dollars, except per share amounts)

	Note	2017	2016
Revenue			
Gross written and assumed premiums		**285,718**	217,486
Less: Premiums ceded to reinsurers		**(18,911)**	(17,885)
Net written and assumed premiums		**266,807**	199,601
(Increase) in gross unearned premiums		**(40,393)**	(19,338)
Increase in unearned premiums, reinsurers' share		**982**	797
Change in provision for unearned premiums		**(39,411)**	(18,541)
Net earned premiums		**227,396**	181,060
Investment income	6	**17,196**	16,507
Total revenue		**244,592**	197,567
Expenses			
Gross claims incurred		**160,895**	114,587
Less: claims recoveries from reinsurers		**(4,081)**	(3,815)
Net incurred claims		**156,814**	110,772
Gross acquisition costs		**58,059**	47,227
Less: acquisition cost recoveries from reinsurers		**(6,065)**	(5,682)
Net acquisition costs		**51,994**	41,545
Operating costs	20	**31,293**	33,423
Total expenses		**240,101**	185,740
Income before taxes and discount rate impact on claims		**4,491**	11,827
Impact of change in discount rate on claims[1]	12	**3,254**	(2,822)
Income before interest expense and income taxes		**7,745**	9,005
Interest expense	9	**155**	217
Income tax expense	16	**947**	1,670
Net income on continued operations		**6,643**	7,118
Net (loss) on discontinued operations	27	**(4,855)**	(36,646)
Net income (loss)		**1,788**	(29,528)
Attributed to:			
Shareholders of the Company – continued operations		**6,489**	6,606
Shareholders of the Company – discontinued operations	27	**(4,855)**	(36,414)
Non-controlling interest – continued operations	28	**154**	512
Non-controlling interest – discontinued operations	27	**—**	(232)
Net income (loss)		**1,788**	(29,528)
Other comprehensive income (loss), net of taxes that may be classified subsequently to net income			
Available-for-sale investments:			
Change in net unrealized (losses)/gains		**(2,323)**	(459)
Reclassification of net realized (gains) losses to net income		**425**	(5,597)
Cumulative translation gain (loss)		**—**	(395)
(Loss) gain on foreign exchange forward	6	**(4,314)**	4,314
Tax impact		**1,213**	291
Other comprehensive (loss) on continued operations		**(4,999)**	(1,846)
Other comprehensive income (loss) on discontinued operations	27	**7,268**	(9,459)
Other comprehensive income (loss)		**2,269**	(11,305)

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

(in thousands of Canadian dollars, except per share amounts)

	Note	2017	2016
Attributed to:			
Shareholders of the Company – continued operations		**(4,932)**	(1,794)
Shareholders of the Company – discontinued operations	27	**7,268**	(9,336)
Non-controlling interest – continued operation	28	**(67)**	(52)
Non-controlling interest – discontinued operation	27	**—**	(123)
Other comprehensive income (loss)		**2,269**	(11,305)
Total comprehensive income (loss)		**4,057**	(40,833)
Attributed to:			
Shareholders of the Company – continued operations		**1,557**	4,812
Shareholders of the Company – discontinued operations	27	**2,413**	(45,750)
Non-controlling interest – continued operation	28	**87**	460
Non-controlling interest – discontinued operation	27	**—**	(355)
Total comprehensive (loss) income		**4,057**	(40,833)
Earnings per share attributable to shareholders of the Company	26		
Earnings per share continued operations – basic		**$0.55**	$0.56
(Loss) per share discontinued operations – basic		**$(0.41)**	$(3.10)
Earnings (loss) per share – basic		**$0.14**	$(2.54)
Earnings per share continued operations – diluted		**$0.54**	$0.55
(Loss) per share discontinued operations – diluted		**$(0.41)**	$(3.10)
Earnings (loss) per share – diluted		**$0.14**	$(2.54)
Net income (loss)		**1,788**	(29,528)

(1) As the interest rate changes every year there is an impact to the incurred claims. Management believes it is beneficial to the user to see the impact of this change separately in order to understand the true movement in claims incurred.

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

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(in thousands of Canadian dollars)

	Share Capital	Contributed Surplus	Accumulated Other Comprehensive Income	Retained Earnings	Shareholders' Equity	Non-controlling Interest	Total Equity
Balance at January 1, 2017	**70,227**	**322**	**(5,070)**	**71,935**	**137,414**	**3,960**	**141,374**
Net income	**—**	**—**	**—**	**1,634**	**1,634**	**154**	**1,788**
Other comprehensive income	**—**	**—**	**2,336**	**—**	**2,336**	**(67)**	**2,269**
Total comprehensive income	**—**	**—**	**2,336**	**1,634**	**3,970**	**87**	**4,057**
Transfer of currency translation adjustment	**—**	**—**	**(99)**	**318**	**219**	**(219)**	**—**
Common shares issued on stock options exercised	**1,293**	**(147)**	**—**	**—**	**1,146**	**—**	**1,146**
Stock compensation expense	**—**	**73**	**—**	**—**	**73**	**—**	**73**
Balance at December 31, 2017	**71,520**	**248**	**(2,833)**	**73,887**	**142,822**	**3,828**	**146,650**

	Share Capital	Contributed Surplus	Accumulated Other Comprehensive Income	Retained Earnings	Shareholders' Equity	Non-controlling interest	Total Equity
Balance at January 1, 2016	69,653	436	6,060	104,786	180,935	4,010	184,945
Net income (loss)	—	—	—	(29,808)	(29,808)	280	(29,528)
Other comprehensive income (loss)	—	—	(11,130)	—	(11,130)	(175)	(11,305)
Total comprehensive income (loss)	—	—	(11,130)	(29,808)	(40,938)	105	(40,833)
Common shares repurchased	(292)	—	—	(384)	(676)	—	(676)
Dividends paid	—	—	—	(2,814)	(2,814)	—	(2,814)
Investment in subsidiary – Qudos	—	—	—	155	155	(155)	—
Common shares issued on stock options exercised	866	(170)	—	—	696	—	696
Stock options expense	—	56	—	—	56	—	56
Balance at December 31, 2016	70,227	322	(5,070)	71,935	137,414	3,960	141,374

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands of Canadian dollars)

	12 months ended	
	Dec. 31, 2017	Dec. 31, 2016
Cash provided by (used in):		
Operating activities		
Net income from continued operations	**6,643**	7,118
Net loss from discontinued operations	**(4,855)**	(36,646)
Adjusted for:		
Reinsurers' share of unearned premiums	**(982)**	(797)
Reinsurers' share of unpaid claims	**3,552**	2,199
Provision for unpaid claims	**7,837**	(5,719)
Unearned premiums	**40,393**	19,338
Deferred income taxes	**26**	(639)
Unearned commissions	**(621)**	324
Deferred policy acquisition costs	**(10,199)**	(5,771)
Amortization on property plant equipment and intangible assets	**5,378**	4,136
Amortization of premiums on bonds	**1,784**	1,897
Fair value change on FVTPL investments	**(3,503)**	(3,870)
Options expense	**73**	56
Currency translation	**—**	(395)
Foreign exchange forward	**(4,314)**	4,314
Prepaid expenses and other assets	**(192)**	401
	39,232	15,474
Cash flow from changes in		
Accounts receivable	**(28,917)**	(12,739)
Loan receivable	**(6,553)**	––
Net realized losses (gains)	**1,352**	(280)
Income taxes payable	**1,080**	2,817
Due to insurance companies	**1,237**	(409)
Other liabilities	**516**	5,408
Cash provided by continuing operating activities	**14,590**	17,389
Cash (used) provided by discontinued operating activities	**(135,522)**	488
Cash (outflow) inflow from operating activities	**(120,932)**	17,877
Financing activities		
Proceeds from issuing of common shares for stock options	**1,146**	696
Common share dividends	**—**	(2,814)
Share repurchases	**—**	(676)
Cash provided (used) by continuing financing activities	**1,146**	(2,794)
Cash inflow (outflow) from financing activities	**1,146**	(2,794)
Investing activities		
Purchases of property, equipment and intangible assets	**(5,196)**	(6,397)
Purchases of investments	**(308,015)**	(344,787)
Sale/maturity of investments	**272,085**	406,975
Proceeds received from the sale of subsidiary	**16,731**	—
Cash (used) provided by continuing investing activities	**(24,395)**	55,791
Cash provided by discontinued investing activities	**51,005**	43,388
Cash inflow from investing activities	**26,610**	99,179
(Decrease) increase in cash and short-term deposits	**(93,176)**	114,262
Cash and short-term deposits, beginning of period	**137,635**	23,373
Cash and short-term deposits, end of period	**44,459**	137,635
Supplementary information		
Operating activities		
Income taxes paid (recovered)	**93**	(1,712)

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(in thousands of Canadian dollars, except per share amounts)

1 NATURE OF OPERATIONS

Echelon Financial Holdings Inc. ("the Company") was incorporated in Canada on August 18, 1997, under the Business Corporations Act (Ontario). The Company is domiciled in Canada and principally engaged, through its subsidiaries, in property and casualty insurance in Canada. The Company's head office is located at 2680 Matheson Blvd. East, Suite 300, Mississauga, Ontario.

The Company's wholly-owned subsidiaries are Echelon Insurance ("Echelon"), CIM Reinsurance Company Ltd. ("CIM Re") and CUISA Managing General Agency Corporation ("CUISA MGA"). The Company also owns 75% of The Insurance Company of Prince Edward Island ("ICPEI").

The Company completed the sale of Qudos Insurance A/S ("Qudos") March 7, 2017. Please refer to note 27.

2 BASIS OF PREPARATION

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) and IFRS Interpretations Committee interpretations applicable to companies reporting under IFRS.

These consolidated financial statements have been authorized for issue by the Board of Directors on February 15, 2018.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF MEASUREMENT

The consolidated financial statements have been prepared under the historical cost convention, except for investments and insurance contracts which are carried at fair value and in accordance with IFRS 4, respectively. Discontinued operations are held for sale as described below.

BALANCE SHEET PRESENTATION

The Company does not classify its assets and liabilities as current and non-current on its balance sheets. As a financial institution, the Company provides insurance services over a period of years, rather than within a clearly identifiable short-term operating cycle. The consolidated statement of financial position is presented in the order of liquidity, based on expectations regarding recovery or settlement within 12 months after the reporting date, and more than 12 months after the reporting date as presented in the respective notes.

The maturity profile of the investment portfolio is described in note 14 based on expected settlements. The estimated payment period for insurance claims, less related reinsurance recoverable, is provided in note 14. Property and equipment assets are charged to expense over their estimated useful lives of up to three years. Intangible assets with finite useful lives are charged to expense over their estimated useful lives of two years while an impairment analysis is done on all other intangible assets. Cash and short-term deposits, accounts receivables due from insurance companies, income taxes receivables and payable, accounts payable and accrued liabilities are expected to be recovered or settled within twelve months of the period end.

CONSOLIDATION

The consolidated financial statements of the Company consolidate the accounts of Echelon Financial Holdings Inc. and its subsidiaries. All inter-company transactions, balances and unrealized gains and losses from inter-company transactions are eliminated on consolidation.

