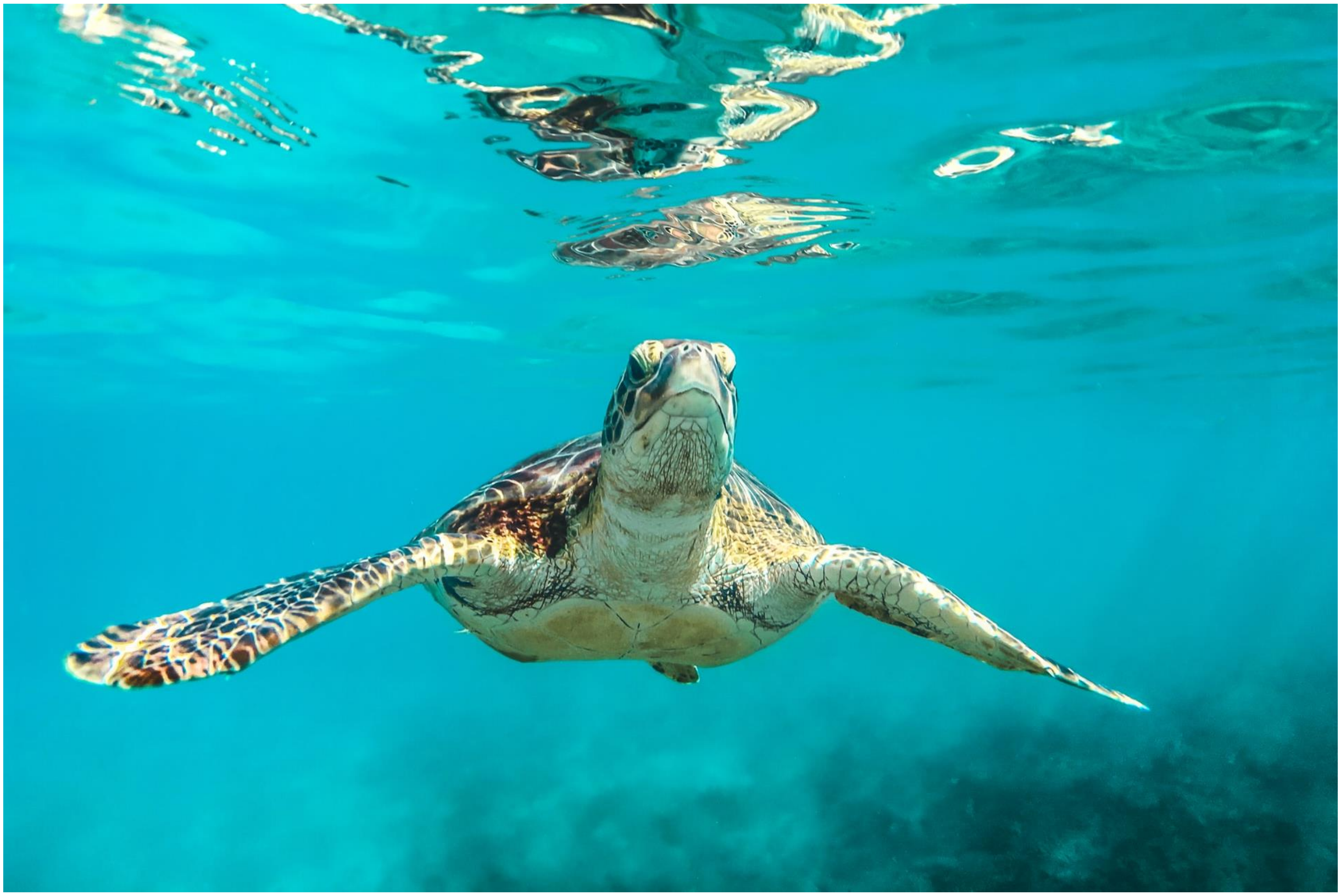
BMO Reinsurance



BMO Reinsurance Limited

Financial Statements

For the Year ended October 31, 2020

BMO Reinsurance

**BMO Reinsurance Limited**
Cedar Court,
Wildey Business Park,
Wildey, St. Michael, BB14006
Barbados
Tel: (246) 62-26673 (62-BMORE)
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# Actuarial Certificate

I have valued the actuarial liabilities and other contract liabilities of BMO Reinsurance Limited for its balance sheet as at October 31, 2020 and the changes in the statement of income and comprehensive income for the year then ended in accordance with the accepted actuarial practice including selection of appropriate assumptions and methods.

In my opinion, the amount of actuarial liabilities net of reinsurance recoverables in this report makes appropriate provision for all policy obligations.

Jerome Lamontagne
Fellow, Canadian Institute of Actuaries & Society of Actuaries
**Cedar Court, Wildey Business Park, Wildey, St. Michael, Barbados**
**December 18, 2020**

# INDEPENDENT AUDITORS' REPORT

## To the Shareholder of BMO Reinsurance Limited

### Report on the Audit of the Financial Statements

### Opinion

We have audited the financial statements of BMO Reinsurance Limited (the "Company"), which comprise the balance sheet as at October 31, 2020, the statements of income and comprehensive income, changes in shareholder's equity, and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Company as at October 31, 2020, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

### Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with International Ethics Standards Board for Accountants International Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in Barbados and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### Responsibilities of Management and Those Charged with Governance for the Financial Statements

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

In preparing the financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

### Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

# INDEPENDENT AUDITORS' REPORT, continued

### To the Shareholder of BMO Reinsurance Limited, continued

**Auditors' Responsibilities for the Audit of the Financial Statements, continued**

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

KPMG

Chartered Accountants
Bridgetown, Barbados
January 22, 2021

# Statement of Income and Comprehensive Income

| For the Year Ended October 31, (Canadian $) | Notes | 2020 | 2019 |
|---|---|---|---|
| **Revenue** | | | |
| Gross premiums | 12 | $ 516,644,333 | 624,199,375 |
| Premiums ceded | 12 | (4,668,842) | (14,843,197) |
| Net premiums | | 511,975,491 | 609,356,178 |
| Change in unearned premiums | 13 | 24,751,326 | 42,681,965 |
| Net premiums earned | | 536,726,817 | 652,038,143 |
| Net investment income | 4 | 14,572,676 | 7,216,754 |
| **Total revenue** | | 551,299,493 | 659,254,897 |
| **Expenses** | | | |
| Gross claims | 18 | 343,075,427 | 316,624,748 |
| Claims ceded | 18 | (2,725,419) | (1,360,095) |
| Change in actuarial liabilities | 15 | (4,361,941) | (16,643,945) |
| Change in reinsurance assets | 16 | 1,095,443 | (1,128,493) |
| Change in outstanding losses and loss expenses | 17 | (54,303,983) | 84,088,318 |
| Acquisition expenses | 10 | 87,418,040 | 109,679,899 |
| Operating expenses | 2, 19 | 4,143,069 | 7,007,763 |
| **Total expenses** | | 374,340,636 | 498,268,195 |
| **Net income attributable to shareholder** | | 176,958,857 | 160,986,702 |
| **Other comprehensive (loss) income** | | | |
| Items that may be subsequently reclassified to net income: | | | |
| Unrealized gains on fair value through other comprehensive income debt securities arising during the period | | 4,150,439 | 13,909,893 |
| Reclassification of realized gains to net income during the period | | (9,238,235) | (9,564) |
| Unrealized losses on cash flow hedges arising during the period | | - | (62,912) |
| Reclassification to net income of losses (gains) on cash flow hedges | | 104,753 | (43,222) |
| **Total comprehensive income** | | $ 171,975,814 | 174,780,897 |

