Annual Report 2009

Striving for excellence

Who we are

We are the leading provider of property and casualty (P&C) insurance in Canada, insuring more than four million individuals and businesses through our insurance subsidiaries. With an estimated 11% market share, we are the largest private sector provider of P&C insurance in Ontario, Quebec, Alberta and Nova Scotia. We distribute insurance through brokers under the Intact Insurance, Grey Power and Canada Brokerlink brands, and direct-to-consumers through belairdirect.

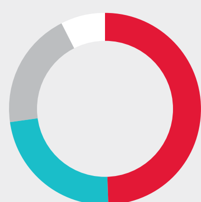
We also manage our own investment portfolio with approximately $8 billion in invested assets.

Financial highlights

(in millions of Canadian dollars, except as noted)

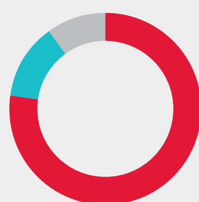
	2009	2008	2007	2006	2005	2004
Consolidated performance						
Written insured risks (thousands)	**4,603.6**	4,601.5	4,679.9	4,565.1	4,417.9	3,857.6
Direct premiums written (excluding pools)	**4,274.9**	4,145.5	4,108.6	3,993.6	3,905.9	3,501.4
Net premiums earned	**4,055.4**	4,039.4	3,932.0	3,826.6	3,840.2	3,364.6
Net claims and general expenses	**4,043.0**	3,972.4	3,723.2	3,422.8	3,302.5	2,894.6
Combined ratio (excluding MYA)	**98.7%**	97.1%	95.2%	89.4%	86.0%	86.0%
Interest and dividend income, net of expenses	**292.7**	328.8	344.8	321.3	307.5	249.1
Net gains on invested assets and other gains	**(172.5)**	(288.0)	73.6	193.5	223.5	132.4
Corporate and distribution income	**7.2**	15.6	44.3	33.4	22.3	4.3
Income before income taxes	**139.8**	123.6	671.6	952.0	1,091.0	855.8
Effective tax rate	**9.4%**	(3.8%)	24.3%	30.9%	28.3%	27.1%
Net operating income	**281.6**	360.7	457.0	530.5	612.3	532.3
Net income	**126.7**	128.2	508.3	658.1	781.8	624.2
Earnings per share ($)	**1.06**	1.05	4.01	4.92	5.85	6.51
Average number of shares outstanding (millions)	**119.9**	122.0	126.7	133.7	133.5	95.8
Book value per share ($)	**24.88**	21.96	25.48	25.58	21.63	15.40
Return on equity	**4.5%**	4.4%	15.4%	20.8%	31.6%	40.9%

Direct premiums written by business line
(excluding pools, %)



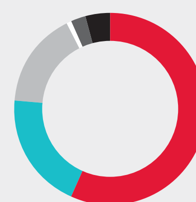
Personal auto	49.7%
Personal property	23.3%
Commercial P&C	19.5%
Commercial auto	7.5%

Direct premiums written by distribution channel
(excluding pools, %)



Brokers	77.4%
belairdirect	12.8%
Affiliated distribution network brokerages	9.8%

Investment asset mix
(% of fair value)



Fixed income securities	56.8%
Preferred shares	19.6%
Common shares	16.3%
Cash and cash equivalents	0.7%
Short-term notes	2.6%
Other	4.0%

Dear fellow shareholders,

2009 was a defining year in the history of our company. Not only did we become a 100% public Canadian company with the ability to chart our own path forward, shortly afterwards we also successfully launched our new brand into the marketplace. Along with these significant changes, we managed to increase our employee engagement scores by eight points in the last two years and continued to build on our leadership, scale, discipline and strong financial position – all this during a time that has been described as one of the worst economic downturns since the 1930s. No small feat by any standard, and a testament to the endurance of our company and the passion, tenacity and expertise of our people as we continue to strive for excellence.

Leveraging our brands

Our new Intact brand is the external representation of the company that each one of our 7,000 employees is helping us to become – a company recognized for putting customers at the centre of everything we do. This reenergized customer focus is the cornerstone of our quest for excellence. We've transformed our claims operations and improved service nationally by expanding and networking all of our call centres, extending our service hours and improving our response time to customers. These efforts are already paying off in increased customer and broker satisfaction. We were also recognized in the J.D. Power survey of car insurance companies, with Intact Insurance ranked the top broker distribution company and belairdirect taking the overall number one ranking in customer satisfaction.

We are committed to continue building on our customer-driven efforts, an important part of which is the unique experience and choice we offer consumers on how they can shop for our products through our distinct brands. Intact Insurance is available for consumers who want to deal with a broker, while Grey Power and belairdirect give them the option of buying our products directly by phone and on the Internet. Our distribution strategy is to be available to customers whenever and wherever they want us to be – a multi-channel approach that allows us to respond to trends in consumer demographics and technology usage, while also providing us with strong organic growth potential.

The year in review

While 2009 has certainly been eventful, it has been a successful one in my view. We posted direct written premiums of $4.3 billion with the pace of our growth accelerating throughout the year. Our underwriting results have also continued to outperform the industry with a favourable combined ratio of 98.7% in 2009 and we maintained our strong capital position with approximately $850 million of excess capital – despite significant challenges in the external environment. Last year also brought meaningful improvement in our personal property business, one of our key objectives for the year, with it returning to profitability in the fourth quarter under better weather conditions and solid traction on our home insurance action plan.

Our $8 billion investment portfolio also generated healthy returns with more than $300 million of investment income. And despite the disruption in the financial markets, our excess capital position continued to grow. We also took advantage of the historically low interest rate environment with the issue of $400 million in medium-term notes, bolstering our financial strength while providing additional strategic flexibility. But we do not intend to sit on idle excess capital, as evidenced by our 6.3% dividend increase and the initiation of our share buyback program, and our first priority remains finding the right acquisition opportunity.

Last year also brought positive developments on the regulatory front, with the Alberta and Nova Scotia courts upholding their minor injury caps and the introduction of new auto reforms in Ontario signalling a positive development in what has been a challenging environment. The recent reforms will provide Ontario drivers with greater choice, while creating a more stable cost environment for the industry.

Industry conditions are improving

Over the last few years, the industry in general has been affected by higher claims, pressure on capital and now historically low investment yields. Due to a combination of these factors, personal insurance premiums are increasing, and market indications suggest that business rates are beginning to firm up. In an environment where a number of insurers are forced to reduce capacity as they re-price their business, we have a competitive advantage in our operational and financial strength. This advantage provides the opportunity for us to grow more rapidly while maintaining adequate price margins.

1,800 brokers strong

Supporting us in our growth are over 1,800 brokers who are also well-positioned to thrive in the current environment. During times of uncertainty, consumers place even more value on the advice and personalized service brokers offer. Which is why brokers have always been – and will continue to be – critical to our success. We strongly believe that when they fully leverage their strengths, there is no substitute for the service brokers provide consumers. This is why one of our key priorities is to continue to support brokers in growing their businesses through quality products and services, simplified processes to help them meet their customers' expectations and financing solutions that are tailored to their needs.

Looking forward

While the industry will likely face further challenges in 2010, we believe that even in times of adversity, opportunities are created for leaders in any industry. We have been closely watching consumer online trends and the demographic shifts occurring in the Canadian population which we believe will continue to create further opportunities for growth. In addition, our operational and financial strengths have proven the sustainability and resilience of our business in the Canadian P&C insurance market – particularly over the last two years. As economic conditions continue to improve, we are confident in the long-term earnings power of our business and the growth opportunities that we see in the near- to mid-term.

I am also proud to say that in 2009, Intact remained committed to our communities. Our employees continued to show tremendous support for the United Way, and together we raised over $1 million. We've also continued to support employee volunteerism and giving through our volunteer and donation match program. The transition to Intact last year also gave us the opportunity to take a closer look at our approach to social responsibility and we are currently refocusing our strategy so that we can better support meaningful, positive, and sustainable change in the communities where we operate.

In closing, I would like to personally thank our Board of Directors whose insight and guidance have helped us successfully navigate the sometimes uncertain terrain of the last year. I would also like to thank all of our employees, who in a year of incredible challenges and change, never took their eyes off the horizon, and in their continuous strive for excellence, helped us deliver a year we can all be proud of.

Charles Brindamour
President and Chief Executive Officer

Message from the Chairman

2009 was a rewarding year for the members of your Board, as we oversaw management's efforts in engineering the most significant transformation of your company in its history. Back in February of last year, your company entered into a new era when it became a widely-held publicly traded company, following the completion of a $2.2 billion secondary offering, one of the largest transactions of its kind in Canada.

This was quite an accomplishment considering the turmoil and the volatility of the financial markets at the time. I would like to thank all of our shareholders who showed their confidence in our company by either acquiring an initial equity stake or increasing their ownership position. As the discussions surrounding these transactions were taking place between management and our then majority shareholder, your Board was kept fully abreast of the potential developments and their impact on your company; and my colleagues and I ensured that the highest principles of corporate governance were applied and that the interests of our minority shareholders were fully taken into consideration and protected. The fact that your company became, as a result of the transaction, a 100% Canadian-listed company with a strong balance sheet speaks volumes about the vision that management and your Board had about Intact and its future.

As your company was also getting ready to adopt a new name to reflect its customer orientation, launch a new brand and make a new promise to its customers, your Board was actively consulted by management, and we provided counsel and advice.

Becoming a widely-held company provided the management team and the Board the opportunity to review exhaustively the company's corporate governance and compliance practices and re-evaluate its internal audit processes. This ensured that our policies, practices and processes were aligned with the status of your company and reflected the best practices adopted by publicly-held Canadian companies.

As part of this review, your Board adopted a new Code of Conduct, also known as "Living Our Values." This document is organized around the five core values that guide the actions of all of us at Intact – integrity, respect, customer driven, excellence and social responsibility. It also sets out the commitment of all Board members and employees to act with the highest ethical standards.

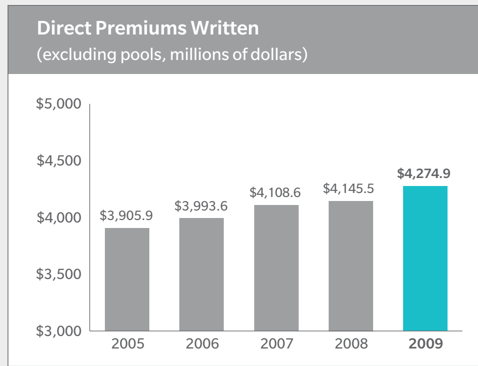
While we are looking to the future of your company with confidence, we are sorry to see that two of your valued Board members will not join us in this journey, having reached the retirement age we have set for our members. Mr. Ivan E.H. Duvar, who has been associated with our company for more than 25 years, either as a Board member of Halifax Insurance, NN Life, ING Canada or Intact Financial Corporation, as well as Mr. Robert Normand, who has served as a director of our affiliates for the last 10 years and a member of your Board since 2004, are retiring and will not seek re-election at our next Annual General Meeting. Both of them have served Intact and your Board with distinction and I would like to thank them for their invaluable counsel, guidance and contribution.

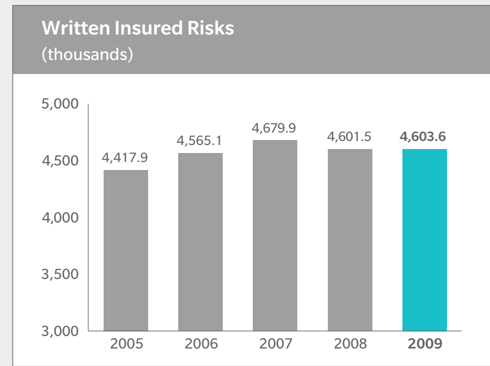
On behalf of the Board of Directors, I also want to congratulate all our employees for having wholeheartedly embraced our transformation and thank them for their dedication and contribution to our success. I am honoured to serve as your Chair and would like to re-iterate the commitment of all your Board members to continue counselling and supporting the outstanding management team that is aptly guiding Intact on an exciting course.

Claude Dussault
Chairman of the Board

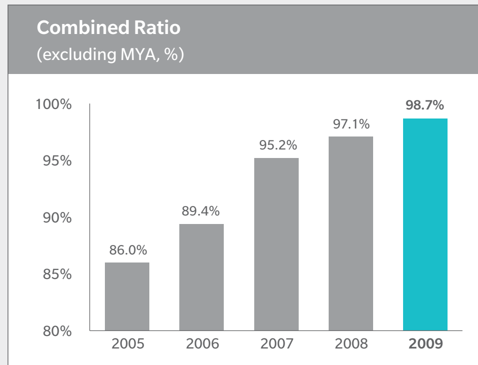
Key Performance Measures

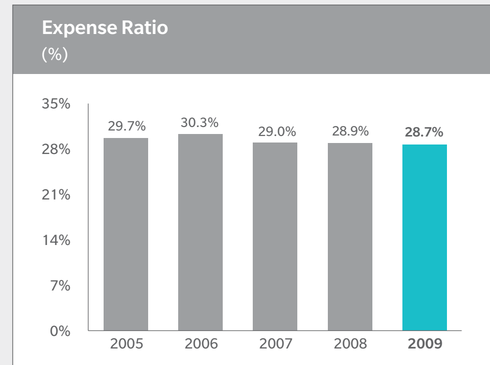
Growth



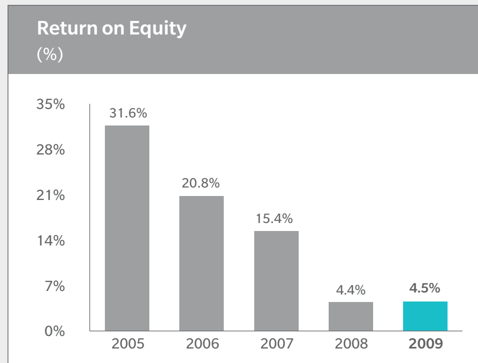


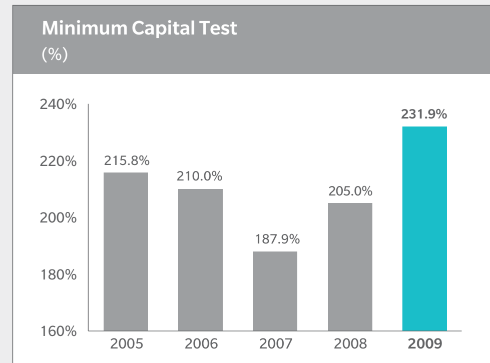
Performance and execution

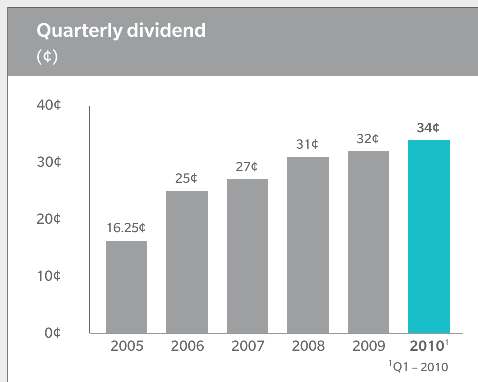


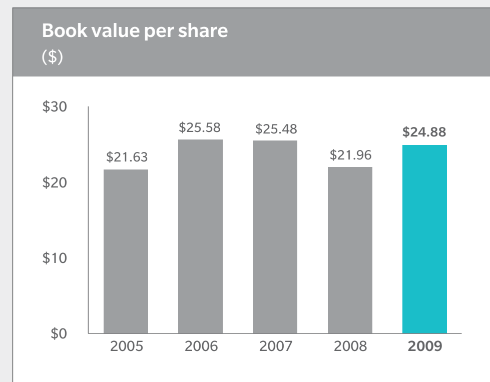


Capital management









Intact Financial Corporation
Management's Discussion and Analysis
For the year ended December 31, 2009

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Introduction

March 26, 2010

The following Management's Discussion and Analysis ("MD&A"), which was approved by the Board of Directors for the year ended December 31, 2009, is intended to enable the reader to assess the company's results of operations and financial conditions for the three- and twelve-month periods ended December 31, 2009, compared to the corresponding periods in 2008. It should be read in conjunction with the company's consolidated financial statements and accompanying notes for its fiscal year ended December 31, 2009.

The company uses both generally accepted accounting principles ("GAAP") and certain non-GAAP measures to assess performance. Non-GAAP measures do not have any standardized meaning prescribed by GAAP and are unlikely to be comparable to any similar measures presented by other companies. Intact Financial Corporation analyzes performance based on underwriting ratios such as combined, general expenses and claims ratios as well as other performance measures generally excluding the market yield adjustment ("MYA") to claims liabilities. These measures are defined in the company's glossary which is included in the company's Annual Financial Report and posted on the Intact Financial Corporation web site at www.Intactfc.com. Click on "Investor Relations" and "Glossary" on the left navigation bar.

Forward-looking statements

This document contains forward-looking statements that involve risks and uncertainties. The company's actual results could differ materially from these forward-looking statements as a result of various factors, including those discussed hereinafter or in the company's 2009 Annual Information Form. Please read the cautionary note at the end of this document.

Certain totals, subtotals and percentages may not agree due to rounding. Additional information about Intact Financial Corporation, including the Annual Information Form, may be found online on SEDAR at www.sedar.com. A change column has been provided for convenience showing the variation between the current period and the prior period. Not applicable (n/a) is used to indicate that the current and prior year figures are not comparable or if the percentage change exceeds 1,000%.

Notes:

All references to direct premiums written in this MD&A exclude underwriting pools, unless otherwise noted.

All references to "excess capital" in this MD&A include excess capital in the P&C insurance subsidiaries at 170% minimum capital test ("MCT") plus liquid assets in the holding company, unless otherwise noted.

"IFC", "Intact", "the company," "we" and "our" are terms used throughout the document to refer to Intact Financial Corporation and its subsidiaries.

In the captions used in this MD&A, words such as "Income", "Earnings" and "Gains" will always be placed before the words "Expense", "Loss" and "Losses".

SECTION 1 – Intact Financial Corporation

1.1 Overview of the business

Intact Financial Corporation ("IFC") is the largest provider of automobile, home and business insurance in Canada insuring approximately four million individuals and businesses across Canada. Overall, the company has an approximate 11% market share and is the leading private sector property and casualty ("P&C") insurer in Ontario, Quebec, Alberta and Nova Scotia. IFC distributes insurance through brokers under Intact Insurance and Grey Power brands, and direct-to-consumers through belairdirect. At December 31, 2009, IFC and its insurance subsidiaries had an $8.1 billion portfolio of cash and invested assets, managed by the company's investment management subsidiary.

Personal insurance

IFC is the largest personal auto and property insurer in Canada. The market as a whole is fragmented – the top five P&C insurers represent less than 40% of annual premiums in Canada. In automobile insurance, the company is more than 35% larger than the second largest P&C insurer in Canada and about 65% larger than the third ranking P&C insurer, based on the most recently reported industry data for 2008 which includes both personal and commercial auto. In personal property, the gap is even larger – IFC is approximately 43% larger than the second largest insurer and about 90% larger than the number three insurer in the Canadian market. Though the company holds the number one position in both segments of personal insurance, its estimated market share is only 14% in both automobile and property, demonstrating the growth potential of this segment of the business.

Commercial insurance

IFC is also one of the largest players in commercial insurance in Canada with a significant share of the small- to medium-size commercial segment. These two segments make up approximately 90% of the company's commercial premiums. Small and medium-sized commercial accounts have been more profitable over time and market pricing is less volatile than large commercial business.

Investment management

IFC actively manages its $8.1 billion portfolio of cash and invested assets to generate superior after-tax returns while balancing capital preservation and risk. The company invests mainly in high-quality Canadian securities that are publicly traded. See section 6.3 for more information on the quality and mix of the company's portfolio of invested assets.