Subsidiaries are those entities which Echelon Financial Holdings Inc., through its investment in the entity, are exposed or has rights to variable returns from its involvement with the investee, and has the ability to affect those returns through its power over the investee. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether Echelon Financial Holdings Inc. controls another entity. Subsidiaries are fully consolidated from the date on which control is obtained by Echelon Financial Holdings Inc. and are de-consolidated from the date that control ceases.

Non-controlling interests represent equity interests in subsidiaries owned by outside parties. The share of net assets of subsidiaries attributable to non-controlling interests is presented as a component of equity. Changes in the parent company's ownership interest in subsidiaries that do not result in a loss of control are accounted for as equity transactions.

SEGMENT REPORTING

Operating segments are reported in a manner consistent with the internal reporting provided to senior management, the Chief Executive Officer and Board of Directors of the Company.

DISCONTINUED OPERATIONS

Assets and liabilities are classified as held for sale (discontinued operations) if their carrying amounts are recovered through a sales transaction rather than through continuing use. This condition is satisfied when the asset is available for immediate sale in its present condition, management is committed to the sale and it is highly probable to occur within one year. Assets classified as held-for-sale are measured at their lower of their previous carrying amount and fair value, less costs to sell, and are presented separately from other assets on our Consolidated Balance Sheets.

A disposal group is classified as a discontinued operation if it meets the following conditions: (a) it is a component that can be distinguished operationally and financially from the rest of our operations, and (b) it represents either a separate major line of business or is part of a single coordinated plan to dispose of a separate major line of business or geographical area of operations.

FOREIGN CURRENCY TRANSLATION

(i) Functional and presentation currency

Items included in the financial statements of each consolidated entity of the Company are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in Canadian dollars, which is the Company's functional and presentation currency.

The financial statements of subsidiaries that have a functional currency different from the presentation currency of the Company ("foreign operations") are translated into Canadian dollars as follows: assets and liabilities – at the closing rate at the date of the balance sheet; and, income and expenses – at the average rate of the period (as this is considered a reasonable approximation to actual rates). The accumulated gains or losses arising from translation of functional currencies to the presentation currency are included as a separate component of OCI within equity.

QIC Holdings ApS's (QIC), Qudos Insurance A/S ("Qudos") and CIM Re's functional currency is Danish Krone and is subject to foreign currency translation adjustments upon consolidation. Qudos primarily underwrites property and casualty insurance in the United Kingdom, Ireland, and Denmark. These are now part of Discontinued Operations, as noted above.

When an entity disposes of its entire interest in a foreign operation, or loses control, joint control, or significant influence over a foreign operation, the foreign currency gains or losses accumulated in OCI related to the foreign operation are recognized in the income statement. If an entity disposes of part of an interest in a foreign operation which remains a subsidiary, a proportionate amount of foreign currency gains or losses accumulated in OCI related to the subsidiary are reallocated between controlling and non-controlling interests.

(ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates in effect at the date the transactions occurred. Foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at period-end exchange rates of monetary assets and liabilities are recognized in investment income in the consolidated statements of income and comprehensive income. Exchange gains and losses related to non-monetary investments classified as available for sale (AFS) are recorded in OCI. Changes in the fair value of monetary securities denominated in foreign currency classified as available for sale are analyzed between translation differences resulting from changes in the amortized cost of the security and other changes in the carrying amount of the security. Translation differences related to changes in amortized cost are recognized in profit or loss, and other changes in carrying amount are recognized in OCI.

CASH AND SHORT-TERM DEPOSITS

Cash and short-term deposits include cash on hand, cash balances with banks and short-term investments. Short-term investments are defined as loans of less than one year to maturity at the time of acquisition. These financial assets are classified as loans and receivables and are recorded at an amortized cost which approximates fair value.

INVESTMENTS UNDER SECURITIES LENDING PROGRAM

Securities lending transactions are entered into on a collateralized basis. The securities lent are not derecognized on the consolidated balance sheet given that the risks and rewards of ownership are not transferred from the Company to the counterparties in the course of such transactions. Securities received from counterparties as collateral are not recorded on the consolidated balance sheet given that the risks and rewards of ownership are not transferred from the counterparties to the Company in the course of such transactions.

In the event that any loan made pursuant to the securities lending agreement is terminated and the loaned security, or any portion thereof, is not returned to the Company for any reason (including, without limitation, the insolvency or bankruptcy of the Borrower) within the time specified by the applicable Borrowing Agreement, the agent shall be jointly and severally liable, at its expense to:

(i) Promptly replace such security, or any portion thereof, not so returned with other securities of the same issuer, class, and denomination and with the same interest/dividend rights and other economic benefits as such, should the security have been returned; or,

(ii) If it is unable to purchase such security on the open market, the agent will credit Echelon in cash with the market value of such unreturned security, such market value to be determined as of the close of business on the date on which such security was required to be returned, including any future economic benefits that the company would have earned on holding the security.

FINANCIAL INSTRUMENTS

Financial assets and liabilities are recognized when the Company becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership.

Financial assets and liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

At initial recognition, the Company classifies its financial instruments in the following categories depending on the purpose for which the instruments were acquired:

(i) **Financial assets and liabilities at fair value through profit or loss (FVTPL):** A financial asset or liability is classified in this category if acquired principally for the purpose of selling or repurchasing in the short-term, or if it is designated at FVTPL by management. The Company has designated as FVTPL under the fair value option financial assets which contain embedded derivatives that significantly alter the cash flows of the underlying asset.

Financial instruments in this category are recognized initially and subsequently at fair value. Gains and losses arising from changes in fair value are presented in the consolidated statements of income and comprehensive income within investment income in the period in which they arise. The Company's investments in preferred shares are classified as FVTPL.

(ii) **Available-for-sale (AFS) investments:** Non-derivative financial assets that are either designated in this category or not classified in any of the other categories are AFS investments. The Company's AFS investments are comprised of marketable securities and investments in debt and common equity securities.

AFS investments are recognized initially at fair value plus transaction costs and are subsequently carried at fair value. Gains or losses arising from changes in fair value are recognized in OCI.

Interest on AFS investments, calculated using the effective interest method, is recognized in the consolidated statements of income and comprehensive income within investment income. Dividends on AFS equity instruments are recognized in the consolidated statements of income and comprehensive income as part of investment income when the Company's right to receive payment is established. When an AFS investment is sold or impaired, the accumulated gains or losses are moved from accumulated OCI to the consolidated statements of income and comprehensive income and included within investment income.

(iii) Loans and receivables: Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Company's loans and receivables are comprised of accounts receivables, due from insurance companies, and cash and short-term deposits. Loans and receivables are initially recognized at fair value plus transaction costs. Subsequently, loans and receivables are measured at amortized cost using the effective interest method less any provision for impairment.

(iv) Financial liabilities at amortized cost: Financial liabilities at amortized cost include accounts payable. Accounts payable are initially recognized at fair value. Subsequently, accounts payable are measured at amortized cost using the effective interest method.

IMPAIRMENT OF FINANCIAL ASSETS AND ACCRUED LIABILITIES

The Company determines, at each reporting date, whether there is objective evidence that financial assets and liabilities are impaired. The criteria used to determine if objective evidence of an impairment loss include:

(i) Significant financial difficulty of the obligor;

(ii) Delinquencies in interest, principal or dividend payments; and

(iii) it becomes probable that the borrower will enter bankruptcy or other financial reorganization.

For equity securities, a significant or prolonged decline in the fair value of the security below its cost is also evidence that the assets are impaired.

If such evidence exists, the Company recognizes an impairment loss, as follows:

AFS investments: The impairment loss is the difference between the amortized cost of the asset and its fair value at the measurement date, less any impairment losses previously recognized in the consolidated statements of income and comprehensive income. This amount represents the cumulative loss in accumulated OCI that is reclassified to the consolidated statements of income and comprehensive income.

Loans and receivables carried at amortized costs: The loss is the difference between the amortized cost of the loan and receivables and the present value of the estimated future cash flows, discounted using the instrument's original effective interest rate. The carrying amount of the asset is reduced by this amount either directly or indirectly through the use of an allowance account.

Impairment losses on financial assets and accrued liabilities carried at amortized cost are reversed in subsequent periods if the amount of the loss decreases or the fair value of financial assets and accrued liabilities carried at amortized cost increases and the decrease/increase can be related objectively to an event occurring after the impairment was recognized. In contrast, impairment losses on AFS equity instruments are not reversed.

INSURANCE CONTRACTS

Insurance contracts are those contracts that transfer significant insurance risk at the inception of the contract. Insurance risk arises when the Company agrees to compensate a policyholder if a specified uncertain future event adversely affects the policyholder. Significant risk is defined as the possibility of having to pay significantly more in a scenario where the insured event occurs than when it does not occur.

PROVISION FOR UNPAID CLAIMS

Provision for unpaid claims, including adjustment expenses, represents the estimated amounts required to settle all outstanding and unreported claims incurred to the end of the period. Unpaid claims liabilities are discounted to take into account the time value of money. It also includes a provision for adverse deviation. Expected reinsurance recoveries on unpaid claims and adjustment expenses, net of any required provision for doubtful amounts, are recognized as assets at the same time, using principles consistent with the Company's method for establishing the related liability.

STRUCTURED SETTLEMENTS

In the normal course of claims adjudication, the Company settles certain obligations to claimants through the purchase of annuities from third-party life insurance companies under structured settlement arrangements (structured settlements). In accordance with OSFI Guideline D-5, these contracts are categorized as either Type 1 or Type 2 based on the characteristics of the claim settlement. When the Company does not retain a reversionary interest under the contractual arrangement to any current or future benefits of the annuity, and the Company has obtained a legal release of the obligation from the claimant, it will be classified as a Type 1 structured settlement. For such contracts, any gain or loss arising on the purchase of an annuity is recognized in the consolidated statement of income at the date of purchase and the related claims liabilities are de-recognized. All other structured settlements that do not meet these criteria are classified as Type 2, with the Company recognizing the annuity contract in other investments within invested assets. A corresponding liability representing the outstanding obligation to the claimant is recognized in insurance contracts.

REINSURANCE

Reinsurance assets include the reinsurers' share of claims liabilities and unearned premiums. The Company reports third-party reinsurance balances on the consolidated balance sheets on a gross basis to indicate the extent of credit risk related to third-party reinsurance. The estimates for the reinsurers' share of claims liabilities are presented as an asset and are determined on a basis consistent with the related claims liabilities. Reinsurance assets are reviewed for impairment at each reporting date or more frequently when an indication of impairment arises during the reporting period.

REVENUE RECOGNITION

Premiums and unearned premiums

Insurance premiums written are deferred as unearned premiums and recorded in income as the premium is earned on a straight-line basis over the terms of the underlying policies, except on certain long-term policies for which premiums are earned using an actuarial risk assessment that matches claim expectations. The portion of the premiums related to the unexpired term of the policy at the end of the period is reflected in unearned premiums.