*The accompanying notes form an integral part of these financial statements.*

Financial Statements

# Balance Sheet

| As at October 31, (Canadian $) | Notes | 2020 | 2019 |
|---|---|---|---|
| **Assets** | | | |
| Cash | | $ 299,141,743 | 118,960,160 |
| Investments | 3, 4 | 112,539,382 | 455,721,869 |
| Accrued interest receivable | 4 | 615,283 | 2,424,174 |
| Cross-currency swaps | 3, 5 | - | 901,436 |
| Reinsurance balances receivable | 9 | 66,977,591 | 115,214,609 |
| Other assets | 2, 10 | 4,862,502 | 10,120,490 |
| Reinsurance assets | 16 | 2,286,915 | 3,382,358 |
| **Total Assets** | | $ 486,423,416 | 706,725,096 |
| **Liabilities and Shareholder's Equity** | | | |
| **Liabilities** | | | |
| Accounts payable and other liabilities | 2, 11 | $ 2,000,234 | 2,383,436 |
| Balances due to reinsurers | 11 | 4,546,851 | 4,043,101 |
| Unearned premium reserve | 13 | 17,182,373 | 41,933,699 |
| Cross-currency swaps | 3, 5 | - | 3,980,792 |
| Actuarial liabilities | 15 | 54,619,136 | 58,981,077 |
| Outstanding losses and loss expenses | 17 | 235,919,898 | 290,223,881 |
| **Total Liabilities** | | 314,268,492 | 401,545,986 |
| **Shareholder's Equity** | | | |
| Share capital | | | |
| Common | 20 | 10,000,000 | 50,000,000 |
| Preferred | 20 | 78,000,000 | 213,000,000 |
| Accumulated other comprehensive income | | 1,648,838 | 6,631,881 |
| Retained earnings | | 82,506,086 | 35,547,229 |
| **Total Shareholder's Equity** | | 172,154,924 | 305,179,110 |
| **Total Liabilities and Shareholder's Equity** | | $ 486,423,416 | 706,725,096 |

*The accompanying notes form an integral part of these financial statements.*

Approved on behalf of the Board of Directors:

Wayne Fields
Director

Sir Trevor Carmichael
Director

Financial Statements

# Statement of Changes in Shareholder's Equity

| For the Year Ended October 31, (Canadian $) | Notes | 2020 | 2019 |
|---|---|---|---|
| **Share capital:** | | | |
| Common shares | | | |
| Balance, beginning of year | 20 | $ 50,000,000 | 50,000,000 |
| Share capital reduction | 20 | (40,000,000) | - |
| Balance, end of year | 20 | 10,000,000 | 50,000,000 |
| Preferred shares | | | |
| Balance, beginning of year | 20 | 213,000,000 | 213,000,000 |
| Share capital reduction | 20 | (135,000,000) | - |
| Balance, end of year | 20 | 78,000,000 | 213,000,000 |
| **Retained earnings:** | | | |
| Balance, beginning of year | | 35,547,229 | 69,560,527 |
| Net income for the year | | 176,958,857 | 160,986,702 |
| Dividends declared | | | |
| Common | | (53,719,008) | (80,578,513) |
| Preferred | | (76,280,992) | (114,421,487) |
| | | (130,000,000) | (195,000,000) |
| Balance, end of year | | 82,506,086 | 35,547,229 |
| **Accumulated other comprehensive income (loss):** | | | |
| Balance, beginning of year | | 6,631,881 | (7,162,314) |
| Unrealized gains on fair value through other comprehensive income debt securities arising during the year | | 4,150,439 | 13,909,893 |
| Reclassification of realized gains to net income during the year | | (9,238,235) | (9,564) |
| Unrealized losses on cash flow hedges arising during the year | | - | (62,912) |
| Reclassification to net income of losses (gains) on cash flow hedges | | 104,753 | (43,222) |
| Balance, end of year | | 1,648,838 | 6,631,881 |
| **Total Shareholder's Equity** | | $ 172,154,924 | 305,179,110 |

*The accompanying notes form an integral part of these financial statements.*

# Statement of Cash Flows

| For the Year Ended October 31, (Canadian $) | Notes | 2020 | 2019 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Net income for the year | | $ 176,958,857 | 160,986,702 |
| Adjustment to reconcile net income to net cash from operating activities: | | | |
| Unrealized foreign exchange gain on investments | | (26,278,242) | (885,818) |
| Amortization of discount on bonds, net | | (809,275) | (1,523,132) |
| Realized gains on sale of investments, net | | (9,238,235) | (9,564) |
| Gain on sale of premises and equipment | | (80,864) | (1,795) |
| Amortization of premises and equipment | 10,19 | 196,506 | 65,737 |
| Unrealized losses on cross-currency swaps | 5 | 18,149,982 | 1,600,251 |
| Change in operating assets | 21 | 56,634,385 | 15,961,992 |
| Change in operating liabilities | 21 | (83,444,717) | 24,368,218 |
| Net cash from operating activities | | 132,088,397 | 200,562,591 |
| **Cash flows used in financing activities** | | | |
| Share capital reduction | | (175,000,000) | - |
| Dividends paid | | (130,000,000) | (195,000,000) |
| Repayment of lease liabilities | | (145,109) | - |
| Cash used in financing activities | | (305,145,109) | (195,000,000) |
| **Cash flows from investing activities** | | | |
| Proceeds from sale/maturities of investments | | 1,108,799,558 | 1,651,561,544 |
| Purchase of investments | | (734,379,116) | (1,609,601,115) |
| Proceeds from unwound cross-currency swaps, net | | (21,124,585) | - |
| Proceeds from sale of premises and equipment | | 90,308 | 1,795 |
| Purchase of premises and equipment | | (147,870) | (19,094) |
| Net cash from investing activities | | 353,238,295 | 41,943,130 |
| Net increase in cash | | 180,181,583 | 47,505,721 |
| Cash at beginning of year | | 118,960,160 | 71,454,439 |
| **Cash at end of year** | | $ 299,141,743 | 118,960,160 |
| **Supplemental cash flow information:** | | | |
| Net cash provided by operating activities includes: | | | |
| Interest received | | $ 6,141,301 | 9,766,046 |
| Interest paid | | 3,810 | - |

*Certain comparative figures have been reclassified to conform with the current period's presentation and for changes in accounting policy (Note 2). Prior to adoption of IFRS 16, repayments of lease liabilities were included in "Net cash from operating activities".*

*The accompanying notes form an integral part of these financial statements.*

# Note 1: Reporting Entity

BMO Reinsurance Limited ("the Company") was incorporated in Barbados on September 29, 1986 and is a wholly owned subsidiary of BMO Investments Limited, a company incorporated in Bermuda. Its ultimate parent is Bank of Montreal ("BMO" or "the Bank"), a company incorporated in Canada.

The Company is a Class 2 licensed insurer under the Insurance Act, Cap. 310. Effective January 1, 2019, the Company opted to be grandfathered under the Exempt Insurance Act, retaining the benefits thereunder until June 30, 2021. At any time during this period, the Company may elect to transition to the provisions of the Insurance Act.

The Company's principal activity is the reinsurance of life, health, disability, job loss, property catastrophe and specialty property and casualty insurance risks. During 2019, a decision was made to exit the property and casualty reinsurance market.

The principal place of business is St. Michael, Barbados.

# Note 2: Basis of Preparation

## Statement of Compliance

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

These financial statements were authorized for issue by the Company's Board of Directors on January 22, 2021.

## Basis of Measurement

These financial statements have been prepared on a historical cost basis, except for the revaluation of bonds and cross-currency swaps.

## Significant Accounting Policies

To facilitate a better understanding of the financial statements, the significant accounting policies have been disclosed throughout the notes with the related financial disclosures by major caption.

## Translation of Foreign Currencies

The Company conducts business in a variety of foreign currencies and presents the financial statements in Canadian dollars, which is the functional currency. Monetary assets and liabilities as well as non-monetary assets and liabilities measured at fair value that are denominated in foreign currencies, are translated into Canadian dollars at the exchange rate in effect at the balance sheet date. Non-monetary assets and liabilities not measured at fair value are translated into Canadian dollars at historical rates. Revenues and expenses denominated in foreign currencies are translated using the average exchange rate for the year. Resulting exchange gains and losses are recorded in the Statement of Income and Comprehensive Income.

From time to time, the Company enters into foreign exchange hedge contracts to reduce its exposure to changes in the value of foreign currencies. Realized and unrealized gains and losses that arise on the mark-to-market of foreign exchange contracts related to economic hedges are included in net investment income in the Statement of Income and Comprehensive Income.

## Offsetting Financial Assets and Financial Liabilities

Financial assets and financial 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.

## Use of Estimates and Judgments

The preparation of the financial statements requires management to use estimates and assumptions that affect the carrying amounts of certain assets and liabilities, certain amounts reported in comprehensive income and other related disclosures.

The most significant assets and liabilities where management must make estimates and judgments include the fair value of bonds and cross- currency interest rate swaps and the determination of reinsurance assets, actuarial liabilities and outstanding losses and loss expenses. Note 3 discusses the nature and method of determining the significant assumptions made in the computation of the fair value of bonds and cross-currency swaps. Notes 15, 16 and 17 discuss the nature and method of determining the significant assumptions made in the computation of actuarial liabilities, reinsurance assets and outstanding losses and loss expenses. If actual results differ from the estimates, the impact would be recorded in future periods.