1.2 Critical capabilities

IFC has several critical capabilities which have enabled the company to sustain a performance advantage over other P&C insurers in Canada. These critical capabilities are described in the table below:

Capability	Description
Significant scale advantage	The key benefit of scale is IFC's large database of customer and claims information that enables the company to identify trends in claims and more accurately model the risk of each policy. IFC also uses its scale to negotiate preferred terms with suppliers, priority service on repairs, quality guarantees on workmanship and lower material costs.
Underwriting discipline/ pricing sophistication	The company has superior underwriting expertise and proprietary segmentation models used to price risks. These models are continuously being refined to create a pricing advantage over competitors and identify certain segments of the market that are more profitable than others. The company's objective is to establish pricing that 1) will continue to attract new business, 2) is fair for the customer; and, 3) is profitable.
Expertise in claims management	Substantially all of IFC's claims are handled in-house. By managing claims in-house, claims are settled faster and less expensively, and a more consistent service experience is created for the customer.
Product innovation	IFC is continuously developing new products to attract and retain customers. IFC has a history of product innovation such as its Claims Service Guarantee and Responsible Driver Guarantee which reflect the company's customer-driven strategy. IFC has also worked aggressively to expand its customer loss prevention services in commercial lines.
Proven acquisition strategy	IFC is an active acquirer with 11 successful acquisitions since 1988. The company's strategy is three-fold: – acquire businesses that fit existing business lines; – integrate those businesses into the company's technology infrastructure; – increase the profitability of the acquired book of business through pricing, underwriting expertise and claims.
Solid investment returns	IFC's investment strategy is to generate solid after-tax returns while preserving capital and diversifying risk. The company's $8.1 billion portfolio (including cash and cash equivalents) is mainly comprised of Canadian securities, including high-quality fixed income securities as well as common shares of large-cap companies and preferred shares that pay dividends.
Multi-channel growth model	The company has a multi-channel distribution strategy including broker and direct-to-consumer brands. This strategy maximizes growth in the market and enables the company to appeal to different customer preferences.
Broker relationships	The broker channel represents approximately 77.4% of annual direct written premiums. IFC has more than 1,800 broker relationships across Canada for customers that prefer the highly-personalized, community-based service that insurance brokers provide. IFC provides a variety of services including technology, sales training and financing to brokers to enable them to continue to grow and expand their businesses.

1.3 Key performance indicators

IFC's key performance indicators are defined in the table below. Certain key performance indicators are considered non-GAAP measures. Non-GAAP measures do not have any standardized meaning prescribed by GAAP and may not be comparable to similar measures used by other companies in the company's industry.

Category	Indicator
Growth	**Direct premiums written** The total premiums written during a specified period (excluding pools).
	Written insured risks The number of vehicles in automobile insurance, the number of premises in personal property insurance and the number of policies in commercial insurance (excluding commercial auto insurance).
Profitability	**Net underwriting income** Net premiums earned less net claims incurred, commissions, premium taxes and general expenses (excluding MYA).
	Market-based yield Annualized total pre-tax dividend and interest income (before expenses) divided by the average fair values of equity and fixed income securities held during the reporting period.
	Net operating income After-tax net income from underwriting activities, corporate and distribution activities and interest and dividend income from invested assets.
	Operating return on equity Net operating income for the last 12-months divided by the average shareholders' equity (excluding accumulated other comprehensive income) over the same 12-month period. The average shareholders' equity is the mean of shareholders' equity at the beginning and the end of the period.
	Net income As reported in the Consolidated statements of income.
Performance and execution	**Claims ratio** Claims incurred, net of reinsurance, during a defined period and expressed as a percentage of net premiums earned for the same period.
	Expense ratio Underwriting expenses including commissions, premium taxes and all general and administrative expenses, incurred in underwriting income during a defined period and expressed as a percentage of net premiums earned for the same period.
	Combined ratio The sum of the claims ratio and the expense ratio. A combined ratio below 100.0% indicates a profitable underwriting result. A combined ratio over 100.0% indicates an unprofitable underwriting result.
Capital management	**Return on equity (ROE)** Net income for a 12-month period divided by the average shareholders' equity over the same 12-month period. Net income and shareholders' equity are determined in accordance with GAAP. The average shareholders' equity is the mean of shareholders' equity at the beginning and end of the period.
	Book value per share Shareholders' equity divided by the number of outstanding common shares at the same date. Shareholders' equity is determined in accordance with GAAP.
	Minimum Capital Test (MCT) Ratio of available capital to required capital. The regulatory minimum required capital is 150%. The company has an internal operating target of 170%.
	Excess Capital Excess capital in the P&C insurance subsidiaries at 170% MCT plus excess liquid assets in the holding company and other subsidiaries.

1.4 Seasonality of the business

The property and casualty insurance business is seasonal in nature. While net premiums earned are generally stable from quarter to quarter, net underwriting income is typically highest in the second quarter of each year. This mainly is driven by weather conditions, reflected in the seasonal index below. The seasonal indicator is a non-GAAP measure which represents the ratio of the quarterly combined ratio to the annual combined ratio, excluding the MYA.

TABLE 1 – SEASONAL INDICATOR

	2009	2008	2007	2006	2005	2004	Six-year average
Q1	**1.00**	1.03	1.01	1.02	1.02	1.10	1.03
Q2	**0.97**	0.98	0.99	0.93	0.94	0.92	0.96
Q3	**1.07**	0.97	1.02	1.01	1.02	0.98	1.01
Q4	**0.96**	1.02	0.98	1.05	1.01	1.01	1.00

SECTION 2 – Industry outlook

2.1 Canadian property and casualty insurance industry 12-month outlook

IFC is well-positioned to continue to outperform the P&C insurance industry in the current environment due to its significant scale, pricing and underwriting discipline, prudent investment and capital management practices, and strong financial position.

	P&C insurance industry	IFC's response
Pricing and claims environment (12-month outlook)	• Personal auto premiums are increasing due to medical cost inflation in Ontario. To address this issue, the Ontario Government announced proposed changes to the Ontario auto reforms in November 2009 which are expected to become effective in the summer of 2010. • Personal property premiums are increasing due to severe storms and water-related losses which are now the leading cause of home insurance claims. • In commercial lines, there are clear signs that pricing is firming up, particularly in Ontario. IFC expects that conditions will develop similarly across Canada over time. • While the market is still very competitive, a number of P&C companies are retrenching across all lines of business due to the deterioration in underwriting margins over the last couple of years.	• Maintaining pricing discipline and commitment to adequate margins: – IFC has increased personal auto new business rates in Ontario by 19.0% since September 2007 to address higher accident benefit costs in the province. – In commercial lines, IFC continues to maintain discipline to be ready to take advantage as the market turns. • IFC's home insurance action plan is gaining traction with the objective of achieving a 10–15% combined ratio improvement over 12–18 months: – Rate adjustments and enhanced segmentation – Greater efficiency in claims management – Loss prevention and education – Product review • As a result of IFC's disciplined pricing strategy, the company is well-positioned to grow organically as other companies reduce their appetite for new business and market pricing becomes less competitive.
Capital markets	• Capital market weakness over the last year has resulted in investment losses, generally higher borrowing costs and diminished excess capital levels across the industry. • Lower industry capital levels and investment yields could influence higher premiums across the industry.	• Strong financial position with $858.7 million in excess capital (over an MCT of 170%). • MCT ratio of 231.9%; up 12.7 percentage points from the third quarter of 2009. • $8.1 billion cash and investment portfolio is largely Canadian with minimal US exposure and no leveraged investments. • The market-based yield of the investment portfolio remains healthy at 4.5%.

SECTION 3 – Overview of consolidated performance

Fourth quarter highlights

– Premium growth accelerated to 4.5%
– Net operating income per share up 30.2% on strong underwriting results
– Combined ratio of 94.6% driven by improvement in personal lines
– Book value per share up 13.3% in 2009 with excess capital of $858.7 million at year end

3.1 Consolidated financial results

TABLE 2 – COMPONENTS OF NET INCOME

(in millions of dollars, except as noted)	Q4 2009	Q4 2008	Change	2009	2008	Change
Direct premiums written (excluding pools)	1,011.4	968.2	4.5%	4,274.9	4,145.5	3.1%
Net underwriting income (excluding MYA) (table 5)	56.0	11.0	409.1%	54.0	117.0	(53.8)%
Combined ratio (excluding MYA)	94.6%	98.9%	(4.3) pts	98.7%	97.1%	1.6 pts
Interest and dividend income, net of expenses (table 11)	77.3	78.3	(1.3%)	292.7	328.8	(11.0)%
Total gains (losses) excluding held for trading ("HFT") fixed income securities (table 12)	4.6	(194.2)	n/a	(169.5)	(316.4)	n/a
Interest expense on debt outstanding	4.4	–	n/a	5.6	–	n/a
Income (loss) before income taxes	125.4	(108.2)	n/a	139.8	123.6	13.1%
Income tax expense (benefit)	28.7	(44.1)	n/a	13.1	(4.6)	n/a
Effective income tax rate	22.9%	40.7%	(17.8) pts	9.4%	(3.8)%	13.2 pts
Net income (loss)	96.7	(64.1)	n/a	126.7	128.2	(1.2)%
Net operating income (table 22)	98.1	75.1	30.6%	281.6	360.7	(21.9)%
Earnings per share ("EPS") – basic and diluted (dollars)	0.81	(0.53)	n/a	1.06	1.05	1.0%
Net operating income per share (dollars)	0.82	0.63	30.2%	2.35	2.96	(20.6)%
Return on equity ("ROE") for the last 12 months				4.5%	4.4%	0.1 pts
Operating return on equity for the last 12 months				9.2%	11.3%	(2.1) pts
Book value per share (dollars)				24.88	21.96	13.3%

3.2 Explanation of consolidated financial results

TABLE 3 – CHANGES IN PRE-TAX OPERATING INCOME (YEAR-OVER-YEAR)

(in millions of dollars)	Q4 2009	2009
Pre-tax operating income, as reported in 2008	91.3	461.4
Change in net underwriting income excluding MYA:		
Change in favourable prior year claims development	13.8	(25.2)
Change in current accident year net underwriting income	13.3	(39.9)
Change in catastrophe losses[1]	22.8	(0.5)
Change in income from Facility Association	(4.8)	2.6
Total change in net underwriting income excluding MYA	45.1	(63.0)
Change in interest and dividend income, net of expenses	(1.0)	(36.1)
Change in corporate and distribution	(9.5)	(8.4)
Total change in pre-tax operating income	34.6	(107.5)
Pre-**tax operating income, as reported in 2009**	125.9	353.9

1 Pre-tax operating income is a non-GAAP measure. Catastrophe claims are defined as a single event resulting in $5.0 million or more in aggregate claims.

TABLE 4 – CHANGES IN INCOME BEFORE INCOME TAXES (YEAR-OVER-YEAR)

(in millions of dollars)	Q4 2009	2009
Income before income taxes, as reported in 2008	(108.2)	123.6
Change in net gains on invested assets and other gains excluding HFT fixed income securities (table 12)	198.8	146.8
Change in pre-tax operating income (table 3)	34.6	(107.5)
Change in market yield effect (table 21)	0.2	(23.1)
Income before income taxes, as reported in 2009	125.4	139.8
Income tax	(28.7)	(13.1)
Net income as reported in 2009	96.7	126.7

3.3 Net underwriting income

TABLE 5 – NET PREMIUMS EARNED, CLAIMS AND GENERAL EXPENSES

(in millions of dollars, except as noted)	Q4 2009	Q4 2008	Change	2009	2008	Change
Net premiums earned	1,036.5	1,019.2	1.7%	4,055.4	4,039.4	0.4%
Net claims (excluding MYA):						
Current year claims	740.8	743.8	(0.4)%	2,844.0	2,790.4	1.9%
Current year catastrophes (recoveries) losses	(1.2)	21.6	(105.6)%	115.3	114.8	0.4%
(Favourable) prior year claims development	(66.0)	(52.2)	n/a	(123.7)	(148.9)	n/a
Total net claims	673.6	713.2	(5.6)%	2,835.6	2,756.3	2.9%
Commissions, net	145.5	150.2	(3.1)%	573.2	577.3	(0.7)%
Premium taxes, net	35.8	35.4	1.1%	140.4	140.4	–
General expenses, net	125.5	109.5	14.6%	452.2	448.4	0.8%
Total underwriting expenses	306.9	295.1	4.0%	1,165.8	1,166.1	0.0%
Total net underwriting income (excluding MYA)	56.0	11.0	409.1%	54.0	117.0	(53.8)%

TABLE 6 – UNDERWRITING RATIOS (EXCLUDING MYA)

	Q4 2009	Q4 2008	Change	2009	2008	Change
Claims ratio	65.0%	70.0%	(5.0) pts	70.0%	68.2%	1.8 pts
Expense ratio	29.6%	28.9%	0.7 pts	28.7%	28.9%	(0.2) pts
Combined ratio	94.6%	98.9%	(4.3) pts	98.7%	97.1%	1.6 pts

Fourth quarter 2009

Direct written premiums were up 4.5% with accelerated growth across key lines of business throughout 2009. In personal lines, premiums grew 5.2% mainly due to higher rates and insured amounts. Commercial lines also gained momentum through the year with moderate single-digit premium growth in the fourth quarter reflecting unit growth and net increases in rates. Conditions are improving as premiums in personal lines are increasing and aggressive industry commercial pricing behaviour has begun to ease, particularly in certain geographic areas and in unprofitable business segments (see section 2, Industry outlook).

IFC's top-line momentum in 2009 reflects the success of the company's organic growth strategies as some competitors have started to reduce their appetite for growth and raise rates on under-priced risks. The change in the environment has been caused by three broad factors which influence both the availability and price of P&C insurance. These include 1) the deterioration in industry underwriting margins due to higher claims and under-pricing, 2) generally lower investment yields and 3) pressure on capital due to the financial crisis. To mitigate these factors, IFC has focused on protecting its strong financial position and ensuring that policies are priced adequately. As a result of this discipline, the company has maintained a healthy insurance portfolio with underwriting results that continued to exceed the Canadian industry into 2009, based on the most recent information, while continuing to grow.

IFC's combined ratio was strong at 94.6%, driven by improved results in personal lines. There were a number of positive developments in the fourth quarter including a return to profitability in our home insurance business, which was a key focus area for IFC in 2009. The combined ratio in that segment was robust at 87.8% reflecting a combination of better weather conditions, as well as continued traction on the home insurance action plan. In personal auto, underwriting performance also improved significantly with a combined ratio of 98.0% compared to 102.9% in the same quarter of last year. The improvement reflects better current accident year results and the release of provisions associated with minor injury cap reforms which had a $22.4 million impact on underwriting income. These positive results were partly offset by losses from industry risk sharing pools.

In commercial lines, auto results were excellent with a 70.4% combined ratio compared to 91.6% in the same quarter last year due better underwriting results in the current accident year as well as favourable prior year development. In commercial P&C, IFC has also had a consistent track record of strong profitability. However, 2009 results were affected by a number of large fires and the short term impact of some commercial group accounts which have been cancelled. Excluding these group accounts, commercial P&C was profitable with a combined ratio of 98.6%. IFC began accelerating commercial P&C rate increases in late 2009 with continued unit growth.

On the investment side, interest and dividend income, net of expenses, remained robust at $77.3 million with modest net investment gains excluding HFT fixed income securities, on the backdrop of healthier capital market conditions. 2008 results were adversely affected by significant impairments as the Canadian equity market reached one of its lowest points in the financial crisis toward the end of last year. As conditions improved in 2009, the market value of the company's invested assets increased substantially and the common equity and fixed income portfolios ended the year in an unrealized gain position.

The company's financial position is very strong with $858.7 million in excess capital and an MCT of 231.9%, up 12.7 points from the end of the third quarter. The increases reflect proceeds of $150 million from the medium term note issue in November 2009 and an increase in the market value of IFC's investment portfolio (see section 3.4, Recent events).

Full year 2009

Direct written premiums increased 3.1% as the growth rate accelerated in each consecutive quarter. The quality of IFC's insurance portfolio continues to be very healthy and industry pricing is improving with premiums increasing in personal lines and better dynamics in commercial lines. With IFC's operational and financial strengths, the company is well-positioned to grow organically while taking advantage of more favourable competitive conditions.

Underwriting results were healthy with an overall combined ratio of 98.7% versus 97.1% last year. Compared to 2008, performance improved in every line of business except commercial P&C. In the company's largest business, personal auto, the combined ratio was strong at 94.9%, improving 1.0 point year-over-year due to a lower expense ratio and the release of provisions that were set up in prior years related to minor injury cap reforms, discussed previously. In personal property, the magnitude of water losses continues to pose a challenge; however, despite severe summer storms, the combined ratio improved 4.6 points to 109.0%. IFC made further progress on the home insurance action plan as the business produced a profit in the last quarter under better weather conditions. On the commercial side, auto results were excellent with a combined ratio of 79.8% compared to 87.2% in 2008. Commercial P&C has historically been very profitable but in 2009 the combined ratio was 104.1% due to a small number of large fire claims and the short-term impact of unprofitable commercial group accounts which IFC cancelled.

Interest and dividend income, net of expenses, remained healthy at $292.7 million despite changes in the asset mix in late 2008 to help protect the company's strong financial position through the peak of market volatility. Due to other de-risking steps and factors fully described in section 6.2, the company recorded $169.5 million in investment losses excluding HFT bonds (see table 12). Overall, the investment portfolio grew $1.5 billion to $8.1 billion during 2009 due to higher market values and two medium term note offerings totalling $400.0 million (see section 3.4, Recent events). The substantial appreciation in market values also contributed to the 13.3% increase in book value per share to $24.88 at year end.

3.4 Recent events

Proposed auto reforms by Ontario Government

In Ontario, the personal auto insurance environment has been affected by medical claims inflation, with industry rates in Ontario increasing 12.4% since January 2008 to help recoup the costs. To address this issue, on November 2, 2009, the Ontario Government released a list of changes to the personal auto regime intended to provide greater choice for consumers while creating a more stable cost environment. The new reforms set the right direction to keep inflation in check and maintain the affordability of the product for consumers.

Alberta minor injury cap

In December 2009, the Supreme Court of Canada decided not to allow a further appeal of the Alberta personal auto minor injury cap on the basis that it is discriminatory. As a result, the Alberta minor injury cap will remain in effect. Accordingly, IFC's provision for claims associated with the cap is no longer required and was released in the fourth quarter.

Medium term notes ("MTN") offerings

During 2009, the company completed two medium term notes offerings for a total of $400.0 million. In August, the company issued $250.0 million in 10-year MTNs with a coupon of 5.41%. This was followed by a subsequent offering in November of $150.0 million in 30-year MTNs at a coupon of 6.40%. The proceeds have been invested in the company's investment portfolio.

Dividend increase

On February 16, 2010 the Board of Directors increased the quarterly dividend by 6.3%, or two cents, to 34 cents per share on its outstanding common shares. The dividend will be payable on March 31, 2010 to shareholders of record on March 15, 2010. The decision reflects the company's objective of returning value to shareholders, the strength of the Company's financial position and quality of operating earnings. This is the fifth consecutive year the company has increased its dividend.

Normal course issuer bid

On February 16, 2010 the Board of Directors authorized a normal course issuer bid ("NCIB") to purchase during the next 12 months up to 5,977,913 shares, representing approximately 5% of its currently outstanding common shares, subject to approval by the Toronto Stock Exchange ("TSX").

The company's strong capital base and financial condition enable it to return capital to shareholders, while maintaining the financial resources required to pursue its growth strategies.