Ceded premiums and reinsurers' share of unearned premiums

The reinsurers' share of unearned premiums, net of a provision for doubtful amounts, is recognized as an asset at the same time and using principles consistent with the Company's method for determining the unearned premium liability.

DEFERRED POLICY ACQUISITION COSTS

Commissions, premium taxes and general expenses incurred in the writing of premiums are deferred only to the extent that they are expected to be recovered from unearned premiums and are amortized to income as the related premiums are earned. If unearned premiums are not sufficient to pay expected claims and expenses, including policy maintenance expenses and unamortized policy acquisition costs, a premium deficiency is said to exist. Premium deficiency is recognized by a charge to income initially by writing down deferred policy acquisition costs. If the premium deficiency is greater than the deferred policy acquisition costs, a liability would be accrued for the excess deficiency.

UNEARNED COMMISSION

Unearned commissions are based on ceded premiums with a coverage period beyond the current year-end. Unearned commissions are recognized as liabilities using principles consistent with the Company's method of determining policy acquisition costs.

PROPERTY AND EQUIPMENT

Property and equipment are recorded at cost less accumulated amortization and impairment. Amortization is provided over the estimated useful lives of the assets using the straight-line method over the following terms:

Furniture and equipment	3 years
Computer hardware	3 years

INTANGIBLE ASSETS

Intangible assets with finite useful lives, comprised primarily of computer software, are recorded at cost less accumulated amortization and impairment. Amortization is provided over the estimated useful life of the asset (2-3 years) using the straight-line method. Intangible assets with indefinite lives are recorded at lower of cost and recoverable amount.

IMPAIRMENT OF NON-FINANCIAL ASSETS

Property, plant and equipment and intangible assets are tested for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. For the purpose of measuring recoverable amounts, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units – or "CGUs"). Recoverable amount is the higher of an asset's fair value less costs to sell and value in use (being the present value of the expected future cash flows of the relevant asset or CGU, as determined by management).

The Company evaluates impairment losses, for potential reversals when events or circumstances warrant such consideration.

EMPLOYEE BENEFITS

The Company contributes to a group registered savings plan for employees as services are incurred. Contributions are charged to operating expenses. There are no other post-employment benefit expenses.

INCOME TAXES

Income taxes are recognized in the consolidated statements of income and comprehensive income except to the extent that it relates to items recognized in OCI or directly in equity. In those cases, the related taxes are also recognized in OCI or directly in equity, respectively.

Current income tax is based on the results of the operations, adjusted for items that are not taxable or not deductible, that is payable for the current year. Current income tax is calculated based on income tax laws and rates enacted or substantively enacted as at the balance sheet date.

The Company follows the asset and liability method of accounting for income taxes, whereby deferred income tax assets and liabilities are recognized for the future income tax consequences attributable to differences between the carrying values of existing assets and liabilities and their respective income tax bases and taxable losses and tax credit carry forwards. Deferred income tax assets and liabilities are measured using enacted or substantively enacted income tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in income tax rates on future income tax assets and liabilities is recognized in income or OCI or equity in the year which includes the date of enactment or substantive enactment. Deferred income tax assets are recognized only to the extent the realization of such assets is probable. Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income tax assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is intention to settle the balances on a net basis.

STOCK-BASED COMPENSATION

The Company has a Stock Option Plan that provides for the issuance of shares of the Company's common stock not exceeding 10% of the total issued and outstanding shares (on a diluted basis) and shares reserved for issuance under the employee stock option plans, options for services and employee stock purchase plans.

The Company utilizes the fair-value-based method of accounting for stock-based compensation. The fair value of stock-based compensation determined using an option pricing model, is recorded over the vesting period as a charge to net earnings with a corresponding credit to contributed surplus. Awards are equity-settled.

Stock options which contain a graded vesting feature (the total options granted vest on a graded basis such as annually over 5 years) are accounted for separately based on the date of vesting. At the time the options are granted, expected forfeiture rates are estimated and used to reduce the amount expensed over the life of the options. The estimated forfeiture rate is adjusted to actual forfeiture experience as information becomes available.

The Company has established a Share Unit Plan, under which the Board of Directors may from time to time determine (i) those eligible employees and directors (a "participant") who shall receive a grant of Restricted Share Units ("RSUs") and/or Performance Share Units ("PSUs") (RSUs and PSUs are collectively referred to as "Share Units"), (ii) the number of such RSUs and/or PSUs, and (iii) the grant date(s) applicable to such RSUs and/or PSUs. Compensation expense and the related liability are recorded equally over the vesting period, taking into account fluctuations in the market price of the Company's share price.

Each Share Unit granted under the Share Unit Plan will entitle the participant, upon satisfying all applicable vesting criteria, to receive one common share or a cash payment equal to the market value of such share, calculated based on the weighted average trading price per common share on the Toronto Stock Exchange for the 5 trading days prior to a fixed date. The grant of a Share Unit will not entitle the participant to exercise any voting rights, or exercise any other right which attaches to ownership of common shares.

Grant date fair value of each Share Unit is calculated based on the weighted average trading price per common share on the Toronto Stock Exchange for the 5 trading days prior to a fixed date. The fair value of the Share Unit is re-measured each period for subsequent changes in the market value of common shares.

Members of the Board, who are not otherwise employees of the Company or any affiliate and are not employed by a corporation that holds at least 100,000 Shares of the Corporation, are eligible to participate in a Deferred Share Unit Incentive Plan, which allows them to elect to defer all or a portion of their annual retainer received in the form of Deferred Share Units (DSUs), each of which is equivalent in value to one common share of the Company. The number of DSUs is established by dividing the amount of retainers not paid in cash by the weighted average trading price of the Common Shares for the last 5 trading days preceding the determination. Whenever cash dividends are paid on the common shares, the director's account under the DSU plan is credited with additional DSUs corresponding to the dividend paid on the common shares. The fair value of the DSUs is re-measured each period for subsequent changes in the market value of common shares.

PROVISIONS

Provisions are recognized as liabilities when the Company has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount can be reliably estimated. Provisions are measured at management's best estimate of the expenditure required to settle the obligation at the end of the reporting period, and are discounted to present value where the effect is material. The Company performs evaluations to identify onerous contracts and, where applicable, records provisions for such contracts.

SHARE CAPITAL

Incremental costs directly attributable to the issuance of shares are recognized as a deduction from equity. The cost method is used to account for the shares purchased under a normal course issuer bid with the average cost of the shares reducing share capital and any excess recorded as a deduction to retained earnings.

DIVIDENDS

Dividends on common shares are recognized in the Company's consolidated financial statements in the period in which the dividends are approved by the Board of Directors.

EARNINGS PER SHARE

Basic earnings per share ("EPS") are calculated by dividing the net income (loss) for the period attributable to shareholders of the Company by the weighted average number of common shares outstanding during the period. Diluted EPS is calculated by adjusting the weighted average number of common shares outstanding for dilutive instruments. The number of shares included with respect to options, and similar instruments is computed using the treasury stock method. The Company's potentially dilutive common shares comprise stock options, DSUs and RSUs granted to employees and directors.

STANDARDS, AMENDMENTS AND INTERPRETATIONS NOT YET ADOPTED OR EFFECTIVE

IFRS 9, Financial Instruments

In July 2014, the IASB published the complete version of IFRS 9 which is effective for annual periods beginning on or after January 1, 2018, with retrospective application. The new standard includes requirements on the classification and measurement of financial assets and liabilities, an expected credit loss model that replaces the existing incurred loss impairment model and new hedge accounting guidance. The Company has evaluated and meets the requirements to defer the adoption of IFRS 9 until the new insurance contracts standard is adopted effective January 1, 2021.

IFRS 15, Revenue from Contracts with Customers

IFRS 15, Revenue from contracts with customers deals with revenue recognition and establishes principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. The standard replaces IAS 18, 'Revenue' and IAS 11, 'Construction contracts' and related interpretations. The standard is effective for annual periods beginning on or after January 1, 2018. Revenue arising from insurance contracts and from financial instruments is outside the scope of IFRS 15. There are no other revenues arising from other sources of income.

IFRS 16, Leases

In January 2016, the IASB published IFRS 16 which is effective January 1, 2019. The new standard requires the capitalization of all leases by recognizing the present value of the lease payments and showing them as lease assets, and recognizing a financial liability representing an obligation to make future lease payments. The Company has evaluated the impact of IFRS 16 on its consolidated financial statements and the impact will be minimal.

IFRS 17, Insurance Contracts

In May 2017, the IASB published IFRS 17 which is effective January 1, 2021, with retrospective application. The standard replaces IFRS 4. The standard is comprehensive in scope and addresses recognition, measurement, presentation and disclosure for insurance contracts. The standard requires the entity to recognize a group of insurance contracts it issues from the earliest of the following: (a) the beginning of the coverage period of the group of contracts; (b) the date when the first payment from a policyholder in the group becomes due; and (c) for a group of onerous contracts, when the group becomes onerous. The measurement approach is based on the following building blocks: (i) a current, unbiased probability-weighted estimate of future cash flows expected to arise as the insurer fulfills the contract; (ii) the effect of the time value of money; (iii) a risk adjustment that measures the effects of uncertainty about the amount and timing of future cash flows; and (iv) a contractual service margin which represents the unearned profit in a contract (that is recognized in net earnings as the insurer fulfills its performance obligations under the contract). Estimates are required to be re-measured each reporting period. In addition, a simplified measurement approach is permitted for short-duration contracts in which the coverage period is approximately one year or less. The Company is currently evaluating the impacts of IFRS 17 on its consolidated financial statements.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The preparation of the Company's consolidated financial statements requires management to use estimates and judgements that affect the amounts reported in the financial statements. These estimates and judgements principally relate to the establishment of reserves for claims and expenses, impairments of investment securities, amounts recoverable from reinsurers and income taxes. As more information becomes known, these estimates and judgements could change and impact future results.

VALUATION OF PROVISIONS FOR UNPAID CLAIMS

Provision for unpaid claims are maintained to cover the Company's estimated ultimate liability for unpaid losses and loss adjustment expenses with respect to reported and unreported claims incurred as of the end of each accounting period. The provision for unpaid claims and adjustment expenses is first determined on a case-by-case basis as claims are reported and then reassessed as additional information becomes known. The provision also accounts for the future development of these claims, including claims incurred but not reported (IBNR). Provision for unpaid claims do not represent an exact calculation of liability, but instead represent estimates developed using projection techniques in accordance with Canadian accepted actuarial practice. These estimates are expectations of the ultimate cost of settlement and administration of claims based on the Company's assessment of facts and circumstances then known, its review of historical settlement patterns, estimates of trends in claims severity and frequency, legal theories of liability and other factors. The appointed actuary of the Company's subsidiaries, using appropriate actuarial techniques, evaluates the adequacy of the policy liabilities at the end of each reporting period.