The full extent of the impact that COVID-19, including government and regulatory responses to the outbreak, will have on the Canadian and U.S. economies and the Company's business remains uncertain and difficult to predict at this time. By their very nature, the judgments and estimates the Company makes for the purposes of preparing the financial statements relate to matters that are inherently uncertain. However, the Company has detailed policies and internal controls that are intended to ensure that these judgments and estimates are well controlled and independently reviewed, and that its policies are consistently applied from period to period. Management believes that the estimates of the value of the Company's assets and liabilities are appropriate as at October 31, 2020.

*Leases*

The Company enters into leases as a lessee for which it recognizes a lease liability and a corresponding right-of-use asset. In calculating the lease liability and corresponding right-of-use asset, the Company assesses whether a contract is a lease by determining if it has the right to control the asset based on its ability to make decisions or direct how and for what purpose the asset is used. The Company evaluates the lease term based on the terms of the lease contract including any extension or termination options that are reasonably certain to be exercised based on the economic rationale underlying the decision. The Company makes judgments in determining the incremental borrowing rate that is used to discount lease liabilities, based on its expected costs of secured borrowing for the lease term.

*Allowance for Credit Losses*

The expected credit loss model ("ECL") requires the recognition of credit losses generally based on twelve months of expected losses for performing financial assets and the recognition of lifetime losses on financial assets that have experienced a significant increase in credit risk since origination.

In determining whether there has been a significant increase in credit risk and in calculating the amount of expected credit losses, the Company must rely on estimates and exercise judgment regarding matters for which the ultimate outcome is unknown. These judgments include changes in circumstances that may cause future assessments of credit risk to be materially different from current assessments, which could require an increase or decrease in the allowance for credit losses.

*Impairment of Securities*
Debt securities classified as fair value through other comprehensive income ("FVOCI") are assessed for impairment using the ECL model. For securities determined to have low credit risk, the allowance for credit losses is measured at 12-month expected credit loss. A financial asset is considered to have low credit risk if the financial asset has a low risk of default, the borrower has a strong capacity to meet its contractual cash flow obligations in the near term and adverse changes in economic and business conditions in the longer term may, but will not necessarily, reduce the ability of the borrower to fulfill its contractual cash flow obligations.

## Changes in Accounting Policy

*Leases*
Effective November 1, 2019, the Company adopted IFRS 16 *Leases* ("IFRS 16"), whereby lessees are required to recognize a liability for the present value of future lease payments and record a corresponding asset on the Balance Sheet for most leases.

The main impact for the Company is recording real estate leases on the Balance Sheet. Previously, the Company's real estate lease was classified as an operating lease, whereby lease expense was recorded over the lease term with no asset or liability recorded on the Balance Sheet other than any related leasehold improvements.

On transition, the Company calculated the right-of-use asset and set it equal to the lease liability. The Company will continue to account for low dollar value leases as executory contracts with lease expense recorded over the lease term and no corresponding right-of-use asset or lease liability. On transition, the Company elected to exclude intangibles from the scope of lease accounting.

On transition, the impact to the Balance Sheet as at November 1, 2019 was an increase in other assets and an increase in accounts payable and other liabilities of $291,110, with no changes to prior years.

The following table sets out a reconciliation of the Company's operating lease commitments, as disclosed under IAS 17 Leases as at October 31, 2019, which were used to derive the lease liabilities as at November 1, 2019.

| | November 1 |
|---|---|
| Operating lease commitments at October 31, 2019 as disclosed in the financial statements | $ 296,644 |
| Discounted using the incremental borrowing rate at November 1, 2019 | (5,534) |
| Lease liability recognized at November 1, 2019 | $ 291,110 |

When measuring lease liabilities, the Company discounted lease payments using its incremental borrowing rate at November 1, 2019. The weighted-average rate applied is 1.87%.

## Future Changes in IFRS

*Insurance Contracts*
In May 2017, the IASB issued IFRS 17 *Insurance Contracts* which provides a comprehensive approach to accounting for all types of insurance contracts and will replace the existing IFRS 4 *Insurance Contracts.* In June 2020, the IASB issued amendments to IFRS 17 *Insurance Contracts* which included deferral of the effective date, resulting in a new adoption date of November 1, 2023 instead November 1, 2022. The Company will continue to closely monitor the ongoing developments related to the standard. The Company is currently assessing the impact of the standard on its future financial results.

*Conceptual Framework*
In March 2018, the IASB issued the revised *Conceptual Framework* ("Framework"), which sets out the fundamental concepts for financial reporting to ensure consistency in standard-setting decisions and that similar transactions are treated in a similar way, so as to provide useful information to users of financial statements. The revised Framework, which is effective for the Company's fiscal year beginning November 1, 2020, will inform future standard-setting decisions but does not impact existing IFRS. The Company does not expect the Framework to have a significant impact on its accounting policies.

# Note 3: Fair Value

Fair value represents the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between willing market participants at the measurement date (i.e. an exit price). The fair value amounts disclosed represent point-in-time estimates that may change in subsequent reporting periods due to changes in market conditions or other factors. Some financial instruments are not typically exchangeable or exchanged and therefore it is difficult to determine their fair value. Where there is no quoted market price, fair value is determined using management's best estimates based on a range of valuation techniques and assumptions; since they involve uncertainties, the fair values may not be realized in an actual sale or immediate settlement of the asset or liability.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

*Investments – FVOCI*
The fair value of investments is determined using prices observed in the most recent transactions. When observable price quotations are not available, fair value is determined based on discounted cash flow models using discounting curves and spreads obtained from independent dealers, brokers and multi-contributor pricing sources.

*Cross-Currency Swaps ("the swaps")*
Cross-currency swaps are carried at fair value, which is determined based on discounted cash flow calculations.

*Other*
For all of the Company's other financial instruments, the carrying values are assumed to be reasonable estimates of fair values due to their predominantly short-term nature.

## Fair value hierarchy

The Company uses a fair value hierarchy to categorize financial instruments according to inputs used in its valuation techniques to measure fair value. The Company determines the fair value of publicly traded fixed maturity investments using quoted market prices in active markets (Level 1) when these are available. When quoted prices in active markets are not available, the Company determines the fair value of financial instruments using models such as discounted cash flows, with observable market data for inputs, such as yield and prepayment rates or broker quotes and other third-party vendor quotes (Level 2).

Fair value may also be determined using models where significant market inputs are unobservable due to inactive or minimal market activity (Level 3). The Company maximizes the use of market inputs to the extent possible.

The extent of the use of quoted market prices (Level 1) and internal models using observable market information as inputs (Level 2) in the valuation of investments and swaps were as follows:

| | | | 2020 |
|---|---|---|---|
| | Valued using quoted market prices | Valued using Internal models (with observable inputs) | Total |
| Investments - FVOCI | $ 17,752,659 | 94,786,723 | 112,539,382 |
| Total | $ 17,752,659 | 94,786,723 | 112,539,382 |

Notes

| 2019 | Valued using quoted market prices | Valued using internal models (with observable inputs) | Total |
|---|---|---|---|
| Investments - FVOCI | $ 144,333,650 | 311,388,219 | 455,721,869 |
| Swaps – trading (net) | - | (2,697,377) | (2,697,377) |
| Swaps – hedging (net) | - | (381,979) | (381,979) |
| Total | $ 144,333,650 | 308,308,863 | 452,642,513 |

The Company had no Level 3 financial instruments at October 31, 2020 and 2019.

*Significant Transfers*
The Company's policy is to record transfers of assets and liabilities between fair value hierarchy levels at their fair values as at the end of each reporting period, consistent with the date of the determination of fair value. Transfers between the various fair value hierarchy levels reflect changes in the availability of quoted market prices or observable market inputs that result from changes in market conditions.

During the year ended October 31, 2020, $11,729,176 of FVOCI investments (2019: $76,296,281) were transferred from Level 1 to Level 2 due to reduced observability of the inputs used to value these securities.