SECTION 4 – **Personal lines**

4.1 Financial results

TABLE 7

(in millions of dollars, except as noted)	**Q4 2009**	Q4 2008	Change	**2009**	2008	Change
Direct premiums written (excluding pools)						
Automobile	**474.6**	452.5	4.9%	**2,126.6**	2,057.0	3.4%
Property	**239.7**	226.6	5.8%	**994.2**	952.9	4.3%
Total	**714.3**	679.1	5.2%	**3,120.8**	3,009.9	3.7%
Written insured risks (thousands)						
Automobile	**535.1**	528.7	1.2%	**2,454.7**	2,449.3	0.2%
Property	**385.4**	385.6	(0.1)%	**1,643.2**	1,654.4	(0.7)%
Total	**920.5**	914.3	0.7%	**4,097.9**	4,103.7	(0.1)%
Net premiums earned						
Automobile	**531.0**	520.6	2.0%	**2,066.5**	2,067.5	0.0%
Property	**240.2**	227.9	5.4%	**926.4**	891.3	3.9%
Total	**771.2**	748.5	3.0%	**2,992.9**	2,958.8	1.2%
Net underwriting income (loss) (excluding MYA)						
Automobile	**10.4**	(14.8)	n/a	**105.0**	84.7	24.0%
Property	**29.3**	(32.0)	n/a	**(83.7)**	(120.7)	n/a
Total (excluding MYA)	**39.7**	(46.8)	n/a	**21.3**	(36.0)	n/a
Market yield adjustment	**8.3**	(30.7)	39.0	**(26.8)**	(32.4)	5.6
Net underwriting income (loss) (including MYA)	**48.0**	(77.5)	125.5	**(5.5)**	(68.4)	62.9

TABLE 8 – UNDERWRITING RATIOS

	Q4 2009	Q4 2008	Change	**2009**	2008	Change
Personal auto						
Claims ratio (excluding MYA)	**73.6%**	78.5%	(4.9) pts	**71.3%**	71.2%	0.1 pts
Expense ratio	**24.4%**	24.4%	–	**23.6%**	24.7%	(1.1) pts
Combined ratio (excluding MYA)	**98.0%**	102.9%	(4.9) pts	**94.9%**	95.9%	(1.0) pts
Personal property						
Claims ratio (excluding MYA)	**53.5%**	80.7%	(27.2) pts	**75.2%**	80.2%	(5.0) pts
Expense ratio	**34.3%**	33.4%	0.9 pts	**33.8%**	33.4%	0.4 pts
Combined ratio (excluding MYA)	**87.8%**	114.1%	(26.3) pts	**109.0%**	113.6%	(4.6) pts
Personal lines – total						
Claims ratio (excluding MYA)	**67.4%**	79.2%	(11.8) pts	**72.5%**	73.9%	(1.4) pts
Expense ratio	**27.5%**	27.1%	0.4 pts	**26.8%**	27.3%	(0.5) pts
Combined ratio (excluding MYA)	**94.9%**	106.3%	(11.4) pts	**99.3%**	101.2%	(1.9) pts

4.2 Explanation of financial results

Fourth quarter 2009

Direct written premium growth in personal auto was solid at 4.9% reflecting higher average premiums and unit growth as industry pricing has continued to firm up through 2009, particularly in Ontario which is the largest auto market in Canada. IFC has steadily increased rates in Ontario over the last two years ahead of competitors due to escalating accident benefit costs and bodily injury claims. In mid 2010, the Ontario Government will introduce new reforms to help stabilize costs and maintain the affordability of auto insurance in the province (see Section 3.4, Recent events).

Personal auto underwriting income was good with a combined ratio of 98.0%, a 4.9 point improvement year-over-year due to more favourable prior year claims development. Personal auto results benefited from better current accident year results and the release of provisions associated with minor injury cap regulations which increased underwriting income by $22.4 million. These positive factors were partly offset by losses from industry risk sharing pools. Results for industry risk sharing pools tend to fluctuate between periods.

Direct written premium growth in personal property was 5.8% due to high single-digit premium increases under IFC's home insurance action plan. The personal property business returned to profitability in the fourth quarter with a very strong combined ratio of 87.8% due to better weather conditions as IFC continued to make progress on the home insurance action plan. Addressing the challenges in IFC's home insurance business was a key focus area in 2009. This is reflected in the improvement in current accident year underwriting results excluding catastrophes in each of the last three quarters.

Full year 2009

IFC's organic growth strategy in personal lines gained traction in 2009 with direct written premium growth of 3.7% due to higher average premiums. As personal auto and property premiums go up across the industry it creates a more favourable competitive environment for IFC to continue to grow at healthy margin levels.

Personal auto underwriting results were solid with a combined ratio of 94.9% compared to 95.9% in 2008 due to a lower expense ratio. Underwriting income also benefited from the release of provisions that were set up in prior years related to personal auto minor injury cap regulations (previously discussed). In personal property, the industry faces ongoing challenges caused by water damage claims. However, with some benefits from IFC's action plan, underwriting results in personal property improved by 4.6 points year-over-year with a combined ratio of 109.0%.

Home insurance action plan

The industry faces ongoing challenges caused by water damage claims, changing weather patterns and higher reconstruction costs. IFC is addressing these issues in the personal property segment through a robust action plan to improve the combined ratio by 10–15% over the next 12–18 months. The main initiatives include:

- ***Rate adjustments and price segmentation*** Certain regions are more prone to water-related losses due to aging city infrastructure and/or changing weather patterns. IFC is implementing rate adjustments in higher-risk zones and caps on certain types of coverage in these geographic areas. On average, policies are being renewed with double-digit premium increases due to a combination of higher rates and insured amounts.
- ***Adjusting insured amounts*** In general, the industry has been affected by under-insurance in personal property due to higher material and building cost inflation. Across Canada, IFC has been reassessing the value of properties to ensure that: 1) customers retain adequate coverage, and 2) premiums match prospective reconstruction costs.
- ***Review of claims process*** IFC is reviewing its claims process to ensure consistency in the quality, cost and management of claims including the review of routine claims, appraisal processes, workflow design and enhancement of the Property Rely Network of IFC's preferred suppliers. In addition, larger property losses will be subject to a competitive bid process.
- ***Review of insurance product*** IFC's home insurance products were developed based on historical climate patterns and claims experience, which are now changing. As a result, IFC is reviewing its home insurance products to ensure that they fit the evolving needs of customers and current risk exposures. An example of this is the introduction in 2010 of deductibles on water damage claims among many other changes to adapt the insurance product to new climate realities.
- ***Customer education and incentives on loss control and prevention*** IFC encourages customers to reduce their risk of loss by providing information on loss control and prevention. In the future, IFC will encourage customers to take measures to protect their homes against water losses.

SECTION 5 – **Commercial lines**

5.1 Financial results

TABLE 9

(in millions of dollars, except as noted)	Q4 2009	Q4 2008	Change	2009	2008	Change
Direct premiums written (excluding pools)						
Automobile	**80.4**	77.2	4.1%	**321.9**	317.8	1.3%
Commercial P&C	**216.6**	211.9	2.2%	**832.2**	817.8	1.8%
Total	**297.0**	289.1	2.7%	**1,154.1**	1,135.6	1.6%
Written insured risks (thousands)						
Automobile	**66.5**	63.0	5.6%	**269.4**	263.8	2.1%
Commercial P&C	**59.1**	57.0	3.7%	**236.4**	234.0	1.0%
Total	**125.6**	120.0	4.7%	**505.8**	497.8	1.6%
Net premiums earned						
Automobile	**80.4**	80.1	0.4%	**315.2**	318.9	(1.2)%
Commercial P&C	**184.8**	190.7	(3.1)%	**747.3**	761.8	(1.9)%
Total	**265.2**	270.8	(2.1)%	**1,062.5**	1,080.7	(1.7)%
Net underwriting income (loss) (excluding MYA)						
Automobile	**23.8**	6.8	250.0%	**63.6**	40.8	55.9%
Commercial P&C	**(7.4)**	51.0	(114.5)%	**(30.9)**	112.2	(127.5)%
Total (excluding MYA)	**16.4**	57.8	(71.6)%	**32.7**	153.0	(78.6)%
Market yield adjustment	**4.5**	(16.6)	21.1	**(14.8)**	(17.6)	2.8
Net underwriting income (including MYA)	**20.9**	41.2	(20.3)	**17.8**	135.4	(117.6)

TABLE 10 – UNDERWRITING RATIOS

	Q4 2009	Q4 2008	Change	2009	2008	Change
Commercial auto						
Claims ratio (excluding MYA)	**41.2%**	63.9%	(22.7) pts	**51.5%**	59.9%	(8.4) pts
Expense ratio	**29.2%**	27.7%	1.5 pts	**28.3%**	27.3%	1.0 pts
Combined ratio (excluding MYA)	**70.4%**	91.6%	(21.2) pts	**79.8%**	87.2%	(7.4) pts
Commercial P&C						
Claims ratio (excluding MYA)	**65.4%**	36.4%	29.0 pts	**67.4%**	49.7%	17.7 pts
Expense ratio	**38.6%**	36.8%	1.8 pts	**36.7%**	35.6%	1.1 pts
Combined ratio (excluding MYA)	**104.0%**	73.2%	30.8 pts	**104.1%**	85.3%	18.8 pts
Commercial lines – total						
Claims ratio (excluding MYA)	**58.1%**	44.5%	13.6 pts	**62.7%**	52.7%	10.0 pts
Expense ratio	**35.8%**	34.2%	1.6 pts	**34.2%**	33.2%	1.0 pts
Combined ratio (excluding MYA)	**93.8%**	78.7%	15.2 pts	**96.9%**	85.9%	11.0 pts

5.2 Explanation of financial results

Fourth quarter 2009

In commercial lines, direct written premiums grew 2.2% in commercial P&C and 4.1% in commercial auto supported by increases in written insured risks and a modest increase in average rates. Premium growth in commercial P&C was negatively impacted by the run-off of certain unprofitable group accounts which have been cancelled. Excluding these policies, commercial P&C premiums were up a healthy 3.8% in the fourth quarter. This shows further evidence of firming market conditions especially in Ontario.

Strong underwriting income in commercial auto was offset by lower underwriting results in commercial P&C. The combined ratio in commercial auto was excellent at 70.4% compared to 91.6% in the fourth quarter of 2008 due to more favourable prior year development and lower claims frequency and severity. In commercial P&C, underwriting results were disappointing due to fire losses and the run-off of certain cancelled commercial group accounts. Overall the combined ratio in commercial P&C was 104.0%. Excluding the effect of these commercial group accounts, the segment was profitable with a combined ratio of 98.6%.

IFC's commercial growth strategy is based on disciplined pricing and risk selection in the small- to medium-sized business segments. Over the last couple of years, IFC's growth has been moderate mainly due to highly competitive pricing conditions across the industry which made it difficult for disciplined insurers to grow at attractive margin levels. Higher industry loss ratios since 2007, lower investment income and the pressure on industry excess capital are expected to lead to a more favourable competitive environment.

Full year 2009

Direct written premiums in commercial P&C and commercial auto increased 1.8% and 1.3% respectively. Growth was weak in early 2009 due to competitive pricing, but as the pressure has eased in some commercial segments, core growth in the portfolio started to pick up toward the end of the year with an increase in written insured risks in the last quarter. Excluding the run-off of the commercial group accounts mentioned previously, direct written premium growth in commercial P&C was 2.4%.

Underwriting performance in commercial auto has remained robust with a combined ratio of 79.8% in 2009 versus 87.2% last year. The increase in underwriting income was due to lower claims frequency and severity and more favourable prior year claims development. In commercial P&C, underwriting results were lower with a combined ratio of 104.1% mainly due to the factors described in the fourth quarter discussion. Rate increases in commercial lines accelerated in late 2009 as reflected in the growth rates for the fourth quarter.

SECTION 6 – Invested assets

6.1 Interest and dividend income, net of expenses

TABLE 11

(in millions of dollars, except as noted)	Q4 2009	Q4 2008	Change	2009	2008	Change
Interest income	**46.5**	46.9	(0.9)%	**178.7**	187.9	(4.9)%
Dividend income	**35.9**	35.3	1.7%	**130.8**	157.3	(16.8)%
Interest and dividend income, before expenses	**82.4**	82.2	0.2%	**309.5**	345.2	(10.3)%
Expenses	**(5.0)**	(3.9)	(1.1)	**(16.8)**	(16.4)	(0.4)
Interest and dividend income, net of expenses	**77.3**	78.3	(1.3)%	**292.7**	328.8	(11.0)%
Market-based yield [1]	**4.4%**	5.1%	(0.7) pts	**4.5%**	5.0%	(0.5) pts

1 The market-based yield is a non-GAAP measure defined as the annualized total pre-tax dividend and interest income (before expenses) divided by the average fair values of equity and fixed income securities held during the reporting period. The market-based yield is a measure that may not be comparable to other companies since it is a non-GAAP measure.

Fourth quarter dividend and interest income was solid at $82.4 million, in line with the same quarter in 2008. For the full year, income from investments decreased reflecting actions to protect IFC's strong financial position through the financial crisis. In late 2008, the company reduced its exposure to common shares and increased its investments in government bonds and treasuries. Since then, IFC has gradually realigned the portfolio to its target long-term asset mix (see Section 6.3, Portfolio of invested assets).

The market-based yield was 4.4%, down from 5.1% in the fourth quarter of 2008. For the full year, the market yield decreased 50 basis points to 4.5%. The lower yield is due to the change in mix of our portfolio described above and a significant decline in the risk-free interest rate compared to the same period in 2008.

6.2 Net investment gains (losses)

TABLE 12

(in millions of dollars)	Q4 2009	Q4 2008	Change	2009	2008	Change
Fixed income securities						
Gains on AFS securities	**0.8**	1.8	(55.6)%	**16.3**	0.2	n/a
Gains (losses) on derivatives	**0.4**	(6.6)	n/a	**4.4**	(17.4)	n/a
Recovery (losses) on impairments	**2.8**	–	n/a	**(5.6)**	(10.9)	n/a
Gains (losses) on fixed income securities and related derivatives	**4.0**	(4.8)	n/a	**15.1**	(28.1)	n/a
Equity securities						
Gains (losses), net of stand-alone derivatives	**10.4**	(24.4)	n/a	**(75.5)**	(74.6)	n/a
Recovery (losses) on impairments	**(19.2)**	(185.8)	n/a	**(46.2)**	(250.5)	n/a
Gains (losses) on embedded derivatives	**9.4**	20.8	(54.8)%	**(62.9)**	36.8	(270.9)%
Gains (losses) on equity securities and related derivatives	**0.6**	(189.4)	n/a	**(184.6)**	(288.3)	n/a
Total gains (losses) excluding HFT fixed income securities	**4.6**	(194.2)	n/a	**(169.5)**	(316.4)	n/a
Gains (losses) on HFT fixed income securities[1]	**(17.9)**	42.0	(142.6)%	**(3.0)**	28.4	110.6%
Total net gains (losses), before income taxes	**(13.3)**	(152.2)	n/a	**(172.5)**	(288.0)	n/a

1 The gains (losses) on HFT fixed income securities are offset by a MYA to claims liabilities, with an objective of a minimal impact to net income. The difference between the MYA and the gains and losses on HFT fixed income securities is referred to as the "market yield effect" in this MD&A. See table 21.

Fourth quarter 2009

With healthier capital markets, the company recorded modest net investment gains of $4.6 million excluding HFT bonds. The market value of every asset class in IFC's portfolio continued to improve in the fourth quarter. Despite this, the company recorded impairments of $19.2 million on certain common shares that failed to recover sufficiently. IFC's common equity and fixed income portfolios ended the year in an unrealized gain position (See table 19).

Full year 2009

Despite the increase in the market value of the portfolio in 2009, the company recorded net investment losses of $169.5 million excluding HFT bonds. Early in the year, the company implemented a new hedging program to eliminate its exposure to financial common stocks that created a one-time, realized loss of $82.9 million. Full year results were also affected by a $62.9 million non-cash loss on embedded derivatives linked to the substantial increase in the market value of the company's perpetual preferred shares (See section 10.4, Accounting for embedded derivatives). In addition, due to the length and severity of the financial crisis, the company incurred total equity impairments of $46.2 million over the year.

With improved equity market conditions in 2009 and proceeds from two medium term note offerings, the value of the cash and investment portfolio increased to $8.1 billion at year end.

6.3 Portfolio of invested assets

The company's portfolio of invested assets is managed by Intact Investment Management, Inc. ("IIM"), which is a wholly owned subsidiary of Intact Financial Corporation. The assets are managed by IIM in accordance with the company's investment policy.

Investment policy

The company has an investment policy that seeks to provide an attractive risk-return profile over the medium to long term. The investment policy takes into account the current and expected condition of capital markets, the historic return profiles of various asset classes and the variability of those returns over time, the availability of assets, diversification needs and benefits, regulatory capital required to support the various asset types, security ratings and other material variables likely to affect the overall performance of the company's portfolio of invested assets. The overall risk profile of the portfolio is designed to balance the investment portfolio return required to satisfy the company's liabilities while optimizing the investment opportunities available in the marketplace. Management monitors and enforces compliance with the company's investment policy.

Asset mix

The investment portfolio includes high-quality government and corporate bonds, as well as Canadian equity securities of large, publicly-traded, dividend-paying companies. The company does not invest in leveraged securities and exposure to the United States market is minimal. The company manages its investments prudently to protect capital and generate superior after-tax returns.

TABLE 13 – INVESTED ASSET MIX (IN ACCORDANCE WITH GAAP)

	As at December 31, 2009		As at December 31, 2008	
(in millions of dollars, except as noted)	Fair value	% of fair value	Fair value	% of fair value
Cash and cash equivalents	60.1	0.7%	510.4	7.7%
Short-term notes	210.7	2.6%	293.8	4.4%
Fixed income securities	4,573.6	56.8%	3,538.7	53.6%
Preferred shares	1,581.6	19.6%	1,220.1	18.5%
Common shares	1,312.1	16.3%	799.4	12.1%
Loans	318.5	4.0%	242.3	3.7%
Total cash and invested assets	8,056.6	100.0%	6,604.7	100.0%

TABLE 14 – INVESTED ASSET MIX (NET OF HEDGING POSITIONS)

	As at December 31, 2009		As at December 31, 2008	
(in millions of dollars, except as noted)	Fair value	% of fair value	Fair value	% of fair value
Cash and cash equivalents	60.1	0.8%	510.4	7.7%
Short-term notes	210.7	2.7%	293.8	4.5%
Fixed income securities	4,958.7	63.5%	3,615.1	54.7%
Preferred shares	1,510.8	19.4%	1,214.4	18.4%
Common shares	742.9	9.5%	723.4	11.0%
Loans	318.5	4.1%	242.3	3.7%
Total cash and invested assets	7,801.7	100.0%	6,599.3	100.0%

The value of the investment portfolio increased significantly in 2009 due to the equity market rebound and proceeds of $400.0 million from two medium term note offerings.

The majority of the company's portfolio is invested in high-quality Canadian securities that are actively traded. The fair value for most invested assets is based on quoted bid prices. In cases where an active market does not exist, the estimated fair values are based on recent transactions or current market prices for similar securities.

- ***Fixed income securities*** The company invests in highly-rated fixed income securities mainly including corporate bonds and government bonds. The fixed income portfolio is mostly Canadian with 12.4% foreign content. Approximately 98.4% of the fixed income portfolio is rated 'A' or better and all of the securities are investment grade. The company has no exposure to leveraged capital notes in structured investment vehicles, directly or through the use of derivatives. The company has $103.1 million (December 31, 2008 – $285.0 million) in asset-backed securities mostly comprised of Canadian credit card loans and commercial mortgage-backed securities.
- ***Common shares*** Common equity exposure is focused primarily on high dividend-paying Canadian equities. The company seeks enhanced returns by identifying and investing in shares that are likely to pay increased dividends or pay special dividends. Management undertakes intensive analysis of investment opportunities to identify special dividend candidates. Similar evaluations are conducted to assess securities most likely to increase dividends. In addition, the equity portfolios are also actively managed to maximize dividend income throughout the year.
- ***Preferred shares*** The company's investment portfolio includes a large percentage of preferred shares to achieve its objective of maximizing dividend income. The dividend income earned from these preferred shares is generally not taxable. The preferred share portfolio is generally not traded and the shares are generally held until they are called. Consequently, the company's results are generally impacted only when preferred shares are impaired, or when the shares are called or sold to avail of selected market opportunities. The preferred share portfolio is comprised entirely of Canadian securities with a high proportion of the portfolio invested in securities that are at least P2 in their credit rating and all are investment grade.
- ***Derivatives*** The company uses derivative financial instruments for hedging purposes and to modify the risk profile of the portfolio of invested assets as long as the resulting exposures are within investment policy guidelines.