Variables in the reserve estimation process can be affected by both internal and external events, such as changes in claims handling procedures, economic inflation, legal trends and legislative changes. Many of these items are not directly quantifiable, particularly on a prospective basis. Additionally, there may be significant reporting lags between the occurrence of the insured event and the time it is actually reported to the insurer. These estimates are refined in a systematic ongoing process as historical loss experience develops and additional claims are reported and settled. Because the establishment of reserves is an inherently uncertain process involving estimates, current reserves may not be sufficient. Adjustments to reserves, both positive and negative, are reflected in the consolidated statements of income and comprehensive income for the period in which such estimates are updated. Please see note 12.

VALUATION OF REINSURER'S SHARE OF PROVISION FOR UNPAID CLAIMS

Reinsurer's share of the provision for unpaid claims include amounts for expected recoveries related to provision for unpaid claims. Amounts recoverable from reinsurers are estimated in a manner consistent with claim and claim adjustment expense reserves. The ceding of an insurance liability to a reinsurer does not discharge the Company's primary liability to the policyholders. The Company's policy is to record an estimated allowance for doubtful accounts on the basis of periodic evaluations of balances due from reinsurers, reinsurer solvency, credit ratings of reinsurers, collateral held by the Company, management's experience and current economic conditions.

The Company is exposed to disputes on, and defects in, contracts with reinsurers and the possibility of default by reinsurers. Please see note 13.

VALUATION OF DEFERRED TAX ASSET

Deferred income taxes, accumulated as a result of temporary differences, which are probable to reverse, are included in the consolidated balance sheet. In addition, the consolidated statements of income and comprehensive income contains items that are non-taxable or non-deductible for income tax purposes, which cause the income tax provision to differ from what it would be if based on statutory rates. Recoverability of deferred tax assets is primarily based on current and expected profitability applicable to the Company and its ability to utilize any recorded tax assets taking into consideration tax planning strategies and the expiry date of tax losses. Please see note 16.

5 SEASONALITY

The P&C insurance business is seasonal in nature. While net earned premiums are generally stable from quarter to quarter, net underwriting income can be driven by weather conditions which may vary significantly by quarter.

(in thousands of Canadian dollars, except per share amounts)

6 INVESTMENTS

The following table provides a breakdown of the investment portfolio:

	Fair values	
Available-for-sale	**As at Dec. 31, 2017**	As at Dec. 31, 2016
Fixed income		
Canadian		
Federal	**39,408**	67,826
Provincial	**29,883**	44,147
Municipal	**14**	519
Corporate	**127,701**	136,984
	197,006	249,476
Fixed income lent through securities lending program		
Federal	**63,864**	15,390
Provincial	**17,564**	998
Municipal	**1,322**	845
Corporate	**8,535**	1,885
	91,285	19,118
Foreign fixed income		
Corporate	**2,014**	—
	2,014	—
Total fixed income	**290,305**	268,594
Commercial mortgage pooled funds	**—**	17,423
Money market pooled funds	**1,014**	200
Short-term fixed income and mortgage pooled funds	**19,303**	17,229
Specialty pooled fund	**8,240**	—
Total pooled funds	**28,557**	34,852
Common shares		
Canadian	**889**	312
U.S.	**8,428**	—
Total common shares	**9,317**	312
Total available-for-sale	**328,179**	303,758
Fair value through profit or loss		
Preferred shares	**42,754**	32,678
Preferred shares lent through securities lending program	**—**	99
Total preferred shares	**42,754**	32,777
Total investments	**370,933**	336,535
Cash and short-term deposits	**44,459**	50,588
Total investments including cash and short-term deposits	**415,392**	387,123

In accordance with the securities lending agreement, the amount of the collateral must be at least 105% of the fair value of the securities loaned. As at December 31, 2017, the Company had collateral of $98,798 (December 31, 2016 – $20,580) for the loaned securities or approximately 108% of the fair value of the loaned securities.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(in thousands of Canadian dollars, except per share amounts)

FAIR VALUE

The Company is responsible for determining the fair value of its investment portfolio by utilizing market-driven fair value measurements from active markets, where available, by considering other observable and unobservable inputs and by employing valuation techniques which make use of current market data. The technique employed has remained the same from December 31, 2016. The Company uses a fair-value hierarchy to categorize the inputs used in valuation techniques to measure fair value. A description of the inputs used in the valuation of financial instruments is as follows:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities. The fair value of the Company's common and preferred shares is determined based on quoted prices in active markets obtained from external pricing sources.

Level 2 – Inputs, other than quoted prices, that are observable for the investment either directly or indirectly. These inputs include quoted prices for similar instruments exchanged in active markets; quoted prices for identical or similar instruments exchanged in inactive markets; inputs other than quoted prices that are observable for the instruments, such as interest rates and yield curves, volatilities, prepayment speeds, loss severities, credit risks and default rates where available; and inputs that are derived principally from or corroborated by observable market data and correlation or other means.

The Company's investments in government securities (including federal, provincial and municipal bonds), corporate securities, commercial mortgage pooled funds, money market pooled funds and infrequently traded securities are priced using publicly traded, over-the-counter prices or broker-dealer quotes which are based on market observable inputs. Observable inputs such as benchmark yields, reported trades, broker dealer quotes, issuer spreads and bids are available for these investments.

Level 3 – Inputs that are not based on observable market data. Management is required to use assumptions regarding unobservable inputs as there is little, if any, market activity in these investments or related observable inputs that can be corroborated at the measurement date. Unobservable inputs require management to make certain projections and assumptions about the information that would be used by market participants in pricing assets. To verify pricing, the Company assesses the rationality of the fair values by comparing to industry-accepted valuation models, to movements in credit spreads and to recent transaction prices for similar assets where available.

The following table provides the classification of the Company's investments within the fair value hierarchy, as outlined above, as at December 31:

Dec. 31, 2017	**Level 1**	**Level 2**	**Level 3**	**Total**
Fixed income	**—**	**290,305**	**—**	**290,305**
Money market pooled funds	**—**	**1,014**	**—**	**1,014**
Short-term fixed income and mortgage pooled funds	**—**	**19,303**	**—**	**19,303**
Specialty pooled fund	**—**	**—**	**8,240**	**8,240**
Common Shares	**1,932**	**7,385**	**—**	**9,317**
Preferred Shares	**42,754**	**—**	**—**	**42,754**
	44,686	**318,007**	**8,240**	**370,933**

Dec. 31, 2016	Level 1	Level 2	Level 3	Total
Fixed income	—	268,594	—	268,594
Commercial mortgages pooled funds	—	17,423	—	17,423
Money market pooled funds	—	200	—	200
Short-term fixed income and mortgage pooled funds	—	17,229	—	17,229
Common Shares	312	—	—	312
Preferred Shares	32,777	—	—	32,777
	33,089	303,446	—	336,535

The Company's policy is to recognize transfers into and transfers out of fair value hierarchy levels as of the date of the event or change in circumstances that caused the transfer. There were no transfers from the existing portfolio for the year ended December 31, 2017 or 2016.

A new specialty pooled fund was added in the portfolio during the year ended December 31, 2017 which includes Level 3 private debt securities assets. The fund provides special situation financing solutions, generally in the form of senior or subordinated loans to both public and private companies. The fair value of the limited partnership investments is based on the net asset value ("NAV") provided by management of the limited partnership investments. For securities in the fund that are publicly traded, the fund uses the current available market prices provided the market price is reasonable taking into consideration both value and liquidity. Private securities in the fund are valued based upon the value of the underlying components. The loan component is valued by a discounted cash flow method taking into account current market interest rate spreads. The discount rate is determined to be the sum of the following components:

(in thousands of Canadian dollars, except per share amounts)

a) Benchmark yield – for Canadian loans, this is the on-the-run Government of Canada bond with equivalent duration to the loan. For U.S. loans, this is the on-the-run U.S. Treasury with equivalent duration to the loan.
b) Credit spread – this is the BBB index for equivalent duration to the loan.
c) Excess credit spread and Excess illiquidity spread – The excess credit spread and excess illiquidity spread are included so as to account for the additional risk and illiquidity of the loan compared to a comparable publicly traded bond.

Warrants and Gifted Equity make up a small proportion of the fund's valuation. Warrants are valued using a Black-Scholes model, with the implicit volatility of the warrants used in the calculation. This calculated implicit volatility is used for future warrant pricing. The gifted equity component is calculated using a combination of a modified discounted cash flow model and a normalized earnings-based enterprise value model.

Based on the unobservable nature of these NAVs, Echelon does not assess whether applying reasonably possible alternative assumptions would have an impact on the fair value of the limited partnership investments. The total unrealized gain on the fund for year ended December 31, 2017 was $101.

The following table summarizes the changes in the fair value measurement for financial instruments in Level 3 amount of the fair value hierarchy as at December 31, 2017:

Balance as at January 1, 2017	
Purchases	**8,139**
Sales	**—**
Realized gain (loss)	**—**
Change in unrealized gain (loss) in value of investment	**101**
Principal repayment	**—**
Balance as at December 31, 2017	**8,240**

The fair values of cash and short-term deposits, account receivables and financial liabilities, other than the provision for unpaid claims, approximate their carrying values due to their short-term nature.

The Company has interests in unconsolidated structured entities, through investments in pooled funds, which are included in investments on the balance sheets. These entities are not controlled by the Company. The carrying value of pooled funds and maximum exposure to loss as of December 31, 2017 was $28,557 (December 31, 2016 – $34,852). Investments in pooled funds consist of units invested in underlying money market and mortgage securities managed by third-party managers in addition to units invested in a Specialty Pooled Fund that provides special situation financing solutions, generally in the form of senior or subordinated loans to both public and private companies. The pooled funds are perpetual private trusts created under trust agreements. Financing is only provided to the pooled funds through the purchase of units and is therefore limited to the investment made.

IMPAIRED ASSETS AND PROVISIONS FOR LOSSES

A gross unrealized loss of $3,326 on AFS investments at December 31, 2017 (December 31, 2016 – $1,691) is recorded, net of tax, in the amount of $2,415 (December 31, 2016 – $1,231) in Accumulated Other Comprehensive Income primarily due to the impact of higher government bond yields on the Company's fixed income portfolio.

Management has reviewed currently available information regarding those financial assets where estimated fair values are less than amortized cost. For those investments that are considered impaired, the Company records the difference between the amortized cost of the financial assets and its fair value as an impairment which reduces investment income recorded in the period.

No impairments on AFS investments were recognized for the period ended December 31, 2017 and 2016.

INVESTMENT INCOME

The table below provides additional details on net investment income for year ending December 31:

	2017	2016
Interest income	**9,487**	10,597
Dividend income	**1,782**	1,771
Net realized (losses) gains	**(1,352)**	280
Fair value change on FVTPL investments	**3,503**	3,870
Realized and unrealized foreign exchange gains	**4,629**	855
Investment expenses	**(853)**	(866)
Investment income	**17,196**	16,507

7 LOAN RECEIVABLE

As part of the sale of its European operations, the Company entered into a loan agreement with New Nordic Odin Guernsey Limited (NNGL) on March 7, 2017 to lend the principal amount of 91.5 million Danish Krone (DKK) payable on December 31, 2017.