## Note 4: Investments

Investments are designated as FVOCI with changes in fair value recorded in other comprehensive income in the Statement of Income and Comprehensive Income. The summary of investment carrying values is as follows:

| | 2020 | 2019 |
|---|---|---|
| Commercial paper | $ 39,917,177 | 91,019,693 |
| Bonds | 72,622,205 | 364,702,176 |
| | $ 112,539,382 | 455,721,869 |

Investments by geographic region are as follows:

| | 2020 | 2019 |
|---|---|---|
| United States | $ 95,729,833 | 395,443,340 |
| Canada | 1,553,009 | 10,689,989 |
| Europe | - | 13,893,117 |
| Other | 15,256,540 | 35,695,423 |
| | $ 112,539,382 | 455,721,869 |

There are no provisions for credit losses related to these amounts as at October 31, 2020 and 2019.

## Bonds

The par value and carrying amount of bonds are shown by contractual maturity in the tables below.

| | | 2020 |
|---|---|---|
| Term to Maturity | Principal Amount | Carrying Amount & Fair Value |
| Corporate | | |
| Less than one year | $ 33,892,919 | 34,169,545 |
| One to five years | 8,248,484 | 8,437,558 |
| Supranational/Government | | |
| Less than one year | 9,900,000 | 9,999,989 |
| One to five years | 5,000,000 | 5,256,550 |
| More than five years | 10,654,800 | 14,758,563 |
| | $ 67,696,203 | 72,622,205 |

| | | 2019 |
|---|---|---|
| Term to Maturity | Principal Amount | Carrying Amount & Fair Value |
| Corporate | | |
| Less than one year | $ 84,922,360 | 85,249,548 |
| One to five years | 211,505,447 | 215,685,383 |
| Supranational/Government | | |
| Less than one year | 36,942,000 | 36,904,669 |
| One to five years | 12,500,000 | 12,683,871 |
| More than five years | 10,532,000 | 14,178,705 |
| | $ 356,401,807 | 364,702,176 |

Bonds – Interest Rate:

| | | 2020 | 2019 |
|---|---|---|---|
| | Interest Receivable Basis | Coupon Rate (% range) | Coupon Rate (% range) |
| Corporate | Semi-annual | 1.70 – 3.125 | 1.70 – 4.490 |
| Supranational/Government | Semi-annual | 1.25 – 6.375 | 1.125 – 6.375 |

## Investment income

Investment income is derived from the following sources:

| | 2020 | 2019 |
|---|---|---|
| Interest income | $ 5,575,327 | 10,915,253 |
| Realized gains on investments | 9,238,235 | 9,564 |
| Income (loss) derived from swaps | 10,062,495 | (2,079,032) |
| Realized and unrealized foreign exchange losses | (10,303,381) | (1,629,031) |
| | $ 14,572,676 | 7,216,754 |

Interest income is recognized in the Statement of Income and Comprehensive Income as it is accrued and is calculated using the effective interest rate method.

# Note 5: Cross-Currency Swaps

Derivative instruments are financial contracts that derive their value from underlying changes in interest rates, foreign exchange rates or other financial or commodity prices or indices. A cross-currency swap is a type of derivative where there is a contractual agreement between two parties to exchange fixed rate interest payments and principal amounts in different currencies. The Company enters into cross-currency swap agreements with a third party to hedge its currency risk on those bonds not denominated in Canadian dollars.

## Trading Derivatives

Swaps, which do not qualify as hedges for accounting purposes, are classified as trading derivatives and are marked to fair value. Realized and unrealized gains and losses are recorded in net investment income in the Statement of Income and Comprehensive Income. Unrealized gains and losses on trading derivatives are recorded as cross-currency swaps in the Balance Sheet.

## Accounting Hedges

In order for a derivative to qualify as an accounting hedge, the hedging relationship must be designated and formally documented at its inception, detailing the particular risk management objective and strategy for the hedge and the specific asset, liability or cash flow being hedged, as well as how its effectiveness is being assessed. Changes in the fair value of the derivative must be highly effective in offsetting either changes in the fair value of on-balance sheet items caused by the risk being hedged or changes in the amount of the future cash flows.

Hedge effectiveness is evaluated at the inception of the hedging relationship and on an ongoing basis, retrospectively and prospectively, primarily using quantitative statistical regression analysis. Any ineffectiveness in the hedging relationship is recognized in net investment income, in the Statement of Income and Comprehensive Income as it arises.

### Cash Flow Hedges

Cash flow hedges modify exposure to variability in cash flows for FVOCI debt securities denominated in foreign currencies. The Company's cash flow hedges, which have a maximum remaining term to maturity of three years, are hedges of FVOCI debt securities denominated in foreign currency. The Company hedges the full amount of foreign exchange risk.

Interest paid or received on these derivatives is recorded as an adjustment to net investment income in the Statement of Income and Comprehensive Income over the life of the hedge.

To the extent that changes in the fair value of the derivative offset changes in the fair value of the hedged item for the designated hedge risk, they are recorded in other comprehensive income. The excess of the change in fair value of the derivative that does not offset changes in the fair value of the hedged item (the "ineffectiveness of the hedge") is recorded directly in net investment income, in the Statement of Income and Comprehensive Income.

For cash flow hedges that are discontinued before the end of the original hedge term, the unrealized gain or loss recorded in other comprehensive income is amortized to net investment income in the Statement of Income and Comprehensive Income as the hedged item affects earnings. If the hedged item is sold or settled, the entire unrealized gain or loss is recognized in net investment income in the Statement of Income and Comprehensive Income. The Company does not terminate its foreign exchange hedges before maturity.

The main source of hedge ineffectiveness is the difference in the fixed rates between the hedging instrument and the hedged item.

## Fair Value of Trading and Hedging Swaps

Discussion of the fair value measurement of swaps is included in Note 3. Fair values of the swaps are as follows:

| | | | 2020 | | | 2019 |
|---|---|---|---|---|---|---|
| | Gross assets | Gross liabilities | Net | Gross assets | Gross liabilities | Net |
| **Trading** | | | | | | |
| Cross-currency swaps | $ - | - | - | 898,371 | (3,595,748) | (2,697,377) |
| **Hedging** | | | | | | |
| Cash flow hedges – cross-currency swaps | - | - | - | 3,065 | (385,044) | (381,979) |
| Total | $ - | - | - | 901,436 | (3,980,792) | (3,079,356) |

The swaps do not qualify for netting under the requirements of IAS 32, but are subject to master netting agreements with a right of set off only in the event of default, insolvency or bankruptcy. The Company has pledged cash balances to a third party in order to fulfill the collateral requirements for the swaps in place. At October 31, 2020 the cash pledged was $nil (2019: $2,879,000). The net exposure for the swaps was $nil (2019: $200,356).

### Notional Amounts

The notional amounts of the swaps represent the amount to which a rate or price is applied in order to calculate the amount of cash that must be exchanged under the contract. Notional amounts do not represent assets or liabilities and therefore are not recorded in the Balance Sheet.

| | 2020 | 2019 |
|---|---|---|
| **Trading swaps** | | |
| **Foreign exchange contract** | | |
| Cross-currency swaps | $ - | 207,098,674 |
| Total | $ - | 207,098,674 |

The following table outlines the notional amounts and average rates of swaps designated as hedging instruments, by term to maturity and risk type. All swaps were terminated during the year, hence there were no related hedges as at October 31, 2020.

Notes

| | Within 1 year | Remaining term to maturity<br>1 to 3 years | 2019<br>Total |
|---|---|---|---|
| **Cash flow hedges** | | | |
| **Foreign exchange risk – cross-currency swaps** | | | |
| CAD–USD pair | | | |
| Notional Amount | $15,171,850 | 13,019,000 | 28,190,850 |
| Average fixed interest rate | 1.3193 | 1.3023 | 1.3114 |
| Average exchange rate: CAD-USD | 2.22% | 2.07% | 2.15% |

## Cash Flow Hedging Relationships

For cash flow hedges, the following tables contain information related to items designated as hedging instruments, hedged items and hedge ineffectiveness for the years ended October 31, 2020 and October 31, 2019.