Sector mix by asset class

The following table shows sector exposures by asset class as a percentage of total cash and invested assets (excluding loans) as at December 31, 2009.

TABLE 15 – INVESTED ASSET MIX (IN ACCORDANCE WITH GAAP)

			Common shares		
	Fixed income	Preferred shares	IFC	S&P/TSX weighting	IFC total
Energy	1.6%	2.7%	21.2%	27.5%	5.2%
Materials	–	–	6.6%	19.4%	1.1%
Industrials	1.0%	–	10.0%	5.6%	2.4%
Information Technology	–	–	1.6%	3.5%	0.3%
Telecommunication	1.2%	7.5%	9.0%	4.3%	3.9%
Consumer Discretionary	0.8%	2.3%	6.5%	4.3%	2.1%
Consumer Staples	–	1.7%	7.3%	2.8%	1.6%
Health Care	–	–	0.7%	0.5%	0.1%
Financials	20.8%	81.1%	30.2%	30.4%	34.8%
Utilities	2.0%	4.6%	6.6%	1.7%	3.3%
Government	72.6%	0.1%	0.3%	–	45.2%
Total	100.0%	100.0%	100.0%	100.0%	100.0%
Total in millions	4,784.3	1,581.6	1,312.1	n/a	7,678.0

TABLE 16 – INVESTED ASSET MIX (NET OF HEDGING POSITIONS)

	Fixed income	Preferred shares	Common shares IFC	Common shares S&P/TSX weighting	IFC total
Energy	1.5%	2.8%	33.4%	27.5%	5.0%
Materials	–	–	5.8%	19.4%	0.6%
Industrials	1.0%	–	13.4%	5.6%	2.0%
Information Technology	–	–	0.8%	3.5%	0.1%
Telecommunication	1.0%	7.3%	11.1%	4.3%	3.3%
Consumer Discretionary	0.7%	2.3%	8.2%	4.3%	1.8%
Consumer Staples	–	1.7%	10.2%	2.8%	1.4%
Health Care	–	–	1.2%	0.5%	0.1%
Financials	26.9%	81.0%	6.2%	30.4%	35.9%
Utilities	1.9%	4.7%	9.2%	1.7%	3.2%
Government	67.0%	0.2%	0.5%	–	46.6%
Total	100.0%	100.0%	100.0%	100.0%	100.0%
Total in millions	5,169.4	1,510.8	742.9	n/a	7,423.1

Portfolio credit quality

As at December 31, 2009, the weighted average rating of the company's fixed income portfolio was AA+ and the weighted average rating of its preferred share portfolio was P2, equivalent to a rating of BBB+. The company had no fixed income securities or preferred shares with a rating below investment grade at December 31, 2009.

The following table includes the credit quality of the fixed income securities portfolio as at December 31, 2009 and 2008.

TABLE 17

(in millions of dollars, except as noted)	As at December 31, 2009 Fair value	As at December 31, 2009 % of fair value	As at December 31, 2008 Fair value	As at December 31, 2008 % of fair value
Fixed income securities[1]				
AAA	2,463.5	53.9%	2,101.9	59.4%
AA	1,187.3	26.0%	583.3	16.5%
A	846.5	18.5%	751.1	21.2%
BBB	76.3	1.6%	102.4	2.9%
Total	4,573.6	100.0%	3,538.7	100.0%

1 Source: Standard & Poor's ("S&P") or Dominion Bond Rating Services

The following table includes the credit quality of the preferred share portfolio as at December 31, 2009 and 2008.

TABLE 18

(in millions of dollars, except as noted)	As at December 31, 2009 Fair value	As at December 31, 2009 % of fair value	As at December 31, 2008 Fair value	As at December 31, 2008 % of fair value
Preferred shares[1]				
P1	964.5	61.0%	795.0	65.2%
P2	296.3	18.7%	293.2	24.0%
P3	320.8	20.3%	130.9	10.7%
P5	–	–	1.0	0.1%
Total	1,581.6	100.0%	1,220.1	100.0%

1 Source: Standard & Poor's ("S&P") or Dominion Bond Rating Services

Net pre-tax unrealized gains and losses on AFS securities

TABLE 19

(in millions of dollars)	December 31, 2009	September 30, 2009	June 30, 2009	March 31, 2009	December 31, 2008
Fixed income securities	21.4	44.0	18.5	37.3	30.4
Common shares	36.7	(24.3)	(61.7)	(134.4)	(140.7)
Preferred shares	(160.3)	(162.2)	(292.1)	(492.1)	(522.5)
Total net unrealized loss position	(102.2)	(142.5)	(335.3)	(589.2)	(632.8)

The 30.7% increase in the S&P/TSX Composite Index and a 20.2% increase in the S&P/TSX Preferred Share Index in 2009 contributed to the $530.6 million improvement in the unrealized loss position.

Gains and losses in the common share portfolio are generally realized on an ongoing basis under normal capital market conditions reflecting the trading strategy in the high-dividend yield common share portfolio.

In determining the fair values of invested assets, management relies mainly on quoted market prices. There are no invested assets in the AFS or HFT categories which are not quoted on an active market, except for a very limited amount of fixed income securities that IFC holds (Refer to note 6 Fair value measurement to the Consolidated financial statements for details).

Impairment recognition

Common shares classified as AFS are assessed for impairment if the current market value drops significantly below the book value, or if there has been a prolonged decline in fair value below book value. Management then applies judgment based on each issuer's financial condition to determine whether objective evidence of impairment exists. This is determined by an assessment of information available at the time. Fixed income securities and preferred shares are considered to be impaired when there is objective evidence that suggests the issuer will fail to make the contractual interest or principal payments due under the terms of the instrument.

The net unrealized gain position on AFS common shares at the end of December 2009 was $36.7 million.

TABLE 20 – AGING OF UNREALIZED LOSSES ON AFS COMMON SHARES

(in millions of dollars)	**December 31, 2009**	September 30, 2009	June 30, 2009	March 31, 2009	December 31, 2008
>25% below book value for <3 consecutive months	**–**	0.6	1.5	30.6	76.7
>25% below book value for >=3 and <6 consecutive months	**0.4**	–	10.4	60.6	21.1
>25% below book value for >=6 consecutive months	**–**	18.6	45.8	5.7	1.8
Other unrealized losses	**19.4**	37.9	38.9	50.1	51.7
Total net unrealized losses on AFS common shares	**19.8**	57.1	96.6	147.0	151.3

Other comprehensive loss

The improvement in the unrealized loss position on AFS securities and dispositions of AFS securities resulted in positive other comprehensive income ("OCI") of $40.3 million in the fourth quarter. On a year-to-date basis, the decrease in the unrealized loss position reflects improved equity market conditions and the realization of $82.9 million in losses in the first quarter associated with the implementation of the financial hedging program.

Held-for-trading fixed income securities and market yield adjustment

TABLE 21 – MARKET YIELD EFFECT

(in millions of dollars)	**Q4 2009**	Q4 2008	Change	**2009**	2008	Change
Positive (negative) impact of MYA	**12.8**	(47.3)	60.1	**(41.6)**	(50.0)	8.4
Net gains (losses) on HFT fixed income securities	**(17.9)**	42.0	(59.9)	**(3.0)**	28.4	(31.4)
Market yield effect	**(5.1)**	(5.3)	0.2	**(44.6)**	(21.6)	(23.0)

Claims liabilities are discounted at the estimated market yield of the assets backing these liabilities. The MYA to claims liabilities is offset by gains and losses on HFT fixed income securities with the objective that these items offset each other with a minimal overall impact to income. The difference between the MYA and the gains and losses on HFT fixed income securities is referred to as the "market yield effect" in this MD&A.

On a year-to-date basis, the market yield effect had a $44.6 million negative impact mainly due to a mismatch caused by the de-risking of the bond portfolio where the proportion of corporate bonds was reduced. As a result, the market yield rate used to discount claims liabilities fell, and was not offset by gains on HFT bonds. The process of matching the weighted-dollar duration of the claims liabilities to assets classified as HFT works well under normal conditions. However, market fluctuations, change in yield curve, trading and change in asset mix can result in a positive or negative market yield effect.

SECTION 7 – Net operating income

TABLE 22 – COMPONENTS OF NET OPERATING INCOME

(in millions of dollars, except as noted)	Q4 2009	Q4 2008	Change	2009	2008	Change
Net underwriting income (excluding MYA) (table 5)	**56.0**	11.0	409.1%	**54.0**	117.0	(53.8)%
Interest and dividend income (table 11)	**77.3**	78.3	(1.3)%	**292.7**	328.8	(11.0)%
Corporate and distribution income (loss)	**(7.5)**	2.0	(475.0)%	**7.2**	15.6	(53.8)%
Tax impact	**(27.7)**	(16.2)	n/a	**(72.3)**	(100.7)	n/a
Net operating income (excluding MYA)	**98.1**	75.1	30.6%	**281.6**	360.7	(21.9)%

Changes in net operating income are fully described in sections 3.3 and 6.1.

TABLE 23 – RECONCILIATION TO NET INCOME

(in millions of dollars, except as noted)	Q4 2009	Q4 2008	Change	2009	2008	Change
Net income (loss) (table 2)	**96.7**	(64.1)	n/a	**126.7**	128.2	(1.2)%
Add losses (deduct gains) before HFT fixed income securities (table 12)	**(4.6)**	194.2	(198.8)	**169.5**	316.4	(146.9)
Add market yield effect (table 21)	**5.1**	5.3	(0.2)	**44.6**	21.6	23.0
Tax impact	**0.9**	(60.3)	61.2	**(59.2)**	(105.5)	46.3
Net operating income (excluding MYA) [1]	**98.1**	75.1	30.6%	**281.6**	360.7	(21.9)%
Average outstanding shares (millions)	**119.9**	119.9	–	**119.9**	122.0	(2.1)
Net operating income per share (dollars) [2]	**0.82**	0.63	0.19	**2.35**	2.96	(0.61)

1 Net operating income is defined as net income excluding the MYA and net gains (losses) on invested assets and other gains, after tax.
2 Net operating income per share is defined as net operating income for the period divided by the average outstanding number of shares for the same period.

SECTION 8 – Selected quarterly and annual information

8.1 Selected quarterly information

TABLE 24

(in millions of dollars, except as noted)	Q4 2009	Q3 2009	Q2 2009	Q1 2009	Q4 2008	Q3 2008	Q2 2008	Q1 2008	Q4 2007
Written insured risks (thousands)	**1,046.0**	1,244.4	1,376.0	937.2	1,034.3	1,240.7	1,380.6	945.8	1,056.7
Direct premiums written (excluding pools)	**1,011.4**	1,144.1	1,250.6	868.8	968.2	1,100.3	1,216.7	860.3	961.3
Total revenues	**1,124.7**	1,116.4	1,064.6	936.5	956.0	1,045.8	1,065.4	1,064.5	1,096.8
Net premiums earned (table 5)	**1,036.5**	1,019.0	1,011.3	988.7	1,019.2	1,032.3	996.1	991.8	1,004.7
(Favourable) unfavourable prior year claims development[1]	**(66.0)**	(14.0)	(6.5)	(37.2)	(52.2)	(56.4)	(41.2)	0.9	(62.4)
Net underwriting income (loss)[1] (table 5)	**56.0**	(53.2)	43.2	7.9	11.0	61.9	43.4	0.8	68.2
Combined ratio (%)[1]	**94.6%**	105.2%	95.7%	99.2%	98.9%	94.0%	95.6%	99.9%	93.2%
Net operating income[1]	**98.1**	21.6	92.9	69.1	75.1	106.4	109.5	70.2	116.4
Net income (loss)	**96.7**	(8.0)	74.2	(36.3)	(64.1)	57.3	112.0	23.0	95.8
EPS – basic/diluted (dollars)	**0.81**	(0.07)	0.62	(0.30)	(0.53)	0.47	0.91	0.19	0.77
Net operating income per share (dollars)[1]	**0.82**	0.18	0.77	0.58	0.63	0.88	0.89	0.56	0.93

1 Excluding MYA

8.2 Selected annual information

TABLE 25

(in millions of dollars, except as noted)	2009	2008	2007
Total revenue	**4,241.3**	4,131.7	4,439.9
Net underwriting income (excluding MYA) (table 5)	**54.0**	117.0	189.1
Net income	**126.7**	128.2	508.3
EPS – basic and diluted (dollars)	**1.06**	1.05	4.01
Annual dividends per common share	**1.28**	1.24	1.08
Invested assets	**7,996.5**	6,094.3	7,223.3
Total assets	**11,351.3**	9,785.2	10,389.7
Debt outstanding	**397.7**	–	–
Total shareholders' equity	**2,982.6**	2,632.6	3,172.1

SECTION 9 – Financial condition

9.1 Balance sheet highlights

The table below shows the significant balance sheet items as reported on December 31, 2009 and December 31, 2008.

TABLE 26

	As at		
(in millions of dollars, except as noted)	**December 31, 2009**	December 31, 2008	Change ($)
Cash and cash equivalents	**60.1**	510.4	(450.3)
Invested assets			
Fixed income securities	**4,784.3**	3,832.5	951.8
Equity securities	**2,893.7**	2,019.5	874.2
Loans	**318.5**	242.3	76.2
Total invested assets	**7,996.5**	6,094.3	1,902.2
Premiums receivable	**1,640.5**	1,469.4	171.1
Deferred acquisition costs	**396.2**	382.4	13.8
Reinsurance assets	**260.6**	224.2	36.4
Intangible assets and goodwill	**338.2**	297.2	41.0
Other assets	**659.2**	807.3	(148.1)
Total assets	**11,351.3**	9,785.2	1,566.1
Claims liabilities	**4,270.0**	4,064.9	205.1
Unearned premiums	**2,463.6**	2,366.8	96.8
Debt outstanding	**397.7**	–	397.7
Financial liabilities	**278.8**	9.1	269.7
Other liabilities	**958.6**	711.8	246.8
Total liabilities	**8,368.7**	7,152.6	1,216.1
Share capital and contributed surplus	**1,144.8**	1,149.8	(5.0)
Retained earnings	**1,902.2**	1,928.9	(26.7)
Accumulated other comprehensive loss	**(64.4)**	(446.1)	381.7
Shareholders' equity	**2,982.6**	2,632.6	350.0
Book value per share (dollars)	**24.88**	21.96	2.92

Invested assets and cash

The invested assets and cash increased by approximately $1.5 billion or by 22.0%. The increase is due to cash generated from operating activities, net of dividends paid, the issue of the medium term notes totalling $400.0 million and increased market values.

Premiums receivable, deferred acquisition costs and unearned premiums

The increase in these balances is consistent with accelerating growth in direct written premiums of 4.5% in the fourth quarter.

Reinsurance assets

Reinsurance assets have increased $36.4 million. This reflects increased recoverables from reinsurers on losses resulting from catastrophes.

Intangible assets and goodwill

Increase is related to customer relationship rights and goodwill capitalized on the acquisition of new affiliates as well as capitalization of internally developed software, net of amortization expense.

Other assets

Other assets decrease is mainly due to tax refunds received on prior year filings.

Claims liabilities

Claims liabilities increase reflects additional claims related to severe storms in the third quarter 2009.

Debt outstanding

During 2009, the company issued two series of medium term notes with proceeds of $397.7 million net of capitalized issuance costs.

Financial liabilities

The increase is due to new short positions associated with our market neutral investment strategies, as well as the increase in embedded derivative liabilities on our preferred shares.

Other liabilities

The increase is caused mainly by the increased income tax payable relating to the appreciation in value of our equity investment portfolio.

Shareholders' equity

Shareholders' equity increased by $350.0 million reflecting mainly an increase in the market value of the company's investment portfolio.

9.2 Claims liabilities

Assessing claims reserve adequacy

Effectively assessing claims reserve adequacy is a critical skill required to effectively manage any property and casualty insurance business and is a strong determinant of the long-term viability of the organization. The total claims reserve is made up of two main elements: 1) reported claim case reserves, and 2) claims that are incurred but not reported ("IBNR"). IBNR reserves supplement the case reserves by taking into account:

– possible claims that have been incurred but not yet reported to the company by policyholders;
– expected over/underestimation in case reserves based on historical patterns; and
– other adjustment expenses not included in the initial case reserve.

Case reserves and IBNR should be sufficient to cover all expected claims liabilities for events that have already occurred, whether reported or not, taking into account a provision for adverse deviation ("PfAD") and a discount for the time value of money (see Market yield adjustment). The discount is applied to the total claims reserve and adjusted on a regular basis based on changes in market yields. If market yields rise, the discount would increase and reduce total claims liabilities and therefore, positively impact net underwriting income in that period, all else being equal. If market yields decline, it would have the opposite effect. IBNR and the PfAD are reviewed and adjusted periodically.

Historically, the company's claims liabilities have had a 3%–4% percent redundancy per year. This is commonly referred to as favourable prior year claims development. The rate of favourable prior year claims development was unusually high in 2003 to 2005 and does not represent a normal or expected level of reserve redundancy in a typical year. Prior year claims development fluctuates between quarters and from year to year.

TABLE 27 – ANNUALIZED RATE OF FAVOURABLE PRIOR YEAR CLAIMS DEVELOPMENT

(annualized rate, excluding MYA)	**Q4 2009**	Q4 2008	**2009**	2008
(Favourable) unfavourable prior year claims development as a % of opening reserves	**(6.8)%**	(5.6)%	**(3.2)%**	(4.0)%

Favourable prior year claims development

Excluding MYA, favourable prior year claims development was $66.0 million in the fourth quarter and $123.7 million in 2009. For the entire year, favourable prior year claims development was 3.2% of opening reserves in 2009, in line with the historical long-term average.

The following table shows the development of claims liabilities for the 10 most recent accident years, with subsequent developments during the periods. 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 as well as on current estimates of claims liabilities for claims still open or claims still incurred but not reported.

TABLE 28 – DEVELOPMENT OF CLAIMS LIABILITIES

		Accident year									
(in millions of dollars, except as noted)	**Total**	2008	2007	2006	2005	2004	2003	2002	2001	2000	1999 & earlier
Original reserve		1,376.4	1,282.2	1,178.0	1,118.8	1,117.7	973.2	838.6	729.0	655.5	1,512.9
(Favourable) unfavourable development during Q4 2009											
Including MYA	**(78.8)**	(31.6)	(14.8)	(6.8)	(7.5)	(5.7)	(2.1)	(2.4)	(5.8)	(2.6)	0.5
Excluding MYA	**(66.0)**	(27.8)	(12.0)	(4.8)	(6.1)	(4.6)	(1.5)	(2.0)	(5.6)	(2.4)	0.8
(Favourable) unfavourable development during YTD 2009											
Including MYA	**(94.4)**	(18.3)	(10.5)	(8.3)	(14.8)	(16.2)	(4.9)	(13.0)	(6.9)	(4.1)	2.6
Excluding MYA	**(123.7)**	(26.9)	(17.5)	(13.0)	(17.6)	(18.5)	(6.2)	(13.8)	(7.3)	(4.5)	1.6
Cumulative development											
Excluding MYA		(26.9)	(17.2)	(54.5)	(140.5)	(268.0)	(208.3)	(42.5)	24.8	26.6	(7.6)
As a % of original reserve		(2.0)%	(1.3)%	(4.6)%	(12.6)%	(24.0)%	(21.4)%	(5.1)%	3.4%	4.1%	(0.5)%

9.3 Reinsurance

The company's goals related to ceded reinsurance are:

- capital protection;
- reduction of the results' volatility;
- increase of underwriting capacity;
- access to the expertise of reinsurers.