On December 29, 2017, the Company received 59.4 million DKK as partial repayment of the principal amount of the loan. The Company extended the maturity date for the outstanding balance of the loan with NNGL to March 31, 2018.

The loan bears interest on the principal amount outstanding at the rate of six percent (6%) per annum that commenced on July 6, 2017 and is payable monthly. The Company has received all interest payments due to date.

Please refer to note 27 for further details.

(in thousands of Canadian dollars, except per share amounts)

8 DERIVATIVE FINANCIAL INSTRUMENTS

The Company has entered into derivative contract with a major Canadian bank to hedge the principal repayment from the loan receivable from New Nordic Odin Guernsey Limited. The total notional value of the derivative contracts at December 31, 2017 is $6.6 million (December 31, 2016 – $18.0 million). Contracts are classified as Level 2 under the fair value hierarchy:

9 LINE OF CREDIT

The Company had a $10.0 million two-year secured revolving term credit facility effective June 30, 2015, which matured on July 1, 2017. The facility expired and has not been renewed.

For the year ended December 31, 2017, the Company has expensed $0.2 million on the income statement, related to the maintenance of the credit facility (December 31, 2016 – $0.2 million).

10 DEFERRED POLICY ACQUISITION COSTS (DPAC)

Commissions, premium taxes and general expenses incurred in the writing of premiums are deferred in accordance with the Accounting Policy set out in note 3.

A reconciliation of DPAC is shown below as at December 31:

	2017		2016	
	Gross	**Ceded**	Gross	Ceded
Balance at the beginning of the year	**30,689**	**2,288**	77,456	23,689
Acquisition costs during the year	**68,258**	**5,444**	52,998	6,006
Amortization of acquisition costs during the year	**(58,059)**	**(6,065**	(47,227)	(5,682)
Discontinued operations (note 27)	**—**	**—**	(52,538)	(21,725)
Acquisition costs deferred at end of the year	**40,888**	**1,667**	30,689	2,288

11 UNEARNED PREMIUMS

The following table shows unearned premiums by line of business and nature of risk as at December 31:

	2017		2016	
	Gross	**Ceded**	Gross	Ceded
Automobile				
– accident benefits	**18,122**	**562**	15,799	929
– liability	**52,882**	**2,758**	33,942	1,082
– other	**31,393**	**587**	22,448	555
Property				
– commercial	**8,732**	**538**	5,671	553
– personal	**42,395**	**4,650**	36,381	4,724
Liability	**3,607**	**103**	3,521	118
Accident and sickness	**116**	**—**	86	—
Surety	**2,812**	**538**	1,949	890
Other	**518**	**221**	387	124
	160,577	**9,957**	120,184	8,975

A reconciliation of unearned premium is shown below as at December 31:

	2017		2016	
	Gross	**Ceded**	Gross	Ceded
Unearned premium at the beginning of the year	**120,184**	**8,975**	264,584	89,953
Premium written and ceded during the year	**285,718**	**18,911**	217,486	17,885
Premium earned in income	**(245,325)**	**(17,929)**	(198,148)	(17,088)
Discontinued operations (note 27)	**—**	**—**	(163,738)	(81,775)
Unearned premium at the end of the year	**160,577**	**9,957**	120,184	8,975

(in thousands of Canadian dollars, except per share amounts)

12 PROVISION FOR UNPAID CLAIMS

The fair value of the provision for unpaid claims approximates the carrying value determined in accordance with generally accepted actuarial methods in Canada, which discounts future cash flows and includes a margin for adverse deviation.

The Company determines the discount rate based on the expected return on its investment portfolio of assets with appropriate assumptions for interest rates relating to reinvestment of maturing investments. The investment portfolio has experienced an increase in yields compared to December 31, 2016. The Company discounts its best estimate as follows for each entity, which is for all lines of business within the reporting entity:

Entity	**Dec. 31, 2017**	Dec. 31, 2016
Echelon Insurance	**2.65%**	1.90%
ICPEI	**2.80%**	1.75%

The Company recorded a $25,745 reduction to the net provision for unpaid claims relating to redundancies in prior years' estimates (December 31, 2016 – $17,409).

To recognize the uncertainty in establishing these best estimates, to allow for possible deterioration in experience, and to provide greater comfort that the actuarial liabilities are adequate to pay future claims, the Company includes provisions for adverse deviations (PFADs) in some assumptions relating to claims development, reinsurance recoveries and future investment income. The PFADs selected are in the mid-range of those recommended by the Canadian Institute of Actuaries. The aggregate impact of the provision for adverse deviation is to increase the provision for unpaid claims on a net basis by $19,349 as at December 31, 2017 (December 31, 2016 – $21,388).

The provision for unpaid claims on an actuarial present value (APV) gross and ceded basis by line of business is shown below as at December 31:

	2017		2016	
	Gross	**Ceded**	Gross	Ceded
Automobile				
– accident benefits	**94,675**	**14,135**	95,810	16,334
– liability	**120,762**	**6,715**	113,334	7,897
– other	**11,061**	**209**	6,474	86
Property				
– commercial	**5,508**	**611**	4,928	951
– personal	**10,051**	**620**	9,155	989
Liability	**18,051**	**563**	23,063	362
Accident and sickness	**1,182**	**318**	1,858	381
Commercial Auto	**75**	**—**	53	10
Surety	**1,361**	**300**	211	—
Other	**240**	**—**	243	13
Total unpaid claims	**262,966**	**23,471**	255,129	27,023

CLAIMS DEVELOPMENT

Provision for unpaid claims analysis	**Dec. 31, 2017**	Dec. 31, 2016
Unpaid claims, beginning of year, net	**228,106**	231,626
Favourable prior year claims development	**(25,745)**	(17,409)
Provision for claims occurring in current period	**179,305**	132,417
Paid on claims occurring during		
Current year	**(79,120)**	(56,356)
Prior year	**(63,051)**	(62,172)
Unpaid claims, end of period, net	**239,495**	228,106
Reinsurers' share	**23,471**	27,023
Gross unpaid claims	**262,966**	255,129

The development of insurance liabilities provides a measure of the Company's ability to estimate the ultimate value of claims.

(in thousands of Canadian dollars, except per share amounts)

Assumptions used to develop the provision estimate for unpaid claims and adjustment expenses are selected by class of business and geographic location. Consideration is given to the characteristics of the risks, historical trends, and the amount of data available on individual claims, inflation and any other pertinent factors. Some assumptions require a significant amount of judgement such as the expected impacts of future judicial decisions and government legislation. The diversity of these considerations results in it not being practical to identify and quantify all individual assumptions that are more likely than others to have a significant impact on the measurement of the Company's insurance contracts. There were no new assumptions identified in the period as having a potential or identifiable material impact on the overall claims estimate.

The following tables show the estimates of cumulative incurred claims, including IBNR, with subsequent developments during the periods and together with cumulative payments to date. The original reserve estimates are evaluated quarterly for redundancy or deficiency. The evaluation is based on actual payments in full or partial settlement of claims and current estimates of claims liabilities for claims still unreported.

CLAIMS DEVELOPMENT TABLE, GROSS OF REINSURANCE

										Calendar Year	
	2007 & prior	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**
Provision for claims including LAE	169,091	185,255	207,220	239,036	254,519	268,580	296,856	344,692	397,214	255,129	262,966
Reserve re-estimate as of:											
1 year later	163,465	186,446	203,920	232,472	246,972	269,499	284,934	326,083	377,570	226,304	
2 years later	162,916	189,093	201,044	239,117	245,331	252,279	276,565	295,495	355,738		
3 years later	164,290	186,429	206,039	239,338	232,772	250,266	263,289	279,364			
4 years later	161,852	190,342	205,646	228,612	230,271	244,385	252,880				
5 years later	163,440	189,297	197,841	228,628	229,741	239,541					
6 years later	163,069	183,341	199,637	230,487	224,747						
7 years later	159,402	187,392	201,049	228,676							
8 years later	163,480	189,298	200,155								
9 years later	165,003	189,141									
10 years later	165,200										
Cumulative favourable (unfavourable) development	3,891	(3,886)	7,065	10,360	29,772	29,039	43,976	65,328	41,476	28,825	

CLAIMS DEVELOPMENT TABLE, NET OF REINSURANCE

										Calendar Year	
	2007 & prior	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**
Provision for claims including LAE	120,630	143,354	168,484	202,884	221,250	238,297	264,094	295,955	307,055	228,106	239,495
Reserve re-estimate as of:											
1 year later	115,530	142,641	164,393	196,517	215,191	233,517	252,748	277,943	289,646	202,361	
2 years later	112,960	143,980	162,651	203,632	214,128	225,958	245,568	252,548	270,587		
3 years later	112,595	142,924	166,901	203,367	204,365	220,530	234,335	239,444			
4 years later	111,267	144,486	166,300	195,502	197,028	215,901	226,229				
5 years later	110,883	143,125	160,078	192,120	196,751	212,212					
6 years later	110,001	138,578	159,189	193,183	192,517						
7 years later	107,439	139,649	160,168	191,391							
8 years later	108,297	140,793	159,227								
9 years later	109,209	140,470									
10 years later	109,133										
Cumulative favourable (unfavourable) development	11,497	2,884	9,257	11,493	28,733	26,085	37,865	56,511	36,468	25,745	

The provision for unpaid claims relating to the International division, which is discontinued operations, was treated as paid in the development table above.

(in thousands of Canadian dollars, except per share amounts)

13 UNDERWRITING POLICY AND REINSURANCE CEDED

In the normal course of business, the Company seeks to reduce the loss that may arise from catastrophes or other large loss events by purchasing reinsurance to share all or part of the insurance risks originally accepted by the Company in writing premiums. This does not relieve the Company of its primary obligation to policyholders.

During 2017, the Company followed the policy of underwriting and reinsuring contracts of insurance, which limits the net exposure of the Company to a maximum amount on any one loss to $2,000 (2016 – $2,000). In addition, the Company obtained catastrophe reinsurance which limits the loss from a series of claims arising from a single occurrence to $2,000 (2016 – $2,000), to a maximum coverage of $88,000 (2016 – $58,000).

The Company places all its automobile reinsurance with registered reinsurers. There are non-registered reinsurers participating in the specialty property and casualty program business. The Company has access to trust funds that, in the Company's judgement, are adequate to secure the liabilities that the Company has ceded to non-registered reinsurers.

Failure of reinsurers to honour their obligations could result in losses to the Company. Consequently, the Company continually evaluates the financial condition of its reinsurers and monitors concentrations of credit risk to minimize its exposure to significant losses. There have been no defaults and no provision made in the accounts for defaults based on management's review of the creditworthiness of its reinsurers.