2020

| | | Asset | Liability | Losses on hedging derivatives used to calculate hedge ineffectiveness | Losses on hypothetical derivatives used to calculate hedge ineffectiveness | Ineffectiveness recorded in net investment income |
|---|---|---|---|---|---|---|
| **Cash flow hedges** | | | | | | |
| Foreign exchange risk - cross-currency swaps | $ | - | - | 172,071 | 127,632 | 86,136 |
| Total | $ | - | - | 172,071 | 127,632 | 86,136 |

2019

| | | Asset | Liability | Gains on hedging derivatives used to calculate hedge ineffectiveness | Gains on hypothetical derivatives used to calculate hedge ineffectiveness | Ineffectiveness recorded in net investment income |
|---|---|---|---|---|---|---|
| **Cash flow hedges** | | | | | | |
| Foreign exchange risk - cross-currency swaps | $ | 3,065 | (385,044) | (64,567) | (383,604) | 41,567 |
| Total | $ | 3,065 | (385,044) | (64,567) | (383,604) | 41,567 |

For cash flow hedges, the following table contains information related to impacts on the Statement of Other Comprehensive Income for the years ended October 31, 2020 and October 31, 2019.

| 2020 | | | | |
|---|---|---|---|---|
| | Active AOCI as at November 1, 2019 | Losses recognized in OCI | Amount reclassified to net income as the hedged item affects net income | Active AOCI as at October 31, 2020 |
| **Cash flow hedges** | | | | |
| Foreign exchange risk | $ (104,753) | - | 104,753 | - |
| Total | $ (104,753) | - | 104,753 | - |

| 2019 | | | | |
|---|---|---|---|---|
| | Active AOCI as at November 1, 2018 | Losses recognized in OCI | Amount reclassified to net income as the hedged item affects net income | Active AOCI as at October 31, 2019 |
| **Cash flow hedges** | | | | |
| Foreign exchange risk | $ 1,381 | (62,912) | (43,222) | (104,753) |
| Total | $ 1,381 | (62,912) | (43,222) | (104,753) |

# Note 6: Risk Management Framework

## Governance Framework

The Company's governance framework is centred around its Enterprise Risk Management ("ERM") process. The ERM process begins with the Board of Directors who determines the Company's strategy and aligns the objectives and means of the business with its risk appetite. The Company's strategy emphasises the transparency of its risk exposures and the quantitative assessment of these risks. The Company's objective is to avoid surprise losses or un-modelled exposures and ensure an adequate economic return on capital is achieved. It is Management's duty to continuously identify, measure, monitor, manage and report the various risks to which the Company is exposed.

## Capital Management Framework

The Company's objectives for capital management are to ensure capital is adequate to maintain the safety and stability of the Company, exceed minimum regulatory requirements and achieve the most efficient and effective use of capital.

## Regulatory Framework

The Company is regulated by the Insurance Division of the Financial Services Commission of Barbados, as authorized by the Financial Services Commission Act, 2010-21. Barbados has adopted the Insurance Core Principles of the International Association of Insurance Supervisors.

Under the grandfathering provisions, the Company must comply with the guidelines set out under the Exempt Insurance Act. This includes annual filing of audited financial statements no later than six months after the financial year end; provision of an actuarial certificate from an approved Actuary stating that the reserves are adequate to meet the liabilities; and a certificate of solvency must be submitted by the Auditor, in accordance with Section 24 of the Exempt Insurance Act.

### Asset Liability Management (ALM) Framework

Financial risks arise from open positions in interest rate, currency and financial products, all of which are exposed to general and specific market movements. The Company has an ALM framework within its Investment Policy to limit and monitor these risks.

## Note 7: Insurance Risk

The principal risk that the Company faces under reinsurance treaties is that the actual claims and benefit payments or the timing thereof, differ from expectations. This is influenced by the frequency of claims, severity of claims, actual benefits paid and subsequent development of long-term claims. Therefore, the objective of the Company is to ensure that sufficient reserves are available to cover these liabilities.

The Board of Directors has a clearly defined Risk Appetite Statement which ensures that a balanced underwriting approach is taken across all product lines. Insurance risk is further mitigated by diversification across a large portfolio of reinsurance treaties and geographical areas.

### Life insurance risks

The main components of the Company's life insurance risks are:

- Mortality risk – risk of loss arising due to policyholder death experience being different than expected.
- Morbidity risk – risk of loss arising due to policyholder health experience being different than expected.
- Involuntary unemployment risk – risk of loss arising due to policyholder job loss experience being different than expected.
- Catastrophe risk – risk of loss arising due to the frequency or severity of catastrophic events being different than expected.

**Key Assumptions**

Material judgment is required in the selection of the assumptions that determine the actuarial liabilities. Assumptions selected are based on industry and company experience, current observable market prices and other published information. The assumptions are determined at the date of valuation and are evaluated on a continuous basis. The determination of actuarial liabilities is sensitive to the following key assumptions.

*Mortality and morbidity rates*

Assumptions are based on standard industry mortality and morbidity rate tables, according to the type of risk written and the geographic territory. The rates reflect recent historical experience and are adjusted to reflect the Company's own experiences. An increase in rates would lead to a larger amount of claims than estimated.

*Discount rate*

Discount rates reflect investment return estimates on the assets supporting the actuarial liabilities. Actuarial liabilities are the sum of the discounted value of the expected benefits and future administration expenses, less the discounted value of expected premiums that are required to meet future cash outflows.

**Sensitivities**

The sensitivity analysis which follows shows the impact on gross and net liabilities for reasonably possible movements in key assumptions with all other assumptions held constant. The correlation of assumptions has a significant impact in determining the ultimate claims liabilities and are non-linear.

| | | | 2020 |
|---|---|---|---|
| Life Insurance | Change in Assumptions | Increase in gross liabilities | Increase in net liabilities |
| Mortality Rate | +10% | $ 7,689,818 | 7,206,393 |
| Discount Rate | -1% | 1,108,929 | 997,146 |

Notes

| | | | 2019 |
|---|---|---|---|
| Life Insurance | Change in Assumptions | Increase in gross liabilities | Increase in net liabilities |
| Mortality Rate | +10% | $ 7,319,527 | 6,803,369 |
| Discount Rate | -1% | 837,988 | 788,875 |

## General Insurance Risks

General insurance risks reinsured by the Company include aviation, crop, cyber, marine, motor, property per risk and property catastrophe. These risks are mitigated by diversification across geographic regions and perils. The Company's underwriting guidelines dictate the maximum claim exposure that can be incurred from a catastrophic event. The Company will be exiting the Property & Casualty reinsurance market, with all treaties terminating by December 2021, significantly reducing its exposure to catastrophic claims. However, some exposure to catastrophic claims will remain until all outstanding claims that occurred prior to the treaty termination dates are settled and paid.

# Note 8: Financial Instruments Risk Management

## Market Risk

Market risk is the risk of loss arising from adverse changes in market rates and prices, such as interest rates, trading prices of securities, credit spreads and foreign currency exchange rates. Market risk is directly influenced by the volatility and liquidity in the markets in which the related financial instruments are traded, expectations of future price and yield movements and the composition of the Company's investment portfolio. The Company's most significant market risks are interest rate risk and currency risk.

*Interest rate risk*

Interest rate risk is the risk of economic loss due to the need to reinvest or divest during periods of changing interest rates. The Company is exposed to interest rate risk on its fixed-interest rate bonds. The Company limits this risk by investing in short-term duration bonds. An increase of 50 basis points in interest rates would result in a decrease in other comprehensive income of $344,369 (2019: $3,520,111). A decrease of 50 basis points in interest rates would result in an increase in other comprehensive income of $344,395 (2019: $3,520,413).

*Currency risk*

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. As part of the Company's ALM Framework, the Company regularly monitors and matches the currency profile of its assets to its liabilities. The Company's swaps are used to manage the currency risk on its US dollar denominated bonds.

## Credit risk

Credit risk is the risk of financial loss resulting from the failure of debtors or counterparties to make payments of interest and/or principal when due. This credit risk is derived primarily from investments in bonds, derivatives, short term investments and amounts recoverable from reinsurers under reinsurance arrangements.

The Company manages this risk by applying its Investment Policy investment guidelines as approved by the Board of Directors. The investment guidelines establish minimum credit ratings for issuers of bonds and debentures and provide for concentration limits by issuer.

The Company's investment policy objective is to preserve capital while achieving an appropriate return on investment. The policy is to invest in non-Canadian bonds with the aggregate carrying value in any one corporate entity not exceeding 10% of the carrying value of the Company's assets at any time. All investment purchases must carry a minimum risk rating of BBB with the aggregate carrying value of BBB+ to BBB holdings not exceeding 30% of the carrying value of the portfolio. From time to time, the Company may hold bonds that after initial purchase have been downgraded to below BBB, subject to additional credit monitoring. No more than 25% of the aggregate carrying value of bonds may be invested in any one industry or sector.