The reinsurers chosen to participate in the program have a minimum rating of A- from A.M. Best or S&P. The financial analysis performed by the company's specialized reinsurance brokers is also considered. The treaties have a security review clause allowing the company to change a reinsurer during the term of the agreement if its rating falls below the minimum required. Diversification of reinsurers is analyzed and implemented to avoid excessive concentration in a specific reinsurance group.

At December 31, 2009, the company's reinsurance treaties are with unaffiliated reinsurance companies substantially all of which meet the company's financial strength rating requirements.

Reinsurance coverage is spread across many reinsurers to minimize risk to the company in the event of a very large loss. A single catastrophic event such as an earthquake could financially weaken a reinsurer, so distribution of risk is a key reinsurance strategy for the company.

The placement of ceded reinsurance is done almost exclusively on an excess of loss basis (per event or per risk) as per practice, actuarial norms and regulatory guidelines. Under such programs, management considers that in order for a contract to reduce exposure to risk, it must be structured to ensure that the reinsurer assumes significant insurance risk related to the underlying reinsured policies and it is reasonably possible that the reinsurer may realize a significant loss from the reinsurance. A measure of transfer of risk is the variability of the potential negative impact of the reinsured losses on the reinsurer's underwriting results. Furthermore, the reinsurance treaties call for timely reimbursement of ceded losses.

TABLE 29

(in millions of dollars, except as noted)	2009	2008
Single risk events[1]		
Net retentions:		
On property policies	**5.0**	5.0
On liability policies		
From January 1st to June 30th	**7.0**	7.0
From July 1st to December 31st	**10.0**	7.0
Multi-risk events and catastrophes		
Net retentions:	**25.0**	25.0
Coverage limit:	**1,500.0**	1,250.0
Risk retained based on the loss exposure:		
$50–$750 million	**10.00%**	10.00%
$25–$50 million	**16.75%**	10.00%
$0–$25 million	**100.00%**	100.00%

1 In a number of cases, like special classes of business or types of risks, the retention would be lower through specific treaties or the use of facultative reinsurance.

Following industry practice, the company's reinsurance recoverables with licensed Canadian reinsurers (December 31, 2009: $208.8 million; December 31, 2008: $175.4 million) are generally unsecured as Canadian regulations require these reinsurers to maintain minimum asset and capital balances in Canada to meet their Canadian obligations, and claims liabilities take priority over the reinsurer's subordinated creditors. Reinsurance recoverables with non-licensed reinsurers (December 31, 2009: $51.8 million; December 31, 2008: $48.8 million) are secured with cash, letters of credit and/or assets held in trust accounts of $74.7 million (2008 – $92.2 million).

9.4 Shareholders' equity

Share capital

As at December 31, 2009 there were 119,906,567 common shares outstanding. Refer to the company's Annual Information Form for more detailed information on the rights of common shareholders.

Long-term incentive plan

Under the company's long-term incentive plan ("LTIP"), certain employees were awarded performance units as part of their compensation. At the end of the performance cycle, the performance units will ultimately be converted to a certain number of restricted common shares to be purchased on the market based on the company's three-year average return on equity compared to the Canadian P&C industry average. In May 2009, the company delivered 53,495 restricted common shares, as required under the LTIP for the three year performance cycle of 2006–2008. For the current ongoing cycles, the total estimate of units accrued by employees is 163,060 as at December 31, 2009.

Accumulated other comprehensive income (loss)

AOCI reflects the unrealized gains or losses related to AFS assets.

TABLE 30

(in millions of dollars)	Pre-tax	Taxes	After-tax
Opening AOCI balance on January 1, 2009	(632.9)	186.8	(446.1)
Changes in fair values during the period	425.2	(140.6)	284.6
Realized losses (gains) reclassified to income during the period	105.5	(8.4)	97.1
AOCI as at December 31, 2009	**(102.2)**	**37.8**	**(64.4)**

Unrealized losses on AFS assets were $632.9 million on January 1, 2009. During the year, the company sold AFS assets resulting in pre-tax realized net losses of $105.5 million. These were transferred to net gains (losses) on invested assets and other gains in the income statement with corresponding increase in AOCI. AFS assets gained value during the year due to favourable capital market conditions, representing a pre-tax increase of $425.2 million in AOCI.

9.5 Liquidity and capital resources

Cash flows

TABLE 31 – CASH FLOWS AND LIQUIDITIES

(in millions of dollars)	Q4 2009	Q4 2008	Change	2009	2008	Change
Selected inflows and (outflows)						
Operating activities:						
Cash provided by operating activities	77.3	230.5	(153.2)	538.0	619.7	(81.7)
Investing activities:						
Net cash inflow (outflow) from sales (purchases) of invested assets	(358.0)	261.5	(619.5)	(1,130.1)	263.7	(1,393.8)
Financing activities:						
Dividends paid	(38.3)	(37.2)	(1.1)	(153.4)	(151.0)	(2.4)
Net proceeds from debt issuance	148.9	–	148.9	397.7	–	397.7
Common shares repurchased for cancellation	–	–	–	–	(176.0)	176.0
Net cash and cash equivalents at the end of the period	60.1	510.4	(450.3)	60.1	510.4	(450.3)

The company's cash flows from operations remain robust. In the fourth quarter of 2009, operating activities generated less cash flow than in the same quarter last year due in part to the timing of claims payments and premiums collections as well as increased tax payments. On an annual basis, the decrease of operating cash flow is related to the decrease in interest and dividend income received and increase in the premium receivable.

Cash provided by operating activities, as well as the proceeds from the debt issuance, were mainly used for the payment of dividends with the remainder reinvested in the company's investment portfolio.

Capital management

The company's objectives when managing capital consist of maintaining sufficient capital to:

– support claims liabilities and ensure the confidence of policyholders,

– support competitive pricing strategies,

– meet regulatory capital requirements,

– provide returns for its shareholders.

The capital of the company is managed on a consolidated basis as well as individually for each regulated subsidiary. The P&C insurance subsidiaries of the company are subject to the regulatory capital requirements defined by OSFI and the Insurance Companies Act ("ICA"). OSFI has established a Minimum Capital Test guideline ("MCT") which sets out 100% as the minimum and 150% as the supervisory target MCT standards for P&C insurance companies. To mitigate the risk of significant adverse market events that could deteriorate its capital position below the supervisory target, the company has established an internal target MCT of 170%.

The following table presents the MCT of the company's insurance subsidiaries with a total for all companies.

TABLE 32 – MINIMUM CAPITAL TEST

MCT – P&C insurance companies

(in millions of dollars, except as noted)	Intact Insurance	Belair Insurance	Nordic Insurance	Novex Insurance	Trafalgar Insurance	Total
At December 31, 2009						
Total capital available	**1,174.3**	**236.3**	**927.4**	**204.6**	**186.6**	**2,729.2**
Total capital required	**533.0**	**93.2**	**401.2**	**79.1**	**70.4**	**1,176.9**
Excess capital	**641.3**	**143.1**	**526.2**	**125.5**	**116.2**	**1,552.3**
MCT %	**220.3%**	**253.4%**	**231.1%**	**258.6%**	**265.0%**	**231.9%**
Excess at 150%	**374.8**	**96.4**	**325.6**	**86.0**	**81.0**	**963.8**
Excess at 170%	**268.2**	**77.8**	**245.3**	**70.1**	**66.9**	**728.4**
At December 31, 2008						
Total capital available	867.5	186.1	673.3	196.3	173.3	2,096.5
Total capital required	454.0	84.2	359.4	66.5	58.9	1,023.0
Excess capital	413.5	101.9	313.9	129.8	114.4	1,073.5
MCT %	191.1%	221.1%	187.4%	295.2%	294.1%	205.0%
Excess at 150%	186.5	59.8	134.3	96.5	84.9	562.0
Excess at 170%	95.7	43.0	62.3	83.3	73.2	357.4

Total capital available and total capital required represent amounts applicable to the company's P&C insurance subsidiaries and are determined in accordance with prescribed OSFI rules. Total capital available mostly represents total equity less specific deductions for disallowed assets including goodwill and intangibles. Total capital required is calculated by allocating assets and liabilities into categories and applying prescribed risk factors to each category. As at December 31, 2009, the company's P&C insurance subsidiaries were in compliance with both OSFI and ICA requirements as well as being above internal targets.

At year end, the company had a total of $858.7 million in excess capital over an MCT of 170%, including $728.4 million in the insurance subsidiaries. This compares to excess capital of $427.5 million at the end of 2008. The increase reflects profitability, the higher market value of the investment portfolio and $400 million in medium term notes issued during the year. This was partly offset by dividends paid to shareholders of $153.4 million and other strategic investments made during the year.

The company has a $150.0 million committed unsecured credit facility, on which it has not drawn any amount, which is also available to provide additional capital flexibility. This facility matures on December 31, 2010.

MCT monitoring

Annually the company performs dynamic capital adequacy testing on the MCT to ensure that it has sufficient capital to withstand significant adverse event scenarios. These scenarios are reviewed each year to ensure appropriate risks are included in the testing process. The 2009 results indicated that the company's capital position is strong. In addition, the target, actual and forecasted capital position of the company is subject to ongoing monitoring by management using stress and scenario analysis to ensure its adequacy.

The MCT is impacted by many factors including changes in 1) market value of the company's invested assets, 2) mix of invested assets, and 3) net income.

Based on the company's MCT of 231.9% at year end, a 10% increase or decrease in the market value of the company's portfolio of common shares would result in a 0.4 percentage point respective increase or decrease in the MCT, all else being equal. Similarly, a 10% increase or decrease in the market value of the company's preferred share portfolio would have a 6.7 percentage point respective increase or decrease in the MCT, all else being equal.

Rating agencies

IFC is rated by A.M. Best, Moody's and DBRS. The A.M. Best rating is the key financial strength rating specific to P&C insurance companies and is used primarily by brokers, businesses and consumers to assess the financial strength and stability of insurance providers when making a decision to buy insurance. All the agencies have provided Issuer Credit ratings and have specifically rated the company's unsecured medium term notes. The company is committed to maintaining its current ratings.

TABLE 33 – FINANCIAL STRENGTH RATINGS

	A.M. Best	Moody's
Insurance subsidiaries of Intact Financial Corporation	A+	Aa3
	Affirmed on June 2, 2009	Affirmed on August 17, 2009

TABLE 34 – CREDIT RATINGS

	A.M. Best	Moody's	DBRS
Intact Financial Corporation	a-	A3	A (low)
	Affirmed on June 2, 2009	Affirmed on August 17, 2009	Affirmed on August 27, 2009

9.6 Financing

Medium term notes

During 2009, the company completed two offerings (Series 1 and Series 2) of unsecured medium term notes (the "Notes").

TABLE 35 – MEDIUM TERM NOTES OFFERINGS

	Medium term notes	
	Series 1	Series 2
Date issued	**August 31, 2009**	**November 23, 2009**
Maturity date	**September 3, 2019**	**November 23, 2039**
Principal amount outstanding	**$ 250.0**	**$ 150.0**
Carrying value	**$ 248.7**	**$ 149.0**
Fair value	**$ 252.8**	**$ 146.5**
Fixed annual rate	**5.41%**	**6.40%**
Semi-annual coupon payment due each year on:	**March 3, September 3**	**May 23, November 23**

The company determined that its optimal balance sheet should have debt representing up to 20% of total capital. The company expects to reach this level over time but the timing of future debt issuances will depend on prevailing market conditions and the need for funds. A debt to total capital ratio up to 20% is within the limits set out under the credit facility (below) and by the rating agencies to maintain the company's current ratings. As at December 31, 2009, the debt to total capital ratio was approximately 11.8%. $100 million remains available under the Medium Term Notes base shelf prospectus filed in May 22, 2009.

The company's primary purpose for raising debt capital is acquisitions. We may however raise capital independent of any specific acquisition, to take advantage of market opportunities and to optimize the cost of funds. If suitable acquisitions do not materialize in a reasonable time period, the company may consider other uses of the funds, including share repurchase. In the meantime, the proceeds from the issues are invested in the company's investment portfolio.

Credit facility

Effective December 1, 2009, the company extended its unsecured committed credit facility of $150.0 million (2008 – $150.0 million) to December 31, 2010. This credit facility may be drawn as prime loans at the prime rate plus a margin or as bankers' acceptances at the bankers' acceptance rate plus a margin. Under the term of the facility, the company must maintain a debt to total capital ratio of 20% or less and maintain an interest coverage ratio of 3 to 1. At December 31, 2009 the company had not drawn down under the facility and is in full compliance with the covenants of the facility.

9.7 Contractual obligations

TABLE 36

(in millions of dollars)	Total	Payments due by period: Less than 1 year	1–3 years	4–5 years	After 5 years
Debt outstanding	**400.0**	–	–	–	400.0
Interest on debt outstanding	**400.2**	23.1	46.3	46.3	284.5
Claims liabilities	**2,685.1**	1,109.0	730.3	461.8	384.0
Operating leases	**361.7**	62.7	119.8	79.1	100.1
Pension obligations[1]	**74.9**	10.6	16.3	12.6	35.4
Total contractual obligations	**3,921.9**	1,205.4	912.7	599.8	1,204.0

1 These amounts represent the annual mandatory funding required by OSFI, based on December 31, 2008 actuarial valuations.

9.8 Off-balance sheet arrangements

Securities lending

The company participates in a securities lending program to generate fee income. This program is managed by the company's custodian, a major Canadian financial institution, whereby the company lends securities it owns to other financial institutions to allow them to meet their delivery commitments. As at December 31, 2009 the company has loaned securities (which are reported in Invested assets on the company's consolidated balance sheet) with a fair value of $1,002.2 million (2008 – $1,587.9 million)

Collateral is provided by the counterparty and is held in trust by the custodian for the benefit of the company until the underlying security has been returned to the company. The collateral cannot be sold or re-pledged externally by the company, unless the counterparty defaults on its financial obligations. Additional collateral is obtained or refunded on a daily basis as the market value of the loaned securities fluctuates. The collateral consists of government securities with an estimated fair value of 105% of the fair value of the loaned securities and amounts to $1,052.3 million at December 31, 2009 (2008 – $1,688.0 million).

SECTION 10 – Accounting and disclosure matters

10.1 Disclosure controls and procedures

The company is committed to providing timely, accurate and balanced disclosure of all material information about the company and to providing fair and equal access to such information. The company's management is responsible for establishing and maintaining the company's disclosure controls and procedures to ensure that information used internally and disclosed externally is complete and reliable. Due to the inherent limitations in all control systems, an evaluation of controls can provide only reasonable, not absolute assurance, that all control issues and instances of fraud or error, if any, within the company have been detected. The company continues to evolve and enhance its system of controls and procedures.

Management, at the direction and under the supervision of the Chief Executive Officer and the Chief Financial Officer of the company, has evaluated the effectiveness of the company's disclosure controls and procedures. The evaluation was conducted in accordance with the requirements of National Instrument 52-109 of the Canadian Securities Administrators. This evaluation confirmed, subject to the inherent limitations noted above, the effectiveness of the design and operation of disclosure controls and procedures as at December 31, 2009. The company's management can therefore provide reasonable assurance that material information relating to the company and its subsidiaries is reported to it on a timely basis so that it may provide investors with complete and reliable information.

10.2 Internal controls over financial reporting

Management, at the direction and under the supervision of the Chief Executive Officer and the Chief Financial Officer of the company, has designed and is responsible for maintaining adequate internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP and the requirements of National Instrument 52-109 of the Canadian Securities Administrators.

Management, at the direction and under the supervision of the Chief Executive Officer and the Chief Financial Officer of the company, assessed the effectiveness of internal controls over financial reporting and, based on that assessment, concluded that internal controls over financial reporting were effective as at December 31, 2009. There have been no changes in the company's internal controls over financial reporting during the year ended December 31, 2009 that have materially affected, or are reasonably likely to materially affect, the company's internal controls over financial reporting.

10.3 Related-party transactions

Subsequent to the disposal by ING Groep of its shareholding in the company, all related-party transactions are with entities associated with the company's distribution segment. These transactions consist mainly of commissions for brokerage services and interest revenue from loans.

These transactions are carried out in the normal course of operations and are measured at the amount of consideration paid or received as established and agreed by the related parties. Management believes that such exchange amounts approximate fair value.

Notes 1 and 19 of the accompanying audited consolidated financial statements provide additional information on related-party transactions.

10.4 Critical accounting estimates and assumptions

The company's significant accounting policies are disclosed in Note 3 to the company's audited consolidated financial statements. The preparation of the company's consolidated financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the amounts reported in its consolidated financial statements. These estimates and assumptions principally relate to the establishment of the fair value of policy liabilities, financial instruments, impairment losses, income taxes, employee future benefits, goodwill and intangibles. As more information becomes known, these estimates and assumptions could change and impact future results. The most significant estimates and assumptions management makes in preparing the company's financial statements are described below. There were no significant changes made to the company's assumptions over the past two years, except for the provision for adverse deviation and the market yield adjustments.

Policy liabilities

Policy liabilities consist of provisions for claims liabilities and premium liabilities, net of reinsurance. The provision for policy liabilities is discounted to take into account the time value of money. It also includes a provision for adverse deviation, as required by Canadian accepted actuarial practice. The appointed actuary of the company's P&C insurance subsidiaries, using appropriate actuarial techniques, evaluates the adequacy of its claims liabilities.

Claims liabilities are maintained to cover the company's estimated ultimate amount to settle 1) insured losses with respect to reported and unreported claims incurred as of the end of each accounting period and 2) claims expenses. The provision for claims liabilities is first determined on a case-by-case basis as claims are reported and then reassessed as additional information becomes known. The provision also considers future possible development of claims. Such reserves do not represent an exact calculation of liability, but instead represent estimates developed using projection techniques in accordance with Canadian accepted actuarial practice. The estimates used are related to 1) expectations of the ultimate cost of settlement and administration of claims based on management's assessment of facts and circumstances then known, 2) its review of historical settlement patterns, 3) estimates of trends in claims severity and frequency, 4) recent legal decisions and other factors such as changes in the legislation and taxation.

Net claims liabilities are discounted using a rate that reflects the estimated market yield of the underlying assets backing these claims liabilities. Several actuarial assumptions are used to calculate this discount rate. These may change from period to period in order to arrive at the most accurate and representative market yield based discount rate. Accordingly, the company continuously improves the market yield estimate over the recent years to better match the varied duration of liabilities.

Variables in the reserve estimation process can be affected by both internal and external events, such as changes in claims handling procedures, 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. Reserve 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 provisions may not be sufficient. Adjustments to reserves, both positive and negative, are reflected in the statement of income of the period in which such estimates are updated. See table 8.4 in the audited consolidated annual financial statements.

Premium deficiency

Unearned premiums are calculated on a pro rata basis, from the unexpired portion of the premiums written. The unearned premiums estimate is validated through standard actuarial techniques to ensure that these premiums are sufficient to cover the estimated future costs of servicing these policies and related claims. Premium liabilities are considered adequate when the unearned premiums reserve (after deducting any deferred acquisition cost asset) is at least equal to the present value, at the balance sheet date, of cash flows of the claims, expenses and taxes to be incurred after that date on account of the policies in force at that date or at an earlier date.

Deferred acquisition costs comprise commissions, premium taxes and expenses directly related to policy issuance. Such costs are deferred to the extent that they are recoverable from unearned premiums, after considering the anticipated claims, expenses and interest and dividend income in respect of these premiums. They are amortized on the same basis as the premiums and are reported in commissions, premium taxes and general expenses on the Consolidated statements of income.