REINSURANCE RECOVERABLE

The following tables summarize the balances outstanding from reinsurers, by risk rating, as at December 31:

Dec. 31, 2017

Credit rating	Gross reinsurance recoverable	Less: Deposits held in trust	Net exposure
A or higher	**32,582**	**—**	**32,582**
Not rated	**1,355**	**1,221**	**134**
	33,937	**1,221**	**32,716**

Dec. 31, 2016

Credit rating	Gross reinsurance recoverable	Less: Deposits held in trust	Net exposure
A or higher	36,329	—	36,329
Not rated	1,256	1,263	—
	37,585	1,263	36,329

Included in gross reinsurance recoverable is reinsurers' share of unearned premiums of $9,957 (December 31, 2016 – $8,975), reinsurers' share of provision for unpaid claims of $23,471 (December 31, 2016 – $27,023), and receivables from reinsurers presented as due from insurance companies of $510 (December 31, 2016 – $1,587). No balances due from reinsurers are considered past due as at December 31, 2017 and 2016. There is no valuation allowance or amounts written off during the years ended December 31, 2017 and 2016.

14 RISK MANAGEMENT

As a provider of insurance products, effective risk management is fundamental to the Company's ability to protect the interests of its customers and shareholders. The Company is exposed to risks of loss pertaining to insurance products. These include risks surrounding product and pricing, underwriting and claims, catastrophic exposure, and matching of assets and liabilities. The Company is also exposed to potential loss from various risks, including interest rate risk, equity market fluctuation risk, credit risk, liquidity risk, and foreign exchange risk.

The Company has written principles for overall risk management, as well as written policies covering specific areas such as underwriting, reinsurance, foreign exchange risk, interest rate risk, credit risk, use of derivative financial instruments and non–derivative financial instruments, and investment of excess liquidity.

INSURANCE RISK

The risk under any one insurance contract is the possibility that the event occurs and the uncertainty of the amount of the resulting claim. By the very nature of an insurance contract, the risk is random and therefore unpredictable. The principal risk that the Company faces under its insurance contract is that the actual claims payments exceed the carrying amount of the insurance liabilities. This could occur because the frequency or the severity of the claims is greater than estimated. Insurance events are random and the actual number and amount of claims will vary from year to year from the estimate.

Direct Written Premium	Dec. 31, 2017	Dec. 31, 2016
Lines		
Personal Lines	**66%**	71%
Commercial Lines	**34%**	29%
Regions		
Ontario	**46%**	47%
Atlantic Canada	**18%**	22%
Quebec	**21%**	12%
Western Canada	**15%**	19%

(in thousands of Canadian dollars, except per share amounts)

SENSITIVITY TO INSURANCE RISK

The table below shows the sensitivity of earnings from operations before income taxes and total equity after giving effect to a one percentage point increase in the loss ratio and claims settlement costs. The loss ratio is regarded as a non-IFRS measure and is calculated by the Company with respect to its ongoing insurance operations as losses on claims incurred (including losses and loss adjustment expenses) expressed as a percentage of net premiums earned. Such an increase could arise from higher frequency of losses, increased severity of losses, or from a combination of both. The sensitivity analysis presented below does not consider the probability of such losses to loss frequency or severity occurring or any non-linear effects of reinsurance and, as a result, each additional percentage point increase in the loss ratio would result in a linear impact on earnings from operations before income taxes and total equity.

	December 31, 2017		December 31, 2016	
Sensitivity Factor	**Net income before income taxes**	**Shareholders' equity**	Net income before income taxes	Shareholders' equity
Increase of 1% to loss ratio	**(2,274)**	**(1,660)**	(1,811)	(1,322)
Increase of 1% to claims settlement costs	**(2,395)**	**(1,748)**	(2,281)	(1,665)

PRODUCT AND PRICING

The Company prices its products taking into account numerous factors, including claims frequency and severity trends, product line expense ratios, special risk factors, the capital required to support the product line, and the investment income earned on that capital. The Company's pricing process is designed to ensure an appropriate return on capital and long-term rate stability avoiding wide fluctuations in rates, unless necessary. These factors are reviewed and adjusted periodically to ensure they reflect the current environment.

Pricing for automobile insurance must be submitted to each provincial government regulator and, in certain provinces, pre-approved by the regulator. Regulatory decisions may impede automobile rate increases or other actions that the Company may wish to take. Also, during periods of intense competition for any product line, to gain market share, the Company's competitors may price their products below the rates the Company considers acceptable. Although the Company may adjust its pricing up or down to maintain a competitive position, the Company strives to ensure its pricing will produce an appropriate return on invested capital. There is no assurance that the Company will not lose market share during periods of pricing competition.

UNDERWRITING AND CLAIMS

The Company is exposed to loss resulting from the underwriting of risks being insured and the exposure to financial loss resulting from greater than anticipated adjudication, settlement and claims costs.

The Company's underwriting objectives are to develop business within target markets on a prudent and diversified basis and to achieve profitable underwriting results. The Company underwrites automobile business after a review of the applicant's driving record and claims experience. Specialty commercial and personal risks are selected by the Company, working with its external brokers, after consideration of various risk factors associated with these lines of business. Despite its best efforts, and consideration of all known risk factors, there can be no assurance that all risks associated with the insurance policies that it writes can be identified and assessed, and the Company may, therefore, experience increased adjudication, settlement and claims costs.

The Company estimates its claims reserves on a quarterly basis and this is supported by quarterly assessments by the independent appointed actuary. Every quarter, for each line of business, the Company compares actual and expected claims development. To the extent that actual results differ from expected development, assumptions are re-evaluated and new estimates are derived. Although the Company believes its overall provision levels to be adequate to satisfy its obligations under existing policies, actual losses may deviate, perhaps substantially, from the amounts reflected in the Company's consolidated financial statements. To the extent provisions prove to be inadequate, the Company would have to re-evaluate such provisions and may incur a charge to earnings in the future.

UNPREDICTABLE CATASTROPHIC EVENTS

Catastrophes can be caused by various natural and unnatural events. Natural catastrophic events include hurricanes, windstorms, earthquakes, hailstorms, explosions, severe winter weather and fires. Unnatural catastrophic events include hostilities, terrorist acts, riots, crashes and derailments. The incidence and severity of catastrophes are inherently unpredictable. The extent of losses from a catastrophe is a function of both the total amount of insured exposure in the area affected by the event and the severity of the event. Most catastrophes are restricted to small geographic areas; however, hurricanes, windstorms and earthquakes may produce significant damage in large, heavily populated areas.

Catastrophes can cause losses in a variety of business lines. Claims resulting from natural or unnatural catastrophic events could cause substantial volatility in the Company's financial results and could materially reduce the Company's profitability or harm the Company's financial condition. The Company manages the impact of losses which may result from catastrophic events by purchasing excess of loss and catastrophe reinsurance to share all or part of the insurance risks originally accepted by the Company as well as geographic diversification.

(in thousands of Canadian dollars, except per share amounts)

ASSET AND LIABILITY MATCHING

The Company is exposed to:

- changes in the value of its fixed income investments and policy liabilities to the extent that market interest rates change;
- equity price fluctuations, which affect the fair values of equities held by the Company;
- the risk of losses to the extent that the sale of an investment prior to its maturity is required to provide liquidity to satisfy policyholder and other cash outflows;
- the risk that future inflation of policyholder cash flows exceed returns on long-term investments; and
- foreign exchange risks with respect to investments, derivatives, receivables and policy liabilities denominated in foreign currencies.

The Company's exposures are monitored on a regular basis and actions are taken to balance investment positions when approved risk tolerance limits are exceeded.

Risk management is carried out by the Audit and Risk Committee under policies approved by the Board of Directors.

MARKET RISK

Market risk is the risk of loss arising from adverse changes in market rates and prices, such as interest rates, equity market fluctuations, foreign exchange rates and other relevant market rate or price changes. Market risk is directly influenced by the volatility and liquidity in the markets in which the related underlying financial assets are traded. Below is a discussion of the Company's primary market risk exposures and how these exposures are currently managed.

INTEREST RATE RISK

Fluctuations in interest rates have a direct impact on the fair valuation and future cash flow of the Company's fixed income investment portfolio. Generally, the Company's investment income will be reduced during sustained periods of lower interest rates as higher yielding fixed income investments mature or are sold and the proceeds are reinvested at lower rates. During periods of rising interest rates, the fair value of the Company's existing fixed income investments will generally decrease and gains on fixed income securities will likely be reduced.

The sensitivity analysis for interest rate risk as set out in the table below illustrates the impact of changes in interest rates on OCI relating to the fixed income investment portfolio as at December 31, based on parallel 200 basis point shifts in interest rates up and down in 100 basis point increments.

Change in interest rates	**Fair value of fixed income**	**Hypothetical change on fair value**	**Effect on OCI net of tax**
As at Dec. 31, 2017			
200 basis point rise	**274,558**	**(5)%**	**(11,495)**
100 basis point rise	**282,357**	**(3)%**	**(5,802)**
No change	**290,305**	**—**	**—**
100 basis point decline	**298,253**	**3%**	**5,801**
200 basis point decline	**306,053**	**5%**	**11,497**

Change in interest rates	Fair value of fixed income	Hypothetical change on fair value	Effect on OCI net of tax
As at Dec. 31, 2016			
200 basis point rise	252,340	(6)%	(11,865)
100 basis point rise	260,468	(3)%	(5,932)
No change	268,594	—	—
100 basis point decline	276,722	3%	5,931
200 basis point decline	284,850	6%	11,863

As discussed in note 11, the discount rate used in the determination of the provision for unpaid claims is based on the expected return of assets on its investment portfolio with appropriate assumptions for interest rates relating to reinvestment of maturing investments. Fluctuations in market interest rates will therefore have an impact on the discount rate used in the valuation of the net provision for unpaid claims. The table below shows the potential impact of interest rate fluctuations on the net provision for unpaid claims and income statement:

Change in discount rate	**Net provision for unpaid claims**	**Hypothetical change in value**	**Effect on net income net of tax**
As at Dec. 31, 2017			
100 basis point rise	**234,437**	**(2)%**	**(3,692)**
No change	**239,495**	**—**	**—**
100 basis point decline	**244,807**	**2%**	**3,878**
As at Dec. 31, 2016			
100 basis point rise	223,441	(2)%	(3,405)
No change	228,106	—	—
100 basis point decline	233,024	2%	3,590

(in thousands of Canadian dollars, except per share amounts)

LIQUIDITY RISK

Liquidity risk is the risk that the Company may not have sufficient liquid financial resources to meet its obligations when they fall due, or would have to incur excessive costs to do so. The Company's liquidity management strategy is to ensure that there is sufficient cash to meet its financial commitments as they become due. To manage cash flow requirements, the Company maintains a portion of invested assets in liquid investments.