The Company's maximum credit exposure is equivalent to the carrying value of the financial instruments on the Balance Sheet. To reduce its exposure to credit loss related to reinsurance counterparties, the Company enters into reinsurance treaties with reputable third party reinsurers. The Company evaluates the financial condition of its reinsurers to minimize its exposure to significant losses from reinsurer insolvencies (see Note 16). There are no amounts past due or in dispute from reinsurers as at October 31, 2020 and October 31, 2019.

The Company closely monitors the investment ratings of its bonds and as at the reporting date the ratings were:

| | 2020 | 2019 |
|---|---|---|
| AAA | $ 35,510,650 | 91,093,178 |
| AA | 22,240,046 | 144,340,629 |
| A | 14,871,509 | 123,843,722 |
| BBB | - | 5,424,647 |
| Total portfolio | $ 72,622,205 | 364,702,176 |

## Liquidity risk

Liquidity risk is the risk that the Company will not have access to cash to meet claims and other expense payments as they arise. The Company's policy is to ensure a minimum amount of cash is held in order to meet a claims paying threshold, while investing excess cash flows on a timely basis in accordance with investment policies. The threshold amount is set at $10,000,000 and the Company is well above this amount.

The maturities of the Company's financial assets and non-derivative financial liabilities are shown below. Maturity profiles for actuarial liabilities are determined based on the estimated timing of net cash outflows. Unearned premiums have been excluded from the analysis as they are not contractual obligations.

| | | | | 2020 |
|---|---|---|---|---|
| | Less than 1 year | 1 to 5 years | More than 5 years | Total |
| **Financial assets** | | | | |
| Cash | $ 299,141,743 | - | - | 299,141,743 |
| Investments | 85,527,799 | 12,253,020 | 14,758,563 | 112,539,382 |
| Accrued interest receivable | 615,283 | - | - | 615,283 |
| Reinsurance balances receivable | 66,977,591 | - | - | 66,977,591 |
| Other assets | 267,906 | - | - | 267,906 |
| Reinsurance assets | 2,286,915 | - | - | 2,286,915 |
| | $ 454,817,237 | 12,253,020 | 14,758,563 | 481,828,820 |
| **Financial liabilities** | | | | |
| Accounts payable and other liabilities | $ 2,000,234 | - | - | 2,000,234 |
| Balances due to reinsurers | 4,546,851 | - | - | 4,546,851 |
| Actuarial liabilities[1] | 55,943,560 | 7,402,484 | (9,615,562) | 53,730,482 |
| Outstanding losses and loss expenses | 57,453,712 | 178,466,186 | - | 235,919,898 |
| | $ 119,944,357 | 185,868,670 | (9,615,562) | 296,197,465 |

[1] Amounts disclosed above exclude unearned premium reserves.

Notes

| | Less than 1 year | 1 to 5 years | More than 5 years | 2019 Total |
|---|---|---|---|---|
| **Financial assets** | | | | |
| Cash | $ 118,960,160 | - | - | 118,960,160 |
| Investments | 213,173,910 | 228,369,254 | 14,178,705 | 455,721,869 |
| Accrued interest receivable | 2,474,174 | - | - | 2,474,174 |
| Reinsurance balances receivable | 115,214,609 | - | - | 115,214,609 |
| Other assets | 201,085 | - | - | 201,085 |
| Reinsurance assets | 3,382,358 | - | - | 3,382,358 |
| | $ 453,356,296 | 228,369,254 | 14,178,705 | 695,904,255 |
| **Financial liabilities** | | | | |
| Accounts payable and other liabilities | $ 2,383,436 | - | - | 2,383,436 |
| Balances due to reinsurers | 4,043,101 | - | - | 4,043,101 |
| Actuarial liabilities(1) | 61,042,081 | 7,894,406 | (10,989,793) | 57,946,694 |
| Outstanding losses and loss expenses | 53,119,579 | 92,719,031 | 144,385,271 | 290,223,881 |
| | $ 120,588,197 | 100,613,437 | 133,395,478 | 354,597,112 |

(1) Amounts disclosed above exclude unearned premium reserves.

## Note 9: Reinsurance Balances Receivable

Reinsurance balances receivable are recognized when due and measured on initial recognition at the fair value of the consideration received or receivable. Subsequent to initial recognition, reinsurance balances receivable are measured at amortized cost.

The carrying value of reinsurance balances receivable is reviewed for impairment whenever events or circumstances indicate that the carrying amount may not be recoverable, with the impairment loss recorded in the Statement of Income and Comprehensive Income. There has been no impairment loss recorded for the years ended October 31, 2020 and 2019.

## Note 10: Other Assets

Other assets comprise:

| | 2020 | 2019 |
|---|---|---|
| Prepaid expenses | $ 79,828 | 183,729 |
| Deferred acquisition expenses | 3,827,270 | 9,451,004 |
| Deferred reinsurance | 344,437 | 176,655 |
| Premises and equipment, at cost | 1,474,356 | 1,159,797 |
| less accumulated amortization | (1,131,295) | (1,051,780) |
| Other receivables | 267,906 | 201,085 |
| | $ 4,862,502 | 10,120,490 |

Prepaid expenses include rental deposits and payments made in advance for professional services to be rendered. Prepaid expenses are amortized on a straight-line basis over the life of the related service.

Deferred acquisition expenses comprise commissions, premium taxes and other costs which are directly related to the acquisition of premiums. These expenses, to the extent that they are considered recoverable, are deferred and amortized over the terms of the related treaties.

Deferred reinsurance relates to the portion of reinsurance ceded in the reporting periods that cover periods of insurance risk after the reporting date.

Other receivables include balances due from related parties and sales tax recoverable. Other receivables are recognized when due and measured on initial recognition at the fair value of the consideration received or receivable.

Premises and equipment are recorded at cost less accumulated amortization. They are amortized on a straight-line basis over their estimated useful lives ranging between two and ten years. Amortization expense for the year ended October 31, 2020 was $196,506 (2019: $65,737).

Amortization methods, useful lives and the values of premises and equipment are reviewed regularly for any change in circumstances and are adjusted if appropriate.

When the Company enters into new arrangements as a lessee, a right-of-use asset is recognized equal to the lease liability, which is calculated based on the future lease payments discounted at the incremental borrowing rate over the lease term. The lease term is based on the non-cancellable period and includes any options to extend or terminate which are reasonably certain to exercised.

The right-of-use asset is depreciated on a straight-line basis, based on the shorter of useful life of the underlying asset or the lease term, and is adjusted for impairment losses, if any.

The lease liability accretes interest over the lease term, using the effective interest method, with the associated interest expense recognized in operating expenses – other. The lease liability is remeasured when decisions are made to exercise options under the lease arrangement or when the likelihood of exercising an option within the lease changes.

Amounts relating to leases of low value are expensed when incurred in operating expenses – rent.

Prior to the adoption of IFRS 16, net rent expense reported in operating expenses - rent, in the Statement of Income for the years ended October 31, 2019 and 2018 was $178,313 and $171,843, respectively.

At least annually, the Company reviews whether there are any indications that premises and equipment need to be tested for impairment. If there is an indication that an asset may be impaired, the Company tests for impairment by comparing the asset's carrying value to its recoverable amount. The recoverable amount is calculated as the higher of the value in use and the fair value less costs to sell. Value in use is the present value of the future cash flows expected to be derived from the asset. An impairment charge is recorded when the recoverable amount is less than the carrying value. There were no write-downs of premises and equipment due to impairment during the years ended October 31, 2020 and 2019.



## Note 11: Financial Liabilities

Accounts payable and other liabilities, and balances due to reinsurers are classified as financial liabilities. These liabilities are recognized when due and measured on initial recognition at fair value. Subsequent to initial recognition, they are measured at amortized cost. Included in other liabilities are net deposits received in advance under certain reinsurance treaties. These deposits are amortized into income under the treaty terms.

Beginning November 1, 2019, when the Company enters into leases, it records lease liabilities representing the present value of future lease payments over the lease term. Interest expense on lease liabilities for the year ended October 31, 2020 was $3,810. Total cash outflow for leases for the year ended October 31, 2020 was $152,700. Variable lease payments (for example: utilities) not included in the measurement of lease liabilities for the year ended October 31, 2020 was $27,752. IFRS 16 was adopted on November 1, 2019, prior period amounts are not applicable.

The maturity profile of the Company's undiscounted lease liabilities is $107,101 for 2021 and $42,610 for 2022.