A premium deficiency would be recognized immediately by a charge to the statement of income as a reduction of deferred acquisition costs to the extent that the unearned premiums reserve, plus anticipated invested assets income, is not adequate to recover all deferred acquisition costs and related claims and expenses. If the premium deficiency was greater than unamortized deferred acquisition costs, a liability would be accrued for the excess deficiency.

Reinsurance

Reinsurance recoverables include amounts for expected recoveries related to claims liabilities as well as the portion of the reinsurance premium which has not yet been earned. The cost of reinsurance is accounted for over the terms of the underlying reinsured policies using assumptions consistent with those used to account for the policies. Amounts recoverable from reinsurers are estimated in a manner consistent with claims liabilities and are reported in the company's consolidated balance sheet. The ceding of insurance does not discharge the company's primary liability to its insureds. An estimated allowance for doubtful accounts is recorded on the basis of periodic evaluations of balances due from reinsurers, reinsurer solvency, management's experience and current economic conditions.

Structured settlements

The company enters into annuity agreements with various Canadian life insurance companies to provide for fixed and recurring payments to claimants. Under such arrangements, the company derecognizes the liability from its Consolidated balance sheet as the liability to its claimants is substantially discharged, although the company remains exposed to the credit risk that life insurers fail to fulfill their obligations. Refer to Note 7 Risk and capital management of the consolidated financial statements for further details.

Fair value of financial instruments

The fair value of a financial instrument on initial recognition is normally the transaction price, i.e. the fair value of the consideration given or received. Subsequent to initial recognition, the fair values of financial instruments are determined based on available information and the fair values hierarchy as follows:

Level 1

Level 1 are financial assets and liabilities that the company measures by reference to published quotes in an active market (i.e. the bid price for a financial asset and the ask price for a financial liability). A financial instrument is regarded as quoted in an active market if quoted prices for that financial instrument are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis. When a quoted active market exists, the fair values of financial assets are based on bid prices and the fair values of financial liabilities are based on ask prices.

Level 2

In the absence of an active market, fair values are determined by the company based on prevailing market rates for instruments with similar characteristics and risk profiles or the fair values are determined by using valuation techniques commonly used by the market participant, which refer to observable market data. Fair values determined using valuation models require the use of assumptions concerning the amount and timing of estimated future cash flows and discount rates. In determining those assumptions, the external readily observable market inputs are primarily looked at, including factors such as interest rate yield curves, currency rates, and price and rate volatilities, as applicable. Valuation techniques commonly used by the company include comparisons with similar instruments where observable market prices exist, discounted cash flow analysis and option pricing models.

Level 3

In limited circumstances, the company uses input parameters that are not based on observable market data with an adjustment to reflect the uncertainty and to ensure that financial instruments are reported at fair values. Liquidity risks, relating to market prices that are not observable due to insufficient trading volume or a lack of recent trades in a less active or inactive market, will be inherent in the cash flows of an asset or liability that are factored into the valuation techniques when measuring fair value.

The split of the company's financial instruments between each of the above mentioned levels is presented in Note 6 of the consolidated financial statements.

If the fair value of a financial asset measured at fair value becomes negative, it is recorded as a financial liability until its fair value becomes positive at which time it is recorded as a financial asset, except when extinguished. These changes in classifications occur mainly to derivative financial instruments. Derivative financial instruments with positive fair values are reported in Other receivables and those with negative fair values are reported in Other liabilities. See table 5.1 in Note 5 to the consolidated financial statements for more details.

Establishing fair value is a critical accounting estimate and has an impact on held-for-trading securities, AFS financial assets and liabilities and in the consolidated financial statements. This estimate also has an impact on Interest income and Net investment losses in the consolidated statement of income and Other comprehensive income in the Consolidated Statement of Comprehensive income.

Impairment of financial assets

The company assesses impairment, as follows:

Financial assets other than held-for-trading are assessed for impairment at each balance sheet date. Impairment exists when there is objective evidence of an other-than-temporary ("OTT") decline in fair value below cost.

Common shares: A quantitative assessment is made to identify shares which have had a significant or prolonged decline in fair value. Management then applies judgment based on each issuer's financial condition to determine whether objective evidence of impairment exists.

Fixed income securities and preferred shares: These financial assets are impaired when there is evidence which suggests that the issuer will fail to make the contractual interest or principal payments due under the terms of the instrument. Possible impairment indicators include significant financial difficulty, a downgrade in credit rating or bankruptcy and financial reorganization. An impairment loss relating to an available-for-sale fixed income security is reversed when, in a subsequent period, the fair value of the instrument increased and the increase can be objectively related to an event occurring after the impairment loss was recognized.

All impairment losses and reversals are recognized in Net investment losses in the Consolidated statements of income in the period in which they occur.

Members of the company's investment, finance and accounting departments meet quarterly to assess impairments. Management assesses which of these securities are OTT impaired. Any impairment is recognized when the assessment concludes that there is objective evidence of impairment. Each quarter, any security with an unrealized loss that is determined to have been OTT impaired is written down to its published fair value bid price for actively traded securities, with the amount of the write-down reflected in the company's statement of income for that quarter. Previously impaired securities continue to be monitored quarterly, with additional write-downs taken quarterly, if necessary. There are inherent risks and uncertainties involved in making these judgments.

Accounting for embedded derivatives

The company owns perpetual preferred shares with call options which give the issuer the right to redeem the shares at a particular price. Current Canadian GAAP accounting standards require that these options be accounted for separately from the preferred shares which are classified as AFS. Accounting standards also require that changes in the value of the preferred shares are recorded in other comprehensive income (OCI) while changes in the value of the option liability are recorded on the income statement, creating a mismatch. As the preferred shares increased in value during the year, the value of the associated option liability also increased. This change is recorded in Net investment losses on the consolidated statement of income.

The calculation used for evaluating the change in the liability for embedded derivatives is based on the price volatility of the underlying preferred shares. In the past, price volatility was measured over a relatively short time period because 1) preferred share values were fairly static pre-crisis and 2) there was limited market data available upon which to base the measurement due to liquidity. Historically, under normal market conditions, there were not significant changes in the estimated amount of the liability or impact on income. However, market gyrations over the last year created unusual swings in the estimate which management did not believe reflected the actual change in the liability. In the fourth quarter, the calculation was changed to measure the price volatility of the preferred share over a longer time period to more accurately estimate the change in the embedded derivative liability.

The International Accounting Standard Board (IASB) has recently issued a standard, IFRS 9 "Financial Instruments: Classification and measurement", which effectively changes the accounting treatment for embedded derivatives. The standard no longer permits separate accounting, and requires embedded derivatives to be accounted for on the same basis as the underlying investment (or host contract). When adopted by the company, it will eliminate the current accounting mismatch.

Income taxes

Management exercises judgment in estimating the provision for income taxes. The company is subject to income tax laws in various provincial jurisdictions where it operates. Various tax laws are potentially subject to different interpretations by the taxpayer and the relevant tax authority. To the extent that the company's interpretations differ from those of tax authorities or the timing of realization is not as expected, the provision for income taxes only may increase or decrease in future periods to reflect actual experience.

The income tax expense is comprised of two components: current income taxes and future income taxes. Current income taxes are amounts expected to be payable or recoverable as a result of operations in the current year. Future income taxes arise from changes during the year in cumulative temporary differences between the accounting book values of assets and liabilities and their respective tax bases. A future income tax asset is recognized to the extent that future realization of the tax benefit is more likely than not.

Employee future benefits

Pension plans

We sponsor a number of defined benefits plans providing pension to eligible employees after their retirement. The pension plans provide benefits based on years of service, contributions and average earnings at retirement. Due to the long-term nature of these plans, the calculation of benefit expenses and obligations depends on various assumptions such as discount rates, expected rates of return on assets, projected salary increases, retirement age, mortality and termination rates. All assumptions are determined by management and are reviewed annually by the actuaries. The discount rate assumption used in determining pension and other post employment benefit obligations and net benefit expense reflects the market yields, as of the measurement date on high-quality fixed income securities with cash flows that would provide the necessary cash flows to pay for benefit payments as they become due. The expected return on plan assets assumption is based on expected returns for the various asset classes by portfolio allocation. Anticipated future long term performance of individual asset categories is considered reflecting expected future inflation and expected real yields on fixed income securities and equities. Other assumptions are based on actual plan experience and the company's best estimates.

Post-retirement benefits

The company's obligation for post-retirement benefits extends to the provision of medical, dental and life insurance to approximately one thousand currently retired employees. For other retirees and currently active employees, the company has no post-retirement obligation for medical and dental costs, although the company sponsors a retiree funded medical and dental plan.

The table below summarizes some key pension and other employee benefits data as at December 31, 2009 and 2008:

TABLE 37

	Pension plans		Post-retirement benefits	
(in millions of dollars)	**2009**	2008	**2009**	2008
Benefit obligation	**(560.8)**	(448.7)	**(14.8)**	(15.3)
Fair value of plan assets	**570.7**	459.7	**–**	–
Surplus (deficit)	**9.9**	11.0	**(14.8)**	(15.3)
Unrecognized amounts:				
Actuarial losses	**105.7**	97.9	**2.8**	3.5
Past service costs	**2.2**	2.6	**(4.2)**	(4.7)
Transition (asset) obligation	**(21.1)**	(31.6)	**0.6**	0.7
Valuation allowance	**(0.6)**	(0.8)	**–**	–
Current expense	**11.4**	12.4	**0.7**	0.7

For accounting purposes, at the end of 2009, the company's pension plans were in a surplus position of $9.9 million compared to a surplus of $11.0 million last year. Actuarial valuations based on plan assets and membership information as at December 31, 2009 will be performed during 2010 for some of the plans. Currently, the company's best estimate of annual mandatory funding is in the range of 4% and 7% of total plan assets. This mandatory funding estimate includes an annual contribution requirement in the range of 1%–3% of total plan assets to fund past service deficits.

TABLE 38 – IMPACT OF CHANGES IN KEY ASSUMPTIONS ON PENSION AND OTHER POST-RETIREMENT BENEFITS OBLIGATION

	Obligation	
(in millions of dollars, except as noted)	Pension plans	Post retirement benefits
Impact of a change in 1% in key assumptions:		
Discount rate:		
Increase	(86.8)	(1.4)
Decrease	103.1	1.6
Rate of compensation increase:		
Increase	24.9	n/a
Decrease	(23.7)	n/a

Please refer to Note 12 to the company's audited consolidated financial statements for more details on the company's pension plans and other post-retirement benefits.

Goodwill and intangibles

Under GAAP, goodwill is not amortized but is tested annually for impairment of value on a reporting unit basis. Management's judgment is required to identify reporting units with similar economic characteristics and to select an appropriate valuation model. In the P&C insurance industry and the P&C insurance brokerage industry, it is common for companies to be acquired at a multiple of revenue or book value, adjusted for net assets other than intangibles. A range of values used to evaluate the multiple is developed using discounted cash flow valuation techniques. The models used reflect several management assumptions such as the growth rates and expected returns. Consideration is also given to economic conditions and to general outlook for the industry and markets in which the reporting unit operates. When establishing these assumptions, management adopts a conservative approach. When the fair value of the reporting unit exceeds its carrying value, goodwill is considered not to be impaired. When the carrying value of the reporting unit exceeds its fair value, the fair value of the goodwill is compared with its carrying value to determine the amount of impairment, if any. When the carrying value of goodwill exceeds the fair value of the goodwill, an impairment loss is recognized in the consolidated statements of income in an amount equal to the excess. The company performed its impairment test of goodwill for years ended December 31, 2009 and 2008 and no impairment was identified. An intangible asset is recognized separately from goodwill when it results from contractual or other legal rights or when it is capable of being separated from the acquired enterprise and sold, transferred, licensed, rented, or exchanged. Finite life intangible assets are amortized to the consolidated statements of income over their useful lives whereas infinite life intangible assets are not subject to amortization.

10.5 Significant accounting changes

Goodwill and intangible assets

Effective January 1, 2009, the company applied the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 3064, *Goodwill and Intangible Assets*. This Section replaced CICA Handbook Section 3062, *Goodwill and Other Intangible Assets*, and Section 3450, *Research and Development Costs*, and established standards for the recognition, measurement and disclosure of goodwill and intangible assets. The provisions relating to the definition and initial recognition of intangible assets, including internally generated intangible assets, are equivalent to the corresponding provisions of IAS 38, *Intangible Assets*, of International Financial Reporting Standards ("IFRS").

In applying Section 3064, the company reclassified certain assets from Other assets to Intangibles on the consolidated balance sheets. The comparative amount reclassified as at December 31, 2008 was $79.4 million. This reclassification had no impact on the company's net income for 2009. (See note 11 of the Consolidated financial statements).

Credit risk and the fair value of financial assets and financial liabilities

Effective January 20, 2009, the company applied the Emerging Issues Committee ("EIC") Abstract 173, *Credit Risk and the Fair Value of Financial Assets and Financial Liabilities*, requiring an entity to take into account its own credit risk and that of the relevant counterparties when determining the fair value of financial assets and financial liabilities, including derivative instruments. The adoption of this CICA abstract has not had a significant impact on the company's results or financial condition as credit risks associated with the company's financial assets and liabilities are incorporated into the company's valuation methodology.

Impairment of Financial Assets – Amendments to: Financial Instruments – Recognition and Measurement

On August 20, 2009, the CICA issued various amendments to Section 3855, *Financial instruments, recognition and measurement*, and section 3025, *Impaired loans*, which further reduced differences with IFRS. As a result of these amendments debt instruments not quoted in an active market may be classified as loans and receivables, measured at amortized cost and impairment is assessed using the same model as for impaired loans. In addition, the guidance requires reversing an impairment loss relating to an available-for-sale debt instrument when, in a subsequent period, the fair value of the instrument increased and if the increase can be objectively related to an event occurring after the loss was recognized.

The company adopted these amendments, which required retroactive application to January 1, 2009, in the fourth quarter of fiscal year 2009. The impact of adopting these amendments on the company's consolidated financial statements was the reversal of $2.8 million of impairments that were originally recognized in the first quarter of 2009. The company has decided not to change the classification of any of its debt securities.

Financial Instruments – Disclosures

Effective for the period ended December 31, 2009, the company applied the amended CICA Handbook Section 3862, *Financial Instruments – Disclosures*. This section provides improvements to fair value and liquidity risk disclosures and requires specific disclosure of the fair values hierarchy. Refer to note 6 Fair value measurement of the consolidated financial statements.

10.6 Future accounting changes

Business combinations, consolidated financial statements and non-controlling interest

In January 2009, the CICA issued three accounting standards: Section 1582, *Business Combinations*, Section 1601, *Consolidated Financial Statements*, and Section 1602, *Non-controlling Interests*, to converge the accounting for business combinations and the reporting of non-controlling interest to IFRS.

The recommendations of Section 1582, *Business Combinations*, which replaces Section 1581, *Business Combinations*, will be effective for acquisitions completed on or after January 1, 2011. This section establishes guidance on the recognition and measurement basis of all assets and all liabilities acquired through a business combination.

The recommendations of Section 1601, *Consolidated Financial Statements*, and Section 1602, *Non-controlling Interests*, which together replace Section 1600, *Consolidated Financial Statements*, also become effective on January 1, 2011. These standards establish guidance on the accounting and presentation for non-controlling interests and for transactions affecting non-controlling interests. Early adoption is permitted but standards must be adopted concurrently.

The company plans to adopt these sections effective January 1, 2011.

International financial reporting standards

The Canadian Accounting Standards Board ("AcSB") has confirmed January 1, 2011 as the date IFRS will replace current Canadian standards and interpretations as Canadian generally accepted accounting principles (Canadian GAAP) for publicly accountable enterprises. In order to prepare and implement the conversion to IFRS, the company has developed an IFRS changeover plan. As the implementation process moves forward, the company will continue to monitor and amend the changeover plan as appropriate, especially as new IFRS exposure drafts or standards expected to impact the company are released. The company completed its assessment of the October 2009 OSFI Draft Advisory titled "Conversion to International Financial Reporting Standards (IFRSs) by Federally Regulated Entities (FREs)" and has incorporated the requirements of the Draft Advisory in its changeover plan.

The following table outlines the remaining key activities of the company's IFRS changeover plan and its milestones.

TABLE 39

Key activity	Milestones/deadline	Effort accomplished/remaining effort to complete
Identification of differences in Canadian GAAP/IFRS accounting policies, choices and financial reporting requirements: • Selection of IFRS 1 accounting policy transition choices • Selection of entity's continuing IFRS policies • Quantification of effects of: (1) transition choices (IFRS 1) (2) continuing IFRS accounting policies selection (3) new and enhanced IFRS disclosures • Financial statement presentation format	• IFRS 1 transition choices and critical continuing accounting policy choices made by the end of the 1st quarter of 2010. • Maintaining parallel IFRS shell financial statements in 2010 for IFRS comparatives reporting purposes for the year ended 2011.	• The IFRS 1 transition choices have been presented to senior management and to the company's Audit and Risk Review Committee. • The key accounting policy differences between IFRS and Canadian GAAP have been identified, assessed and quantified (See table 40 below). • The company is ready to make these transition choices and policy elections before the end of the 1st quarter 2010. • An initial preliminary draft of IFRS Financial Statements with notes including the company's continuing IFRS significant accounting policies note have been prepared and presented to the company's technical accounting policies team. • Parallel IFRS financial statements will be prepared throughout 2010.
IFC IFRS expertise: Identification of needs throughout the company • Development and education at level of Operating division accounting staff • Other non-accounting departments: Actuarial, legal, tax, information technology, internal audit, etc. • Senior Executive and Board level, including Audit Committee	• Deliver IFRS training to Operating division accounting staff. • Assessments and training sessions with other departments completed by approximately the end of 2nd quarter 2010. • Quarterly reporting to Audit and Risk Review Committee throughout 2010.	• A technical accounting policies team was formed, comprising accounting professionals from within the company who have a sound knowledge of accounting standards and the company's operations. • The team has partnered with the relevant functional areas of the company, including tax, capital management and actuarial services, to assess and provide education on the specific and overall impact of IFRS. • The team held various training sessions and awareness seminars across the company. On a quarterly basis, an IFRS update is presented to the members of the company's Audit and Risk Review Committee.
Information technology: • Systematic processing changes • Program upgrades/changes • One-off calculations (IFRS 1) • Disclosure data gathering • Budget/plan/forecast monitoring process	• Enable opening financial position to be established under IFRS during the 1st quarter 2010. • Ready for parallel processing during the 1st quarter 2010.	• Scoping study completed: resource assessment underway. • Accounting system is ready for 2010 parallel processing. • IFRS 1 one-off calculation requirements have been identified and the company's technical accounting policies team has been engaged to perform the final quantification. • Key IFRS disclosures have been identified and disclosure data gathering processes have been initiated with various departments across the company. • Overall no significant system retooling is required to ensure availability of data required for IFRS reporting.
Control environment: • Controls on accounting policy determination, documentation and implementation • Independent review of applications	• Review by the Audit and Risk Review Committee of all significant accounting policy changes by the end of the 3rd quarter 2010.	• Minimum impact is expected as the company has identified few differences in IFRS vs. Canadian GAAP.
Communication to investors: • Investor day in 2010 to communicate reported earnings and future earnings impacted by the IFRS changes to investors and other stakeholders of the company	• Impact of IFRS changes to be presented at the annual investor day presentation to be held during 2010.	• The presentation material for the Investor day will be prepared in the first half of 2010.
Business policy assessment: • Financial covenants and practices • Customer and supplier contract evaluation • Compensation arrangements	• Review completed by the end of the 2nd quarter 2010.	• Minimum impact is expected as the company has identified few relevant GAAP-dependent covenants and contracts.