The maturity profile of bonds are as follows, as at December 31:

Dec. 31, 2017	**Less than 1 year**	**1 – 3 years**	**3 – 5 years**	**Greater than 5 years**	**Total**
Bonds	**24,001**	**117,230**	**84,152**	**64,922**	**290,305**
Percentage of total	**8%**	**41%**	**29%**	**22%**	**100%**
Dec. 31, 2016	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Bonds	18,190	76,090	100,469	73,845	268,594
Percentage of total	7%	28%	37%	28%	100%

The following tables summarize the expected timing of cash flows arising from insurance obligations, on an undiscounted basis, as at December 31:

Dec. 31, 2017	**Less than 1 year**	**1 – 3 years**	**3 – 5 years**	**Greater than 5 years**	**Total**
Actuarial liabilities (undiscounted)	**93,874**	**89,302**	**46,779**	**25,803**	**255,758**
Less: Reinsurance recoverable (undiscounted)	**10,877**	**7,758**	**2,661**	**1,464**	**22,760**
Net actuarial liabilities	**82,997**	**81,544**	**44,118**	**24,339**	**232,998**
Dec. 31, 2016	Less than 1 year	1 – 3 years	3 – 5 years	Greater than 5 years	Total
Actuarial liabilities (undiscounted)	86,700	87,875	43,864	24,008	242,447
Less: Reinsurance recoverable (undiscounted)	9,251	8,928	3,608	4,660	26,447
Net actuarial liabilities	77,449	78,947	40,256	19,348	216,000

All other financial assets and liabilities are for duration of one year or less. The contractual maturities for lease commitments are listed in note 21.

EQUITY PRICE RISK

Fluctuations in the value of equity investments affect the level and timing of recognition of gains and losses on securities held, and cause changes in realized and unrealized gains and losses. General economic conditions, political conditions and many other factors can also adversely affect the stock and bond markets and, consequently, the value of the equity and fixed income investments held.

The Company has policies to limit and monitor its exposure to individual issuers and classes of issuers of equity securities.

The table below summarizes the potential impact of a 10% change in the value of the equity securities (common and preferred shares) on net income and OCI for the twelve months ended December 31, 2017, and the year ended December 31, 2016. Certain shortcomings are inherent in the method of analysis presented, as the analysis is based on the assumption that all equity holdings increased/decreased by 10% with all other variables held constant.

Change in equity holdings	**Effect on net income (loss) net of tax**		**Effect on OCI net of tax**	
	Dec. 31, 2017	Dec. 31, 2016	**Dec. 31, 2017**	Dec. 31, 2016
10% rise	**3,121**	2,393	**680**	23
10% decline	**(3,121)**	(2,393)	**(680)**	(23)

CREDIT RISK

The Company is exposed to credit risk principally through its investment securities and balances receivable from policyholders and reinsurers. The Company has policies to limit and monitor its exposure to individual issuers and classes of issuers of investment securities which do not carry the guarantee of a national or Canadian provincial government. The Company's credit exposure to any one individual policyholder is not material. The Company has policies that limit its exposure to individual reinsurers and regular review processes to assess the creditworthiness of reinsurers with whom it transacts business.

The Company's maximum exposure to credit risk, without taking into account amounts held as collateral, is:

	As at Dec. 31, 2017	As at Dec. 31, 2016
Bonds	**290,305**	268,594
Gross reinsurance recoverable	**32,582**	36,329
Accounts receivable	**75,622**	46,705
Structured settlements (note 22)	**36,472**	32,729
Cash	**44,459**	50,588
Total	**479,440**	434,945

(in thousands of Canadian dollars, except per share amounts)

Echelon has entered into FX contract for its European subsidiary balance sales proceeds hedging. The FX contract is with Royal Bank of Canada, a Canadian multinational financial services company and the largest bank in Canada. The total notional value of the derivative contracts is $6.6 million.

The following table sets forth the Company's fixed income securities portfolio by credit quality as at December 31:

FIXED INCOME PORTFOLIO

A breakdown of the fixed income portfolio by credit rating is shown below:

	As at Dec. 31, 2017		As at Dec. 31, 2016	
	Fair value	**%**	Fair value	%
AAA	**125,595**	**43%**	107,267	40%
AA	**50,040**	**17%**	52,728	20%
A	**81,816**	**28%**	67,360	25%
BBB	**28,156**	**10%**	41,239	15%
BB	**1,420**	**1%**	—	—
B	**1,741**	**1%**	—	—
CCC	**184**	**—**	—	—
Unrated	**1,353**	**—**	—	—
Total	**290,305**	**100%**	268,594	100%

PREFERRED SHARE PORTFOLIO

A breakdown of the preferred shares portfolio by credit rating is shown below:

	As at Dec. 31, 2017		As at Dec. 31, 2016	
	Fair value	**%**	Fair value	%
P2	**36,335**	**85%**	29,600	90%
P3	**6,419**	**15%**	3,177	10%
Total	**42,754**	**100%**	32,777	100%

CAPITAL MANAGEMENT

Capital is comprised of the Company's total equity. As at December 31, 2017, the Company's equity was $142,822 (December 31, 2016 – $137,414).

The Company's objectives when managing capital consists of:

- Maintaining capital to be above minimum regulatory levels;
- Ensuring capital is above internally determined risk management levels;
- Maintaining creditworthiness, financial strength and protect its claims paying abilities; and
- Maximizing returns to shareholders over the long term.

15 INTANGIBLE ASSETS

A reconciliation of the movement in Intangible Assets is shown below, as at December 31:

	Opening cost	**Additions**	**Disposals**	**End of period cost**	**Accumulated amortization**	**Net**
Software						
December 31, 2017	**28,712**	**4,498**	**—**	**33,210**	**25,573**	**7,637**
December 31, 2016	23,014	5,698	—	28,712	20,915	7,797
Goodwill						
December 31, 2017	**400**	**—**	**—**	**400**	**—**	**400**
December 31, 2016	400	—	—	400	—	400
Total intangible assets						
December 31, 2017	**29,112**	**4,498**	**—**	**33,610**	**25,573**	**8,037**
December 31, 2016	23,414	5,698	—	29,112	20,915	8,197

(in thousands of Canadian dollars, except per share amounts)

16 INCOME TAXES

The income tax is as follows for year ending December 31:

	2017	2016
Current	**921**	1,738
Deferred	**26**	(68)
	947	1,670

The effective income tax rates are different from the combined federal and provincial income tax rates.

The consolidated statements of income and comprehensive income contain items that are non-taxable or non-deductible for income tax purposes, which cause the income tax expense to differ from what it would have been if based on statutory rates.

The difference is broken down as follows for year ending December 31:

	2017	2016
Income tax expense calculated at statutory rates	**27.0%**	27.0%
Increase (decrease) in income tax rates resulting from:		
Non-taxable dividend income	**(6.3)%**	(6.1)%
Non-taxable (income) loss	**—**	(5.7)%
Non-deductible expenses	**1.8%**	2.7%
Tax benefit of losses not previously recognized	**—**	(0.1)%
Tax benefit of losses recognized	**(8.7)%**	0.8%
Statutory rate differences	**2.4%**	1.1%
Non-taxable portion of capital gains	**(6.0)%**	(1.8)%
Other	**2.3%**	1.1%
Effective income tax rate	**12.5%**	19.1%

Deferred income taxes are comprised of the following as at December 31:

	Losses carried forward	Reserves	Investments	Property, equipment and intangible assets	Total
Balance – January 1, 2017	**355**	**4,689**	**(25)**	**841**	**5,860**
Amounts recorded in the income statement	**(226)**	**(9)**	**2**	**207**	**(26)**
Balance – December 31, 2017	**129**	**4,680**	**(23)**	**1,048**	**5,834**

	Losses carried forward	Reserves	Investments	Property, equipment and intangible assets	Total
Balance – January 1, 2016	1,146	4,758	(32)	568	6,440
Amounts recorded in discontinued operations	7,904	(131)	—	—	7,773
Amounts recorded in the income statement	(274)	62	7	273	68
Write-off	(8,421)	—	—	—	(8,421)
Balance – December 31, 2016	355	4,689	(25)	841	5,860

Management reviews the recoverability of the deferred income tax asset on an ongoing basis and adjusts, as necessary, to reflect its anticipated realization. Management expects that the recorded deferred income tax asset will be realized in the normal course of operations.

The Company has tax losses available resulting from capital losses of $54,048 for which no deferred tax assets have been set up. These capital losses have no expiry date.

INCOME TAXES INCLUDED IN OCI

The amounts included in the consolidated statements of comprehensive income are shown net of the following tax benefit, for the years ended December 31:

	2017	2016
Change in unrealized gains	**(753)**	739
Reclassification to net income of (gains) and losses	**(460)**	(1,030)
Total income tax expense included in OCI	**(1,213)**	(291)

Income taxes payable are expected to be settled within one year of the financial statement date.

(in thousands of Canadian dollars, except per share amounts)

17 SHARE CAPITAL

	As at Dec. 31, 2017	As at Dec. 31, 2016
Authorized		
Unlimited common shares (no par value)		
Unlimited special shares issuable in Series (no par value)		
Issued		
11,891,076 common shares (December 31, 2016 – 11,747,736 common shares)	**71,520**	70,227

In 2017, 63,006 common shares (2016 – 52,600) with a value of $1,293 (2016 – $866) were issued for the exercise of stock options. In 2017, 80,334 common shares (2016 – 21,891) were issued pursuant to the Share Unit Plan for eligible employees. During 2017, nil shares were repurchased under the normal course issuer bid and subsequently cancelled (2016 – 55,867 shares or $676).

18 EMPLOYEE STOCK OPTION PLAN

For the year ended December 31, 2017, the Company recorded a compensation expense of $73 (2016 – $56), with an offsetting credit to contributed surplus in relation to its stock option plan. Stock options granted have varying vesting periods. It also recorded an expense of $899 (2016 – $344) in relation to its Share Unit Plan and Options.

The following is a continuity schedule of stock options outstanding as at December 31.

	Number of options		Weighted average exercise price per share	
	2017	2016	**2017**	2016
Outstanding, beginning of year	**202,350**	309,325	**8.27**	8.15
Granted during year	**299,308**	—	**12.9**	—
Exercised during year	**(87,350)**	(52,600)	**7.77**	7.71
Canceled during year	**(12,000)**	(39,750)	**8.89**	8.24
Expired during year	**(2,000)**	(14,625)	**7.19**	7.80
Outstanding, end of year	**400,308**	202,350	**11.83**	8.27

The outstanding stock options consist of the following, as at December 31, 2017:

Stock Option price per share	Number	Average remaining contractual life	Number of options exercisable
$8.90-13.16	284,683	7.5	—
$8.01-$8.89	92,625	2.25	92,625
$7.18-$8.00	23,000	2.25	23,000

The fair values of the stock options issued in 2017 were determined using the Black-Scholes option pricing model with the following assumptions: (i) risk-free rate of 1.50%, (ii) life expectancy of 2-5 years, and (iii) estimated volatility of 10.0%. The grant-date fair value of total options granted during the year is estimated at $12.90 (2016 – $nil). The weighted average grant-date fair value per share option to date is $1.90.

RESTRICTED SHARE UNIT (RSU) PLAN

The restricted share units are share-settled awards for which the provision recorded as at December 31, 2017 was $613 (2016 – $360). The amount debited to operating expenses for 2017 was $253 (2016 – $367).