## Note 12: Premiums

Reinsurance treaties are those in which the Company has accepted significant insurance risk by agreeing to compensate the ceding companies for specified uncertain future events that adversely affect the ceding companies and whose amount and timing is unknown. In the absence of significant insurance risk, the treaty is classified as an investment contract.

A treaty which has been classified as an insurance contract remains as such until all rights and obligations under the contract extinguish or expire. Investment contracts may be reclassified as insurance contracts if insurance risk becomes significant.

### Gross Premiums

Gross premiums on those treaties with a fixed premium are recognized when the treaty is incepted. On all other treaties, premiums are recognized when they are due or reported by the ceding company.

### Premiums Ceded

Reinsurance premiums ceded are recognized when they are due under the terms of the agreements.

## Note 13: Unearned Premium Reserve

Premiums earned are generally recognized in income over the treaty period in proportion to the amount of reinsurance provided. Unearned premium reserves for property and casualty reinsurance treaties relate to the portion of gross premiums written in the reporting periods that cover periods of insurance risk after the reporting date.

| | | 2020 | 2019 |
|---|---|---|---|
| Balance, beginning of year | $ | 41,933,699 | 84,615,664 |
| Premiums written during the year | | 3,653,481 | 96,202,110 |
| Premiums earned during the year | | (29,190,750) | (138,919,103) |
| Foreign currency conversion | | 785,943 | 35,028 |
| Balance, end of year | $ | 17,182,373 | 41,933,699 |

## Note 14: Responsibilities of the Appointed Actuary

The Appointed Actuary is appointed by the Board of Directors subject to approval of the Financial Services Commission. The Actuary's responsibility is to carry out an annual valuation of the Company's long-term insurance business, per the Exempt Insurance Act of Barbados, using methods and assumptions considered to be appropriate to the circumstances of the Company and to the policies in force. In performing the valuation, the Actuary makes assumptions as to the future rates of interest, mortality, morbidity, policy termination, inflation, expenses and other contingencies.

# Note 15: Actuarial Liabilities

## Nature of Actuarial Liabilities

Actuarial liabilities, per the Exempt Insurance Act of Barbados, are calculated in respect of long-term insurance business using methods and assumptions considered to be appropriate to the circumstances of the Company and to the policies in force. They include a provision for losses incurred but not reported, and represent the amount, which in the opinion of the Company's actuary, together with estimated future premiums and investment income, will be sufficient to pay estimated future benefits on policy contracts reinsured by the Company.

Actuarial liabilities, as defined above, comprise:

| | 2020 | 2019 |
|---|---|---|
| Life | $ 25,412,655 | 28,725,983 |
| Health, Disability, and Job Loss | 29,206,481 | 30,255,094 |
| Actuarial liabilities | $ 54,619,136 | 58,981,077 |

| | 2020 | 2019 |
|---|---|---|
| Policy reserves | $ (5,916,138) | (7,560,476) |
| Claims reserves | 60,535,274 | 66,541,553 |
| Actuarial liabilities | $ 54,619,136 | 58,981,077 |

Changes in actuarial liabilities, as defined above, are as follows:

| | 2020 | 2019 |
|---|---|---|
| Actuarial liabilities, beginning of year | $ 58,981,077 | 75,625,022 |
| Change in actuarial liabilities from: | | |
| Existing reinsurance treaties | (5,855,995) | 2,462,804 |
| Changes in actuarial assumptions/methodology | 1,275,265 | (19,135,310) |
| Foreign currency conversion | 218,789 | 28,561 |
| Actuarial liabilities, end of year | $ 54,619,136 | 58,981,077 |

## Assumptions

The calculation of the actuarial liabilities requires assumptions as to the future course of events which will give rise to payments by the Company. These assumptions are established on the basis of current estimates of mortality, morbidity, rates of return on invested assets, administrative expenses and inflation.

*Mortality and morbidity*

The assumptions for mortality and morbidity are based either on industry experience or the ceding company's experience. Given the size of the Company and the statistical nature of claims, the Company may well experience a level of claims different from that expected in a particular year.

*Economic assumptions*

Where applicable, the valuation interest rate to discount future liabilities is based on the average expected yield on the assets supporting the liabilities.

*Administrative expenses and inflation*

Where applicable, amounts may be included in the actuarial liabilities to provide for the cost of administering policies and, where appropriate, the said amount may include inflation adjustments.

## Note 16: Reinsurance Assets

The Company has entered into reinsurance treaties for protection against claims in excess of stipulated amounts. Reinsurance assets represent balances due from retrocessionaires for ceded actuarial liabilities as disclosed in Note 15 and are estimated in the same manner.

Reinsurance assets are reviewed for impairment at each reporting date, or more frequently, when an indication of impairment arises during the reporting year. Impairment occurs when there is objective evidence as a result of an event that occurred after initial recognition of the reinsurance balance receivable that all outstanding amounts due under the terms of the contract may not be received. The event must have a reliably measurable impact on the amounts that the Company will receive from the reinsurer. Any impairment loss is recorded in the Statement of Income and Comprehensive Income. There has been no impairment loss recorded for the years ended October 31, 2020 and 2019.

## Note 17: Outstanding Losses and Loss Expenses

Outstanding losses and loss expenses for property and casualty reinsurance treaties are accrued when reinsured events occur and are based on the estimated ultimate cost of settling the claims, using reports and individual case estimates received from the cedents at the balance sheet date. In addition, a provision for additional case reserves is included when it is likely that there will be adverse development on specific case reserves reported by the cedent. A provision is also included for claims incurred but not reported, which is developed on the basis of past experience adjusted for current trends and other factors that may modify past experience.

The establishment of the appropriate level of reserves is an inherently uncertain process involving estimates and judgments made by management, and therefore there can be no assurance that ultimate losses and loss expenses will not exceed the claims reserves currently established. These estimates are regularly reviewed, and adjustments for differences between estimates and actual payments for claims and for changes in estimates are reflected in income in the period in which the estimates are changed or payments are made.

A reconciliation of the opening and closing reserve balances for outstanding losses and loss expenses for the period is presented as follows:

| | 2020 | 2019 |
|---|---|---|
| Balance, beginning of year | $ 290,223,881 | 206,135,563 |
| Incurred related to: | | |
| Current | 66,545,940 | 134,836,251 |
| Prior | (1,877,920) | 41,002,240 |
| Paid related to: | | |
| Current | (15,593,640) | (15,645,949) |
| Prior | (108,653,492) | (75,910,925) |
| Foreign exchange | 5,275,129 | (193,299) |
| Balance, end of year | $ 235,919,898 | 290,223,881 |

Included in current year are reserves for marine claims for Maersk Honam and Golden Ray, crop, satellite, and cyber claims. Prior claims include 2019 Japanese Typhoons Faxai and Hagibis. 2018 Japanese Typhoons Jebi and Trami and the Colombian Dam collapse, and 2017 claims due to several large natural catastrophes - Hurricanes Harvey, Irma, and Maria, two earthquakes in Mexico and the California wildfires.

## Note 18: Gross and Ceded Claims

Gross claims are comprised of paid claims and are recognized when reported by the ceding companies. Ceded claims are recognized when the related gross claims are expensed.

## Note 19: Operating Expenses

The following outlines the significant operating expenses:

| | | 2020 | 2019 |
|---|---|---|---|
| Salaries and benefits[1] | $ | 3,497,645 | 5,041,112 |
| Professional and consulting | | 84,650 | 46,895 |
| Letter of credit and bank fees | | 229,786 | 259,947 |
| Computer | | 188,162 | 636,276 |
| Rent[2] | | - | 178,313 |
| Amortization of premises and equipment[2] | | 196,506 | 65,737 |
| Other[2] | | (53,680) | 779,483 |
| | $ | 4,143,069 | 7,007,763 |

[1] Included in salaries and benefits in 2019 is a restructuring charge related to severance.

[2] Change in accounting policy reflecting adoption of IFRS16 (Note 2).

## Note 20: Share Capital

The Company is authorized to issue an unlimited number of non-redeemable common shares and an unlimited number of non-redeemable Class A preferred shares without nominal or par value. The holders of Class A Preferred Shares have certain voting rights and can attend the General Meeting of the Company. The holders of the Class A Preferred Shares have preference and priority to any payment of dividends on the Common Shares. The Class A Preferred Share dividends are non-cumulative and are at the discretion of the directors.

In April 2020, the Company's Board of Directors and Shareholder approved a reduction of $40,000,000 in the stated capital of the Company's common shares and a reduction of $135,000,000 in the stated capital of the Company's Class A Preferred Shares.