The company has identified the following IFRS standard choices and accounting policy differences between Canadian GAAP and IFRS as having the largest potential impacts on the company's financial statements:

TABLE 40

Accounting policy	Differences	Potential impacts
Employee benefits (Defined benefit pension plans)	**On transition to IFRS:** First-time adopters can elect to recognize all cumulative actuarial gains and losses at the date of transition as an adjustment to opening retained earnings. Alternatively, entities may elect an IFRS "corridor approach" to leave some actuarial gains and losses unrecognised, as if an IFRS "corridor approach" had always been applied.	The company has elected to recognize all cumulative actuarial gains and losses at the date of transition as an adjustment to retained earnings. The company is currently working at finalizing the transition amount with the help of its actuaries but preliminary estimates indicate that this election would reduce the company's shareholders' equity in the range of \$50–\$70 million.
	Post transition to IFRS: Entities have the choice of recognizing ongoing actuarial gains or losses in profit or loss over time using the "corridor approach", or alternatively, immediately to comprehensive income.	Actuarial gains or losses recognized immediately to comprehensive income are likely to create more volatility in the balance sheet than if the "corridor approach" is chosen as they will be accounted for directly in shareholders' equity as incurred. The company completed the impact assessment that these choices will have on the company's consolidated financial statements. The company is ready to make a choice during the 1st quarter of 2010.
Financial instruments	**On transition to IFRS:** First-time adopters can also choose to (re-)classify their financial assets and financial liabilities at the transition date. As example, first time adopters could choose to reclassify previously classified held-for-trading assets to available-for-sale assets.	The company does not expect to change its investments classification.
	Post transition to IFRS: The company's accounting for financial instruments is for the most part similar to IFRS. One exception is that IFRS requires the foreign exchange gains/losses on monetary items to be recognized immediately in the profit and loss (currently under Canadian GAAP, these gains/losses are presented in the other comprehensive income as part of the balance sheet).	The company is currently working at finalizing the transition amount but preliminary estimates indicate that the impact on the company's shareholders' equity shall be nil.
	Future accounting changes: IASB is currently revisiting the accounting rules pertaining to financial instruments. The IASB's tentative project plan for the replacement of IAS 39 consists of three phases: **Phase 1: Classification and measurement.** On November 12, 2009, the IASB published IFRS 9 *Financial Instruments* on the classification and measurement of financial assets. This revised standard is expected to be effective for the company from January 1, 2012. **Phase 2: Impairment methodology.** On June 25, the Board published a Request for Information on the feasibility of an expected loss model for the impairment of financial assets. The input assisted the IASB in developing the exposure draft published in November 2009. **Phase 3 – Hedge accounting.** The Board is currently conducting outreach with its constituents and intends to issue an exposure draft on hedge accounting in the first quarter of 2010.	The company is currently monitoring and assessing the impacts the adoption of these (and further) amendments will have on its consolidated financial statements. The company's early assessment indicates that the proposed amendments would affect how the company classifies and measures its financial instruments, including its embedded derivatives which are discussed in section 10.4.

SECTION 11 – Risk management

11.1 Introduction

We have a comprehensive risk management framework and internal control procedures designed to manage and monitor various risks in order to protect our business, clients, shareholders and employees. Our risk management programs aim at avoiding risks that could materially impair our financial position, accepting risks that contribute to sustainable earnings and growth and disclosing these risks in a full and complete manner.

Effective risk management rests on identifying, understanding and communicating all risks the company is exposed to in the course of its operations. In order to make sound business decisions, both strategically and operationally, management must have continual direct access to the most timely and accurate information possible. Either directly or through its committees, the Board of Directors ensures that the company's management has put appropriate risk management programs in place. The Board of Directors, directly and in particular through its Audit and Risk Review Committee ("Audit Committee"), oversees the company's risk management programs, procedures and controls and, in this regard, receives periodic reports from, among others, the risk management department through the Chief Risk Officer, internal auditors and the independent auditors. A summary of the company's key risks and the processes for managing and mitigating them is outlined below.

The risks described below and all other information contained in our public documents including our financial statements and notes should be considered carefully. The risks and uncertainties described below are those we currently believe to be material, but they are not the only risks and uncertainties we face. If any of these risks, or any other risks and uncertainties that we have not yet identified, or that we currently consider to not be material, actually occur or become material risks, our business prospects, financial condition, results of operations and cash flows could be materially adversely affected.

While the company employs a broad and diversified set of risk mitigation techniques those techniques and the judgments that accompany their application cannot anticipate every economic and financial outcome in all market environments or the specifics and timing of such outcomes.

11.2 Governance structure

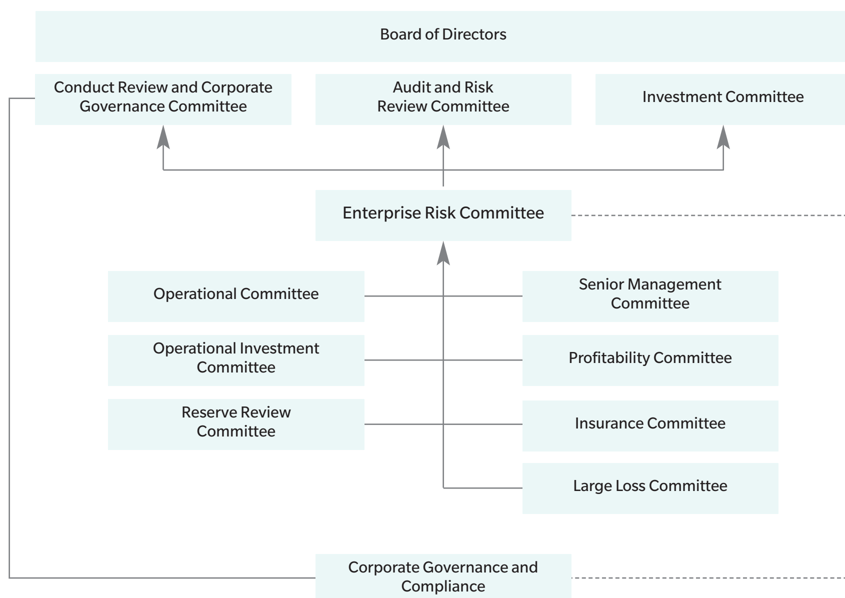
The Board of Directors is ultimately responsible for overseeing the company's risk-taking activities and risk management programs and is supported by the following committees and department to ensure that risks are being properly measured, monitored and reported:

- ***Audit and Risk Review Committee:*** this committee is composed exclusively of independent members of our Board of Directors and is chaired by an independent director. In addition to its audit committee functions, which include the review of financial information and the monitoring of internal controls, this committee reviews trends and key risk positions and exposures, risk management programs, practices and internal controls and compliance with key operational risk policies and limits.
- ***Conduct Review and Corporate Governance Committee:*** this committee is composed of a majority of independent members of our Board of Directors and is chaired by an independent director. This committee reviews, approves or makes recommendations to our Board of Directors with respect to related party transactions, compliance and market conduct programs and policies, including the resolution of conflicts of interests, and restrictions on the use of confidential information.
- ***Investment Committee:*** this committee is composed of a majority of independent members of our Board of Directors with expertise in capital markets and related areas and is chaired by an independent director. The role of this committee is to advise the company on the investment strategies that are appropriate in the context of the company and its subsidiaries' activities. The main functions of this committee are to recommend to the Board of Directors the adoption of investment policies aimed at supporting the company and its subsidiaries in meeting their financial obligations while optimizing risk and return, and minimizing the potential for large losses.
- ***Enterprise Risk Committee*** (see figure 1): this committee is composed of senior officers and is chaired by the Chief Risk Officer designated by our Board of Directors. It meets at least six times a year and oversees and endorses our risk management priorities, assesses the effectiveness of risk management programs, policies and actions of each key function of our business and reports on an ongoing basis to the Chief Executive Officer, quarterly to the audit committee, and at a minimum annually to our Board of Directors. The committee evaluates our overall risk profile, aiming for a balance between risk, return, and capital, and determines policies concerning security and information technology risk, crisis and business continuity risks and reputation risk. The committee is mandated to: (i) identify risks that could materially affect our business; (ii) measure risks from a financial or other impact standpoint, such as reputation; (iii) monitor risks; and (iv) avoid taking risks if they are not in line with the risk tolerance level determined by our Board of Directors.

– ***Corporate Governance and Compliance Department:*** this department, under the direction of the Chief Legal Officer, acts independently from operations for various functions, including privacy matters, dealings with the Ombudsman office and public company matters, and reports directly to a committee of the Board of Directors for these functions. This department works closely with and reports any issues or risks it identifies in the course of its functions to, the risk management function.

In addition, the company has other committees responsible for managing, monitoring and reviewing specific aspects of risk related to our operations, investments, profitability, insurance operations, security and business continuity. Further details on how these committees operate, ensure compliance with laws and regulations and report to the Enterprise Risk Committee follow.

FIGURE 1: RISK MANAGEMENT STRUCTURE



11.3 Corporate governance ensuring compliance with laws and regulatory requirements

The company believes that sound corporate governance and compliance monitoring related to legal and regulatory requirements are paramount for maintaining the confidence of different stakeholders including its investors. Legal and regulatory compliance risk arises from non-compliance with the laws, regulations or guidelines applicable to the company as well as the risk of loss resulting from non-fulfilment of a contract. The company is subject to strict regulatory requirements and detailed monitoring of its operations in all provinces and territories where it conducts business, either directly or through its subsidiaries. The company's corporate governance and compliance program is built on the following foundations:

– The Board of Directors and its committees are structured in accordance with sound corporate governance standards. Directors are presented with relevant information in all areas of the company's operations to enable them to effectively oversee the company's management, business objectives and risks.

– Disclosure controls and processes have been put into place so that relevant information is obtained and communicated to senior management and the Board of Directors to ensure that the company meets its disclosure obligations while protecting the confidentiality of information. A decision-making process through the Disclosure Committee is also in place to facilitate timely and accurate public disclosure.

– Effective corporate governance depends on sound corporate compliance structures and processes. The company has established an enterprise-wide Compliance Policy and framework including procedures and policies necessary to ensure adherence to laws, regulations and related obligations. Compliance activities include identification, mitigation and monitoring of compliance/reputation risks, as well as communication, education, and activities to promote a culture of compliance and ethical business conduct. In this regard, the company recently launched an internal campaign promoting and reaffirming the company's five core values, which are: integrity, respect, customer driven, excellence and social responsibility.

- The Board of Directors and the Audit Committee periodically receive reports on all important litigation, whether in the ordinary course of business where such litigation may have a material adverse effect, or outside the ordinary course of business.
- To manage the risks associated with compliance, regulatory, legal and litigation issues, the company has specialized resources, reporting to the Chief Legal Officer that remain independent of operations. The Chief Legal Officer reports directly to the CEO and to the Board of Directors and its Committees on such matters, including with respect to privacy and Ombudsman complaints. The company also uses third party legal experts and takes provisions when deemed necessary or appropriate.

While senior management has ultimate responsibility for compliance, it is a responsibility that each individual employee shares. This is clearly set out in Intact's core Business Values and Code of Conduct and employees sign a confirmation that they have reviewed and complied with them annually.

11.4 Corporate governance ensuring risk management

Our internal structure is designed in order for the risk related teams, together with operations, to build a sustainable competitive advantage by fully integrating risk management in our daily business activities and strategic planning. Intact believes that each of the employees and management teams is responsible for taking the appropriate action to mitigate risks and ensure compliance with all legal and regulatory requirements:

- Heads of departments have primary responsibility and accountability for the effective control of risks/challenges affecting their respective departments. They are responsible for the execution of the operational risk management policies set by the Enterprise Risk Committee.
- Operational risk management members exercise their functions to partner with and support heads of department in the execution of risk management activities. Risk management oversight functions are carried out independently from the management team that originate the risk exposures. Examples of typical activities are:
  - Overseeing and objectively challenging the execution of risk management activities;
  - Monitoring the key risks of the business;
  - Having the authority to escalate risk management issues to a higher level and vetoing high risk business activity;
  - Allocating specific accountability for risk responses;
  - Enforcing compliance with the risk policies.
- The Internal Audit department provides an independent review of the design and effectiveness of internal controls over the company's business operational risks. In carrying out this work, this department provides specific recommendations for improving the governance, risk and control framework.
- The Corporate governance and compliance department reviews, analyzes and reports current and developing legal and regulatory requirements in order to ensure continued compliance.

11.5 Main risk factors and mitigating actions

The company's main risk factors together with the company's risk management practices used to mitigate these risks are explained below.

Investment related risks

Market risk

Movements in short-term and long-term interest rates, credit spreads, foreign exchange rates and equity prices cause changes in realized and unrealized gains and losses. Generally, the company's interest and dividend income will be reduced during sustained periods of lower interest rates and will likely result in unrealized gains in the value of fixed income securities the company continues to hold, as well as realized gains to the extent the relevant securities are sold. During periods of rising interest rates, the fair value of the company's existing fixed income securities will generally decrease and its realized gains on fixed income securities will likely be reduced or result in realized losses. Changes in credit spreads would have similar impacts as those described above for changes in interest rates.

General economic conditions, political conditions and many other factors can also adversely affect the equity markets and, consequently, the fair value of the equity securities the company owns and ultimately affect the timing and level of realized gains or losses. The recent financial crisis provides an example of an event with a significant adverse impact on the company's financial condition. During the crisis, several financial institutions failed or received government assistance and many others experienced significant distress. Most equity investments and some corporate fixed income securities declined significantly in value while sovereign government bond yields fell. Some of the company's investments were negatively impacted by these events resulting in losses.

While our strategy is long-term in nature, it is reviewed periodically to adapt to the investment environment when necessary, especially in times of turbulence and increased volatility. For example, the company employed several risk mitigation measures during the financial crisis. Specifically, the company implemented changes to its strategic asset mix, implemented a financial hedging program and increased holdings in cash. These actions reduced exposure to common shares and decreased the sensitivity of the MCT ratio to fluctuations in the equity markets.

Sensitivity analysis is one risk management technique that assists management in ensuring that risks assumed remain within the company's risk tolerance level. Sensitivity analysis involves varying a single factor to assess the impact that this would have on the company's results and financial condition.

For example, a 100 basis point increase in interest rates would increase income before taxes by approximately $21.9 million for the company's AFS fixed income securities or preferred securities, as a result of marking to market the written call option liabilities embedded in the company's redeemable preferred shares. A 100 basis point increase would also decrease OCI by approximately $219.3 million. Conversely, a 100 basis point decrease in interest rates would lower income before taxes and increase OCI by the same amounts, respectively.

Furthermore, a 10% increase in equity markets, excluding the impact of any impairment, would have no impact on income before taxes. However, it would result in a linear increase of OCI by $53.6 million. Excluding the impact of any impairment, a 10% decrease in equity prices would have the corresponding opposite effect, lowering OCI by the same amount.

The above sensitivity analyses were prepared using key assumptions as described below:

- the securities in the company's portfolio are not impaired;
- interest rates and equity prices move independently;
- shifts in the yield curve are parallel;
- credit and liquidity risks have not been considered;
- for our HFT debt securities, the estimated impact on income before taxes is assumed to be offset by the MYA. In addition, it is important to note that AFS securities in an unrealized loss position, as reflected in OCI, may at some point in the future be realized either through a sale or impairment.

The company also uses stress tests to determine the impact of various market scenarios on its financial and capital position. (See MCT monitoring discussion in Section 9.5 Liquidity and capital resources.)

To mitigate these risks, the company's investment policies set forth limits for each type of investment and compliance with the policies is closely monitored by the Investment Committee. The company manages market risk through asset class and economic sector diversification and, in some cases, the use of derivatives. The company also monitors and reviews the duration of its fixed income securities and its policy liabilities to ensure any duration mismatch is within acceptable tolerances.

The rate of currency exchange may also have an unintended effect on earnings and equity when measured in domestic currency. Although the company is exposed to some foreign exchange risks arising from securities in some of its U.S. dollar-denominated assets, the general policy is to minimize foreign currency exposure. The company mitigates foreign exchange rate risks by buying or selling successive monthly foreign exchange forward contracts or entering into foreign exchange swaps.

Credit risk

Credit risk is the possibility that counterparties may not be able to meet payment obligations when they become due. A counterparty is any person or entity from which cash or other forms of consideration are expected to extinguish a liability or obligation to us. The company's credit risk exposure is concentrated primarily in its fixed income, preferred share portfolios, over the counter derivatives and, to a lesser extent, in its reinsurance recoverables and annuity agreements entered into with various life insurance companies.

The company's risk management strategy is to invest in fixed income instruments and preferred shares of high credit quality issuers and to limit the amount of credit exposure with respect to any one issuer by imposing limits based upon credit quality. See Tables 17 and 18 for more details on the breakdown of credit quality of fixed income securities and preferred shares. In addition, the company sets limits on the total credit exposure across all asset classes including both on and off balance sheet exposures.

Concentration of credit risk exists where a number of borrowers or counterparties are engaged in similar activities, are located in the same geographic area or have comparable economic characteristics. Their ability to meet contractual obligations may be similarly affected by changing economic, political or other conditions. The company's invested assets could be sensitive to changing conditions in specific geographic regions or specific industries. The company has a significant concentration of its invested assets in the financial sector. This risk concentration is closely monitored by the company and it hedges some of the risk as it deems necessary. See Tables 15 and 16 for more details on the breakdown of invested assets by economic sector.

Credit risk from derivative transactions reflects the potential for the counterparty to default on its contractual obligations when one or more transactions have a positive market value to the company. Therefore, derivative-related credit risk is represented by the positive fair value of the instrument and is normally a small fraction of the contract's notional amount.

The company subjects its derivative-related credit risk to the same credit approval, limit and monitoring standards that it uses for managing other transactions that create credit exposure. This includes evaluating the creditworthiness of counterparties and managing the size, diversification and maturity structure of the portfolio. Credit utilization for all products is compared with established limits on a continual basis and is subject to a quarterly review by the Investment Committee.

Netting is a technique that can reduce credit exposure from derivatives and is generally facilitated through the use of netting clauses in master derivative agreements. The netting clauses in a master derivative agreement provide for a single net settlement of all financial instruments covered by the agreement in the event of default. However, credit risk is reduced only to the extent that the company's financial obligations toward the counterparty to such an agreement can be set off against obligations such counterparty has toward us. The company uses netting clauses in master derivative agreements to reduce derivative-related credit exposure. The overall exposure to credit risk that is reduced through the netting clauses may change substantially following the reporting date as the exposure is affected by each transaction subject to the agreement as well as by changes in underlying market rates and values.

The use of collateral is another significant credit mitigation technique for managing derivative-related counterparty credit risk. Mark-to-market provisions in the company's agreements with some counterparties provide the company with the right to request that the counterparty pay down or collateralize the current market value of its derivatives positions when the value passes a specified threshold amount.

The company enters into annuity agreements with various Canadian life insurance companies which have credit ratings of at least A– or higher, to provide for fixed and recurring payments to claimants. Under such arrangements, the company derecognizes the liability from its consolidated balance sheet as the liability to its claimants is substantially discharged, although the company remains exposed to the credit risk that life insurers may fail to fulfill their obligations.

Use of derivatives

The company uses derivatives principally to mitigate certain of the above mentioned risks. The company's use of derivatives exposes it to a number of risks, including credit risk, interest rate and equity market fluctuations. The hedging of certain risks with derivatives results in basis risk. Basis risk is the risk that offsetting investments in a hedging strategy will not experience price changes in entirely opposite directions from each other. This imperfect correlation between the two investments creates the potential for excess gains or losses in a hedging strategy, thus adding risk to the position. The company monitors the effectiveness of its hedges on a regular basis.