(in thousands of Canadian dollars, except per share amounts)

19 RELATED PARTY TRANSACTIONS

KEY MANAGEMENT

Key management includes named executive officers. Compensation to these individuals are summarized in the following table for the year ending December 31:

Compensation	2017	2016
Salaries, and other short-term benefits	**1,766**	1,626
Equity-settled and cash-settled compensation benefits	**1,069**	552
Termination benefits	**—**	2,067
	2,835	4,245

20 OPERATING COSTS BY NATURE

The table below presents operating costs by major category for the year ending December 31:

	2017	2016
Salaries and benefits	**16,367**	14,475
Systems costs	**8,237**	7,565
Professional fees	**2,509**	1,760
Occupancy	**1,720**	1,358
Severance	**262**	4,266
Other expenses	**2,198**	3,999
	31,293	33,423

21 OPERATING LEASE COMMITMENTS

The Company is committed under lease agreements for office and property operating leases with minimum lease payments of $10,859 as at December 31, 2017:

Lease commitments	
2018	1,773
2019	1,691
2020	1,413
2021	1,417
2022	1,364
2023 and thereafter	3,201
	10,859

22 STRUCTURED SETTLEMENTS

In the normal course of claims adjudication, the Company may settle certain long-term losses through the purchase of annuities (structured settlements) from life insurance companies. The fair estimated value of these annuity contracts amounts to $36,472 (December 31, 2016 – $32,729) using a discount rate of 2.26% (December 31, 2016 – 2.31%). It is the policy of the Company to purchase annuities from life insurers with proven financial stability. The net risk to the Company is the credit risk related to the life insurance companies and this risk is reduced to the extent of coverage provided by Assuris, the life insurance compensation insurance plan. The Company has determined that no credit risk provision is required.

23 CONTINGENCIES

From time to time, in connection with its insurance operations, the Company is named as a defendant in actions for damages and costs allegedly sustained by the plaintiffs. While it is not possible to estimate the outcome, such actions have generally been resolved with minimal damage or expense in excess of amounts provided as policy liabilities. The Company does not believe that it will incur any significant additional loss or expense in connection with such actions.

24 RATE REGULATIONS

The Company writes business subject to rate regulation, including non-standard automobile and motorcycle insurance in Canada, which comprises approximately 66% (2016 – 72%) of gross premiums written and assumed. The Company's automobile insurance premiums can be impacted by mandatory rate rollbacks and mandatory rate assessments as legislated by provincial law and by regulation in certain provinces. This could result in lower future premium rates or reductions to premium rates charged by the Company in prior years. In addition, the Company is required, under certain provincial legislation, to participate in risk-sharing pools, which may impact positively or negatively on underwriting results. Certain benefit payments are also subject to provincial government regulation, including automobile accident benefits.

25 ACCUMULATED OTHER COMPREHENSIVE INCOME

A breakdown of the accumulated other comprehensive income is shown below as at December 31:

	2017	2016
Gross unrealized losses	**(3,966)**	(459)
Foreign currency translation adjustments	**499**	(10,776)
Foreign exchange forward	**—**	4,314
Tax impact	**634**	1,851
Ending balance	**(2,833)**	**(5,070)**

(in thousands of Canadian dollars, except per share amounts)

26 EARNINGS PER SHARE

Earnings Per Share on Continued Operations, for year ending December 31	**2017**	2016
Basic earnings per share on continued operations:		
Net income available to shareholders	**6,489**	6,606
Average number of common shares	**11,819**	11,738
Basic earnings per share on continued operations	**$0.55**	$0.56
Diluted earnings per share:		
Average number of common shares	**11,819**	11,738
Average number of dilutive common shares under employee stock compensation plan	**249**	261
Average number of diluted common shares	**12,068**	11,999
Diluted earnings per share on continued operations	**$0.54**	$0.55

Earnings Per Share on Discontinued Operations, for year ending December 31	**2017**	2016
Basic (loss) per share on discontinued operations:		
Net (loss) available to shareholders	**(4,855)**	(36,414)
Average number of common shares	**11,819**	11,738
Basic (loss) per share on discontinued operations	**$(0.41)**	$(3.10)
Diluted earnings per share:		
Average number of common shares	**11,819**	11,738
Average number of dilutive common shares under employee stock compensation plan	**249**	261
Average number of diluted common shares	**12,068**	11,999
Diluted (loss) per share on discontinued operations	**$(0.41)**	$(3.10)

Total Earnings Per Share, for year ending December 31	**2017**	2016
Basic earnings per share:		
Net income (loss) available to shareholders	**1,634**	(29,808)
Average number of common shares	**11,819**	11,738
Basic earnings (loss) per share	**$0.14**	$(2.54)
Diluted earnings per share:		
Average number of common shares	**11,819**	11,738
Average number of dilutive common shares under employee stock compensation plan	**249**	261
Average number of diluted common shares	**12,068**	11,999
Diluted earnings (loss) per share	**$0.14**	$(2.54)

(in thousands of Canadian dollars, except per share amounts)

27 DISCONTINUED OPERATIONS

On August 4, 2016, Echelon entered into a definitive stock purchase agreement to sell its European insurance subsidiary, subject to regulatory approval. On February 28, 2017, regulatory approval was received from the Danish Financial Supervisory Authority, which completed the necessary approvals required for the sale. The Company completed the sale on March 7, 2017, and has retained no residual insurance risk or other financial risk other than credit risk associated with the loan receivable from the sale.

For year ending December 31:	**2017**	2016
Revenue		
Gross written and assumed premiums	**15,896**	247,573
Net written premium	**12,784**	121,052
Decrease in provision for unearned premium	**6,173**	23,792
Net earned premiums	**18,957**	144,844
Investment (loss) income	**(10,562)**	2,643
Total revenue	**8,395**	147,487
Expenses		
Net incurred claims	**10,392**	108,677
Net acquisition costs	**6,254**	51,198
Operating costs	**1,198**	6,910
Total expenses	**17,844**	166,785
(Loss) before income taxes	**(9,449)**	(19,298)
Income tax (recovery)	**(2,050)**	(6,031)
Net (loss) on discontinued operations	**(7,399)**	(13,267)
Revaluation/(Impairment) of the net assets of disposal group held for sale	**2,544**	(23,379)
Net (loss) on discontinued operations	**(4,855)**	(36,646)
Other comprehensive income (loss) on discontinued operations	**7,268**	(9,459)
Comprehensive income (loss) on discontinued operations	**2,413**	(46,105)

28 NON-CONTROLLING INTEREST

The Company has non-controlling interests attributable to the subsidiary of ICPEI, please refer to note 1. The following tables summarize the comprehensive income attributable to the non-controlling shareholders for year ending December 31:

	2017	2016
Revenue		
Gross written and assumed premiums	**8,122**	7,409
Net earned premiums	**7,017**	6,482
Investment income	**351**	330
Total revenue	**7,368**	6,812
Expenses		
Net incurred claims	**4,468**	3,427
Net acquisition costs	**1,757**	1,636
Operating costs	**942**	1,035
Total expenses	**7,167**	6,098
Income before income taxes	**201**	714
Income tax	**47**	202
Net (loss) income attributable to NCI	**154**	512
Other comprehensive (loss) income attributable to NCI	**(67)**	(52)
Comprehensive (loss) income attributable to NCI	**87**	460

The following tables are the net assets of the non-controlling shareholders as at December 31:

	2017	2016
Assets		
Cash and investments	**9,430**	9,421
Other assets	**5,018**	4,377
Total assets	**14,448**	13,798
Liabilities		
Unearned premium	**4,048**	3,699
Unpaid claims	**6,062**	5,709
Other liabilities	**508**	648
Total liabilities	**10,618**	10,056
Equity		
Share capital	**—**	—
AOCI	**(109)**	(43)
Retained earnings	**3,939**	3,785
Total equity	**3,830**	3,742
Total liabilities and equity	**14,448**	13,798

(in thousands of Canadian dollars, except per share amounts)

The prior year equity balance above excludes discontinued operations and will therefore differ from the non-controlling interest amount disclosed on the balance sheet of these financial statements.

	As at Dec. 31, 2017	As at Dec. 31, 2016
Cash flow from operating activities	**70**	1,138
Cash flow from investing activities	**(720)**	(232)
Net increase (decrease) in cash and short-term deposits	**(650)**	906

29 SEGMENTED INFORMATION

The Company operates through two segments: Personal Lines and Commercial Lines businesses. Through its Personal Lines segment, the Company is engaged primarily in the underwriting of non-standard automobile insurance and insurance for motorcycles, antique and classic vehicles, trailers, motor-homes, recreational vehicles and personal property.

Through its Commercial Lines, the Company designs and underwrites specialized insurance programs, such as commercial property, commercial automobile, long-haul trucking, surety, liability, creditor insurance, and extended warranty..

The European operations are discontinued. Please refer to note 27.

The effect of reinsurance is reflected in the revenue and results of each segment. The investment activities consist of managing the investment portfolio for the Company as a whole. Investment income is shown net of investment expenses. The corporate and other activities include holding company expenses not attributable to a division.

The following tables summarize the net income before interest and income taxes by Personal and Commercial Lines for year ending December 31:

	2017	2016
Revenue		
Net earned premiums		
– Personal Lines	**165,893**	139,616
– Commercial Lines	**61,503**	41,444
Total net earned premium	**227,396**	181,060
Net claims Incurred		
– Personal Lines	**124,885**	97,823
– Commercial Lines	**31,929**	12,949
Total net claims incurred	**156,814**	110,772
Net expenses		
– Personal Lines	**50,194**	44,970
– Commercial Lines	**25,571**	18,504
Total	**75,765**	63,474
Corporate Expenses	**7,260**	7,228
Total net expenses	**83,025**	70,702
(Loss) income before income taxes		
– Personal Lines	**(9,186)**	(3,177)
– Commercial Lines	**4,003**	9,991
Total	**(5,183)**	6,814
Corporate and other	**(7,260)**	(7,228)
Underwriting (loss)	**(12,443)**	(414)
Impact of change in net claims discount rate	**3,254**	(2,822)
Severance expense	**(262)**	(4,266)
Investment income	**17,196**	16,507
Total income before interest expense and income taxes	**7,745**	9,005

Shareholder Information

Echelon Financial Holdings Inc.

2680 Matheson Blvd. E., Suite 300
Mississauga, ON L4W 0A5
Tel: 905-214-7880
Fax: 905-214-8028

Directors

Murray Wallace (Chairman)
James Falle
Serge Lavoie
Andrew Pastor
Gary Quon
Sharon Ranson
Brian Reeve
David Thomson

Transfer Agent and Registrar

Computershare Trust Company of Canada
100 University Avenue, 9th Floor
Toronto, ON M5J 2Y1

Stock Exchange Listing

Toronto Stock Exchange
Trading Symbol "EFH"

Common Shares Outstanding

11,891,076 (as at December 31, 2017)

Dividends

All dividends paid by the Company are "eligible dividends" for Canadian income tax purposes unless indicated otherwise

General Counsel

Blake, Cassels & Graydon LLP

Appointed Actuary

Willis Towers Watson

Auditors

PricewaterhouseCoopers LLP

Investor Relations

Jennifer Kew

Website

www.echeloninsurance.ca

Echelon Insurance

2680 Matheson Blvd. E., Suite 300
Mississauga, ON L4W 0A5