Issued and fully paid:

| | | 2020 | 2019 |
|---|---|---|---|
| 50,000,000 common shares – stated value | $ | 10,000,000 | 50,000,000 |
| 71,000,000 preferred shares - stated value | $ | 78,000,000 | 213,000,000 |

## Note 21: Net Cash Provided by Operating Activities

| | 2020 | 2019 |
|---|---|---|
| **Net change in operational assets** | | |
| Decrease in accrued interest receivable | $ 1,808,891 | 139,772 |
| Decrease in reinsurance balances receivable | 48,237,018 | 5,458,987 |
| Decrease in other assets | 5,493,033 | 11,491,726 |
| Decrease (increase) in reinsurance assets | 1,095,443 | (1,128,493) |
| | $ 56,634,385 | 15,961,992 |

| | 2020 | 2019 |
|---|---|---|
| **Net change in operational liabilities** | | |
| (Decrease) increase in accounts payable and other liabilities | $ (531,217) | 810,521 |
| Increase (decrease) in balances due to reinsurers | 503,750 | (1,204,711) |
| Decrease in unearned premium reserve | (24,751,326) | (42,681,965) |
| Decrease in actuarial liabilities | (4,361,941) | (16,643,945) |
| (Decrease) increase in outstanding losses and loss expenses | (54,303,983) | 84,088,318 |
| | $ (83,444,717) | 24,368,218 |

## Note 22: Related Party Transactions and Balances

Transactions with related parties are measured at the agreed upon exchange amount. The Company uses the legal, marketing, accounting, banking, credit analysis and collateral management services of BMO and the investment management services of BMO Global Asset Management. BMO is paid a fee for providing these services which is based upon terms that are similar with those the Company would charge unrelated parties.

The Company provides the use of its personnel, administrative support, accounting and systems to Bank of Montreal (Barbados) Limited (“BOMBL”), BMO Investments Limited (“BMOIL”), BMO Finance Company V Limited (“Finco V”) and BMO (Bermuda) Finance Ltd. (“BMO Bermuda”), all of which are under common control. The Company charges a fee for these services based upon terms that are similar with those the Company would charge unrelated parties.

Included in net investment income are fees paid to BMO Global Asset Management of $580,178 (2019: $758,341).

Other than those items disclosed elsewhere in these financial statements, transactions with related parties are summarized as follows:

| Operating expenses (income) | 2020 | 2019 |
|---|---|---|
| BMO | $ 246,662 | 458,514 |
| Finco V | (38,882) | (38,882) |
| BMO (Bermuda) | (47,740) | (47,740) |
| BMOIL | (36,565) | (36,565) |
| BOMBL | (332,800) | (332,800) |
| | $ (209,325) | 2,527 |

The following tables show balances with related parties:

| | 2020 | | |
|---|---|---|---|
| | Cash | Other assets | Accounts payable and other liabilities |
| BMO | $ 68,900,271 | - | 20,410 |
| BOMBL | - | 5,938 | - |
| BMOIL | - | 909 | - |
| BMO Bermuda | - | - | 2,765 |
| Finco V | - | 82,648 | - |
| BMO Global Asset Management | - | - | 38,624 |
| | $ 68,900,271 | 89,495 | 61,799 |

| | 2019 | | |
|---|---|---|---|
| | Cash | Other assets | Accounts payable and other liabilities |
| BMO | $ 8,448,230 | - | 26,477 |
| BOMBL | - | 19,464 | - |
| BMOIL | - | 47,650 | - |
| BMO Bermuda | - | 2,323 | - |
| Finco V | - | 677 | - |
| BMO Global Asset Management | - | - | 60,175 |
| | $ 8,448,230 | 70,114 | 86,652 |

## Key Management Personnel

Related parties include key management personnel and their close family members. Close family members include spouses, common-law partners and dependent minors. Key management personnel are defined as those persons having authority and responsibility for planning, directing and controlling the Company's activities, directly or indirectly. Senior management of the Company plan, direct and control the day-to-day business activities. These business activities are carried out within the strategic framework established by the executive of the ultimate parent, the Bank of Montreal. Thus, the Company's key management personnel have been determined to be the Bank's Board of Directors and certain key executives (together "key management personnel") as they provide overall direction and oversight for the Bank. The key management personnel are ultimately responsible for all material decisions of the Bank. The key management personnel are also responsible for establishing the overall strategic direction of the consolidated Bank, both domestically and internationally and, in that regard, establish such parameters for the consolidated Bank within which the Board of Directors and management of each subsidiary in the consolidated Bank exercise their discretion to make decisions concerning the strategic direction and day to day management of the operations of the particular subsidiary. The Bank's Directors oversee the management of the business and provide stewardship.

### Key Management Personnel Compensation

The following table presents the compensation of the Bank's key management personnel.

| (Canadian $ in thousands) | 2020 | 2019 |
|---|---|---|
| Base salary and initiatives | $ 19,775 | 22,068 |
| Post-employment benefits | 2,518 | 2,061 |
| Share-based payments[1] | 32,226 | 43,204 |
| | $ 54,519 | 67,333 |

[1] Amounts included in share-based payments are the fair values of awards granted in the year.

The Bank offers senior executives market interest rates on credit card balances, a fee-based subsidy on annual credit card fees, and a select suite of customer loan and mortgage products at rates normally accorded to preferred customers. At October 31, 2020, loans to key management personnel totaled $19.5 million ($20.6 million in 2019). There are no provisions for credit losses related to these amounts as at October 31, 2020 and 2019.

The Bank's Directors receive a specified amount of their annual retainers in deferred stock units. Until a director's shareholdings (including deferred stock units) are eight times greater than their annual retainer, they are required to take 100% of their annual retainer and other fees in the form of either Bank common shares or deferred stock units. They may elect to receive the remainder of such retainer fees and other remuneration in cash, common shares or deferred stock units.

## Note 23: Letters of Credit

The Company had facilities for letters of credit totaling $85,238,400 (2019: $184,310,000) of which $51,322,351 (2019: $59,160,803) was utilized. These letters of credit relate to certain reinsurance treaties and are unsecured. The Bank provided and issued $65,260,650 and $51,322,351 respectively (2019: $164,562,500 and $59,160,703) of the total facilities.

## Note 24: Solvency Margin

The Company is required by the Exempt Insurance Act of Barbados to comply with certain solvency criteria. At October 31, 2020, the Company's solvency margin exceeded the required minimum.

## Note 25: Taxation

As a grandfathered entity, the Company is subject to taxation in accordance with Section 29 of the Exempt Insurance Act at a rate of eight percent on the first US$125,000 of taxable income and zero percent on taxable income in excess of US$125,000. At the earlier of the date on which the Company opts to transition to the provisions of the Insurance Act and July 1, 2021 the Company will be subject to taxation at a rate of two percent of taxable income.

## Note 26: Reinsurance Security Agreement

Effective October 1, 2005, the Company assumed reinsurance risks from a Canadian primary insurer (the "Insurer") on a full coinsurance basis. The Company and the Insurer established a Reinsurance Security Agreement in respect of this reinsurance arrangement. In accordance with the Office of the Superintendent of Financial Institutions Canada, ("OSFI") guidelines and requirements, the Company is required to grant to the Insurer a security interest in a minimum prescribed amount of assets with a Custodian ("the Collateral Account"); in particular, at least equal to 100% of the actuarial liabilities in respect of the policies ceded by the Insurer. Also, the Company and the Insurer have agreed that the Company will maintain additional assets in the Collateral Account in an amount equal to the maximum eligible deposits for unregistered reinsurance permissible under Section 6.8.1 of the Life Insurance Capital Adequacy Test requirement, as defined by OSFI and determined by the Insurer, in respect of the policies ceded by the Insurer.

As at the effective date of the Balance Sheet, the actuarial liabilities disclosed in Note 15 included an amount of $45,307,679 (2019: $45,013,895) in respect of the policies ceded by the Insurer that are associated with the Collateral Account. The market value of the assets in the Collateral Account as of October 31, 2020 was $86,265,414 (2019: $85,040,408).

## Note 27: Pension Plan

The Company operates an annuity pension scheme for its employees in the form of a defined contribution pension plan. Obligations for contributions to the plan are recognized as an expense in the Statement of Income and Comprehensive Income as incurred. The annual premiums paid to the defined contribution pension plan and charged to operations during the year amounted to $50,872 (2019: $71,603), net of anniversary credits.