Insurance related risks

Reserve adequacy risk

Our success depends upon our ability to accurately assess the risks associated with the insurance policies that we write. We establish reserves to cover our estimated liability for the payment of all losses and loss adjustment expenses incurred with respect to premiums collected or due on the insurance policies that we write. Reserves do not represent an exact calculation of liability. Rather, reserves are our estimates of what we expect to be the ultimate cost of resolution and administration of claims. These estimates are based upon various factors, including:

- actuarial projections of the cost of settlement and administration of claims reflecting facts and circumstances then known;
- estimates of trends in claims severity and frequency;
- judicial theories of liability;
- variables in claims handling procedures;
- economic factors (such as inflation);
- judicial and legislative trends, and actions such as class action lawsuits and judicial interpretation of coverage or policy exclusions; 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 our ability to accurately assess the risks of the policies that we write. In addition, there may be significant reporting lags between the occurrence of the insured event and the time it is actually reported to the insurer and additional lags between the time of reporting and final settlement of claims.

We continually refine our reserve estimates in an ongoing process as claims are reported and settled. Establishing an appropriate level of reserves is an inherently uncertain process. The following factors may have a substantial impact on our future actual losses and loss adjustment expenses experience:

– the amounts of claims payments;
– the expenses that we incur in resolving claims;
– legislative and judicial developments; and
– changes in economic conditions, including inflation.

To the extent that actual losses and loss adjustment expenses exceed our expectations and the reserves reflected in our financial statements, we will be required to reflect those changes by increasing our reserves. In addition, government regulators could require that we increase our reserves if they determine that our reserves were understated in the past. When we increase reserves, our pre-tax income for the period in which we do so will decrease by a corresponding amount. In addition, increasing or "strengthening" reserves causes a reduction in our insurance subsidiaries' capital and could cause a downgrading of the financial strength ratings of our insurance subsidiaries. Any such downgrade could, in turn, adversely affect our ability to sell insurance policies.

Business cycle risk

The P&C insurance industry is cyclical, and we may witness changes in the appetite and underwriting capacity of our competitors, depending on their own loss experience and results. This would have different impacts on pricing and our ability to write new business. The industry's profitability can be affected significantly by:

– competition;
– availability of capital to support the assumption of new business;
– rising levels of actual costs that are unforeseen by companies at the time they price their products;
– volatile and unpredictable developments, including unnatural, weather-related and other natural catastrophes or terrorists' attacks;
– changes in loss reserves resulting from the general claims and legal environments as different types of claims arise and judicial interpretations relating to the scope of insurers' liability develop;
– changes in insurance and tax laws and regulations as well as new legislative initiatives;
– general economic conditions, such as fluctuations in interest rates, inflation and other changes in the investment environment, which affect returns on invested capital and may impact the ultimate payout of loss amounts;
– general industry practices.

In addition, the profitability of automobile insurers can be affected significantly by many factors, including:

– regulatory regimes which limit their ability to detect and defend against fraudulent claims and fraud rings;
– developing trends in tort and class action litigation;
– changes in laws which could limit the use of used or like kind and quality after-market parts or compel compensation for alleged diminution in value notwithstanding repair of the vehicle;
– changes in other laws or regulations, including the adoption of consumer initiatives regarding rates charged for automobile or other insurance coverage or claims handling procedures; and
– privacy and consumer protection laws that prevent insurers from assessing risks 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 generally characterized by increased competition resulting in lower premium rates and underwriting standards followed by "hard" markets generally characterized by lessening competition, stricter underwriting standards and increasing premiums rates. Our 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 our results of operations and financial condition.

Catastrophic events risk

Catastrophes can be caused by various natural and unnatural events. Natural catastrophic events may be affected by the impacts of climate change and include hurricanes, windstorms, earthquakes, hailstorms, rainstorms, ice storms, explosions, severe winter weather and fires. Unnatural catastrophic events include hostilities, terrorist acts, riots, crashes and derailments. Despite the use of "models", 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. For example, the ice storm in Eastern Canada in 1998 caused P&C insurance losses in several lines of business, including business interruption, personal property, automobile and commercial property.

Claims resulting from natural or unnatural catastrophic events could cause substantial volatility in our financial results and could materially reduce our profitability or harm our financial condition.

The company's risk management strategy involves monitoring insured value accumulation and concentration risk, catastrophe scenario modeling, and reinsurance. See section 9.3 above for more details on the company's reinsurance program.

Climate change risk

Climate change is a challenge facing the entire property and casualty insurance industry. In particular, the company's home insurance business has been affected due to changing climate patterns and an increase in the number and cost of claims associated with severe storms. Water damages now make up more than half of the company's home insurance claims.

To address this issue, the company has launched several initiatives including pricing and product changes to reflect new climate realities, a home insurance action plan, a review of claims processes and a greater focus on consumer loss prevention and education. The company's home insurance action plan is described in detail in section 4.2 above.

Reinsurance risk

We use reinsurance to help manage our exposure to insurance risks. The availability and cost of reinsurance are subject to prevailing market conditions, both in terms of price and available capacity, which can affect our premium volume and profitability. Reinsurance companies exclude some coverages from the policies that we purchase from them or may alter the terms of such policies from time to time. For example, following the terrorist attacks of September 11, 2001, some reinsurers excluded coverage for terrorist acts or priced such coverage at prohibitively high rates. These gaps in reinsurance protection expose us to greater risks and greater potential losses and could adversely affect our ability to write future business. We may not be able to successfully mitigate risks through reinsurance arrangements, which could cause us to reduce our premiums written in certain lines or could result in losses.

We are supported by a number of reinsurers which may be affected by difficult situations and results. This increases the potential adverse effect on our results of operations if one or more of our reinsurers are unable to meet its financial obligations. Although all of our reinsurers have, amongst other criteria, a minimum financial strength rating of "A-" from A.M. Best and/or S&P at the time of entering into reinsurance arrangements with us, these ratings are subject to change and may be downgraded. Although reinsurance makes the assuming reinsurer liable to us to the extent of the risk ceded, we are not relieved of our primary liability to our policyholders as the direct insurer. As a result, we bear credit risk with respect to our reinsurers. There is no certainty that our reinsurers will pay all reinsurance claims on a timely basis or at all. We evaluate each reinsurance claim based on the facts of the case, historical experience with the reinsurer for similar claims under existing law, and provide for reinsurance amounts deemed uncollectible in our reserves. Other details regarding reinsurance are also included in sections 9.3 and 10.4 above.

Business interruption risk

We may also experience an abrupt interruption of activities caused by unforeseeable and/or catastrophic events, an example of which being a global flu pandemic (e.g. H1N1). Our 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 our business continuity plans cannot be put into action or do not take such events into account, losses may increase further.

In order to maintain the integrity and continuity of the company's operations in the event of a crisis, we have developed personalized alert and mobilization procedures as well as communication protocols. For example, emergency action plans, business continuity plans, business recovery plans, major health crisis plans, building evacuation plans and crisis communication plans have all been defined and are tested on an ongoing basis. This process is supported by a crisis management structure adapted to our company's organization and to the type of events we may have to manage.

Distribution risk

Distribution risk is the risk related to the distribution of the company's P&C products. It includes the inherent risk of dealing with independent distributors, the risk related to new market entrants and the risk associated with the company's multiple distribution channel strategy.

We distribute our products primarily through a network of brokers and a great part of our success depends on the capacity of this network to be competitive against other distributors, including "direct" insurers, as well as our ability to maintain our business relationships with them while developing our distribution network strategy.

These brokers sell our competitors' insurance products and may stop selling our insurance 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 our insurance products. In addition, our strategy of distributing through the direct channel may adversely impact our relationship with brokers who distribute our products.

From time to time the company issues loans or takes equity participation in certain brokers and by doing so, the company exposes itself to financial risk and to potential relationship issues. In order to maintain strong relationships with brokers, each relationship is managed by officers in each of the main regions in which we operate. To mitigate the financial risk the company generally receives guarantees and uses standard agreements which contain general security and oversight clauses. The Board of Directors participates in this oversight process by reviewing these loan and equity arrangements annually.

Also, the company has established and maintains close relationships with its independent distributors by providing technology and training to help strengthen their market position. It closely monitors pricing gaps between its various channels and manages the different channels under different brand names including Canada Brokerlink, its wholly owned broker network.

Competition risk

The P&C insurance industry is highly competitive and intense competition for our insurance products could harm our ability to maintain or increase our profitability, premium pricing power and written insured risk volume. We believe that the industry will remain highly competitive in the foreseeable future. We also believe that competition in our business lines is based on price, service, commission structure, product features, financial strength and scale, ability to pay claims, ratings, reputation and name or brand recognition. We compete with a large number of domestic and foreign insurers as well as with different Canadian banks that are selling insurance products. These firms may use business models different to ours and sell products through various distribution channels, including brokers and agents who sell products exclusively for one insurer and directly to the consumer. We compete not only for business and individual customers, employers and other group customers but also for brokers and other distributors of investment and insurance products.

In addition, we may not be aware of other companies that may be planning to enter the insurance market or existing insurers that may be planning to raise additional capital. Any new, proposed or potential legislative or industry developments could further increase competition in our markets. We cannot be sure that we will be able to achieve or maintain any particular level of direct premiums written in this competitive environment.

Underwriting ability risk

Our performance depends on our ability to reduce financial loss resulting from the selection of risks to be insured and management of contract clauses. Unfavourable results in these areas can lead to deviations from the estimates based on actuarial assumptions. The company has adopted policies which specify the company's retention limits and risk tolerance and its application depends on training and the discipline of our underwriting teams. Once the retention limits have been reached, the company turns to reinsurance to cover the excess risk. Moreover, our profitability and ability to grow may also be adversely affected by our mandatory participation in the Facility Association in Canada's automobile insurance markets.

Product and pricing risk

Product design and pricing risk is the risk that the established price is or becomes insufficient to ensure an adequate return for shareholders as compared to the company's profitability objectives. This risk may be due to an inadequate assessment of market needs, new business context, a poor estimate of the future experience of several factors, as well as the introduction of new products that could adversely impact the future behaviour of policyholders.

New products are reviewed by Senior Management and the risk is primarily managed by regularly analyzing the pricing adequacy of the company's products as compared to recent experience. The pricing assumptions are revised as needed and/or the various options offered by the reinsurance market are utilized.

Operational risks

Operational risk is the risk of loss resulting from inadequate or failed processes, people and systems or from external events. These include events such as unauthorized activity, internal and external criminal activity, information security failure, among others.

We believe that managing the risks related to the company's business activities significantly reduces losses resulting from failed processes, procedures or controls, inadequate systems, human errors, fraud or external events such as natural disasters. To manage these risks, the company follows a specific framework that is composed of different steps including identification, measurement, monitoring and mitigation.

For early detection of and clear insight into the company's key operational risks, the Operational Committee uses many tools including periodic risk review interviews with management and risk and control self-assessments of the company's critical functions. It also monitors and measures the company's risks on an ongoing basis through key risk indicators which enable management to proactively initiate effective actions. The company has also developed clear incident reporting channels within the organization to systematically report, manage and monitor operational incidents which could lead to potential financial losses or reputation damage. Ongoing training and exercises provided to all employees also contribute in increasing the operational risk awareness culture within the organization and minimizing the severity and occurrence of incidents.

The effective implementation of the overall operational risk management program depends on management. Management is supported by the operational risk management department which assists in monitoring the operational risk processes and ensuring that appropriate actions are taken when necessary. The operational risk department reports to the Enterprise Risk Committee, which is comprised of executive members appointed by the Board of Directors. The committee has the oversight responsibility for all enterprise risks and risk governance within the organization. Finally, to ensure transparency, the committee provides regular updates of its operations to the Senior Management Committee, the Audit Committee and the Board of Directors.

Other related risks

Strategy implementation risk

In order to seek profitable growth and maximize shareholders' returns, we intend to invest significant resources in expanding our core businesses and implementing our strategies. We cannot be sure that we will continue to succeed in implementing our strategies. We may experience difficulty in executing our strategies because of, among other things, increased competition, difficulty in developing and introducing new products, adverse economic conditions, changes in regulatory requirements and difficulty in our relationships with our distribution networks and insured clients. To help mitigate these risks, the company relies extensively on technology to improve the company's capacity to deliver our services.

In executing our growth strategy, we intend to continue to expand our operations and business in part by acquiring additional P&C insurance businesses. We cannot be sure that the market conditions will be favourable to undertaking or completing such acquisitions nor that we will be able to identify appropriate acquisition targets, profitably manage additional businesses or successfully integrate any acquired businesses into our operations. Furthermore, acquisitions may involve a number of special risks, including diversion of management's attention, failure to retain key personnel, unanticipated events or circumstances and legal liabilities, some or all of which could have a material adverse effect on our business, results of operations and financial condition. We cannot be sure that any acquired businesses will achieve the anticipated revenues, income and synergies. Acquisitions could also result in potentially dilutive issuances of equity securities. Failure on our part to manage our acquisition strategy successfully could have a material adverse effect on our business, results of operations and financial condition.

The company mitigates these risks through formal processes and approvals which include:

- obtaining our Board of Directors' final approval of the medium term plan, which provides for strategic planning and capital allocation, and includes risk management analysis;
- having the financial and operational reports reviewed by the Audit Committee and our Board of Directors on a quarterly basis;
- having each of our business units develop detailed business plans, which are then executed by local management;
- having each significant acquisition reviewed and approved by our Board of Directors; and
- developing and maintaining high standards of conduct through distribution of our Code of Conduct to all new employees and through periodical reminders to all employees and training sessions. Fraud detection measures also play a role in reducing potential losses.

Regulation and legal risk

Our insurance subsidiaries are subject to regulation and supervision by insurance regulatory authorities of the jurisdictions in which they are incorporated and licensed to conduct business. These laws and regulations delegate regulatory, supervisory and administrative powers to federal, provincial and territorial insurance commissioners and agencies. Such laws and regulations are generally designed to protect policyholders and creditors rather than shareholders, and are related to matters including:

– personal auto insurance rate setting;

– risk-based capital and solvency standards;

– restrictions on types of invested assets;

– the maintenance of adequate reserves for unearned premiums and unpaid claims;

– the examination of insurance companies by regulatory authorities, including periodic financial and market conduct examinations;

– the licensing of insurers, agents and brokers;

– limitations on dividends and transactions with affiliates; and

– regulatory actions.

We believe that our insurance subsidiaries are in material compliance with all applicable regulatory requirements. It is not possible to predict the future impact of changing federal, provincial and territorial regulations on our operations, and we cannot be sure that laws and regulations enacted in the future will not be more restrictive than current laws. Overall, our business is heavily regulated and changes in regulation may reduce our profitability and limit our growth.

In addition, these laws and regulations typically require us to periodically file financial statements and annual reports, prepared on a statutory accounting basis, and other information with insurance regulatory authorities, including information concerning our capital structure, ownership and financial condition including, on an annual basis, the aggregate amount of contingent commissions paid and general business operations. We could be subject to regulatory actions, sanctions and fines if a regulatory authority believed we had failed to comply with any applicable law or regulation. Any such failure to comply with applicable laws could result in the imposition of significant restrictions on our ability to do business or significant penalties, which could adversely affect our reputation, results of operations and financial condition. In addition, any changes in laws and regulations, including the adoption of consumer or other initiatives regarding contingent and other commissions, rates charged for automobile or claims handling procedures, could materially adversely affect our business, results of operations and financial condition.

In addition to the occasional employment-related litigation, we are a defendant in a number of claims relating to our insurance and other related business operations. We may from time to time be subject to a variety of legal and regulatory actions relating to our current and past business operations, including, but not limited to:

– disputes over coverage or claims adjudication;

– disputes regarding sales practices, disclosures, premium refunds, licensing, regulatory compliance and compensation arrangements;

– disputes with our agents, brokers or network providers over compensation and termination of contracts and related claims;

– regulatory actions relating to consumer pressure in relation to benefits realized by insurers;

– disputes with taxing authorities regarding our tax liabilities and tax assets; and

– disputes relating to certain businesses acquired or disposed of by us.

Plaintiffs may also continue to bring new types of legal claims against the company. Current and future court decisions and legislative activity may increase our exposure to these types of claims. Multiparty or class action claims may present additional exposure to substantial economic, non-economic or punitive damage awards. The loss of even one of these claims, if it resulted in a significant damage award or a judicial ruling that was otherwise detrimental, could have a material adverse effect on our results of operations and financial condition. Unfavourable claim rulings may render fair settlements more difficult to reach. We cannot determine with any certainty what new theories of recovery may evolve or what their impact may be on our businesses.

We may be subject to governmental or administrative investigations and proceedings in the context of our highly regulated sectors of activity. We cannot predict the outcome of these investigations, proceedings and reviews, and cannot be sure that such investigations, proceedings or reviews or related litigation or changes in operating policies and practices would not materially adversely affect our results of operations and financial condition. In addition, if we were to experience difficulties with our relationship with a regulatory body in a given jurisdiction, it could have a material adverse effect on our ability to do business in that jurisdiction and the price of the company's common shares.

We are supported by a team of lawyers and staff, and by outside counsel when deemed necessary or appropriate, in handling general regulation and litigation issues and are an active member of the major industry associations. Additionally, our government relations team ensures contact with the governments of the various provinces in which we operate, and can be proactive in situations that could affect our business.

General economic, financial market and political conditions

Our businesses and profitability may be materially adversely affected from time to time by general economic, financial market and political conditions. In periods of economic downturn characterized by higher unemployment, lower family income, lower corporate earnings, lower business investment and lower consumer spending, individuals and businesses may choose not to purchase insurance products, may allow existing policies to lapse, or may choose to reduce the amount of coverage purchased. In addition to the demand for our insurance products being adversely affected, frequency or severity of claims could increase, resulting in lower earnings. General inflationary pressures may affect the costs of medical care, automobile parts and repair, construction and other items, and may increase the costs of paying claims.

In addition to the risk related to investments discussed previously, an economic downturn could have a significant impact on the financial condition of the company's defined benefit employee pension plans. Consequently, this could impact the company's financial condition.

Solvency risk

Regulatory authorities closely monitor the solvency of insurance companies by requiring them to comply with strict solvency standards based on the risk assumed by each company with respect to asset composition, liability composition, and the matching between these two components. The company is required to submit regular reports to the regulatory authorities regarding its solvency, and publish its solvency ratio every quarter. The minimum solvency ratio targeted by the company is 170.0%, which is higher than the regulatory MCT requirement of 150.0%. The appointed actuary must present an annual report to the Audit Committee and the Senior Management Committee on the company's current and future solvency and mitigating measures.

Reputation risk

Our insurance products and services are ultimately distributed to individual consumers and businesses. From time to time, consumer advocacy groups or the media may focus attention on our products and services, thereby subjecting us or our subsidiaries to periodic negative publicity. We also may be negatively impacted in relation to our information systems, security and technology, or if one of our subsidiaries engages in practices resulting in increased public attention to our businesses. 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 increase may further increase our costs of doing business and adversely affect our profitability by impeding our ability to market our products and services, requiring us to change our products or services or increasing the regulatory burdens under which we operate. The periodic negative insurance publicity and related businesses may negatively impact our financial results and financial condition. To mitigate these risks the Board of Directors has created the Disclosure Committee which is composed of senior officers and chaired by the Chief Legal Officer. This committee oversees the company's disclosure practices and procedures, its role includes maintaining awareness and understanding of corporate disclosure rules and guidelines, educating and informing employees about the company's disclosure practices, determining whether corporate developments constitute material information and reviewing and approving all material disclosure releases or statements of Intact Financial Corporation.

Credit downgrade risk

Independent third party rating agencies assess the company's ability to honour its financial obligations, (the "issuer credit rating"), and the insurance subsidiaries' ability to meet their ongoing policyholder obligations, (the "financial strength rating").

The rating agencies periodically evaluate us to confirm that we continue to meet the criteria of the ratings previously assigned to us.

We may not be in a position to maintain either the issuer credit ratings or the financial strength ratings we have received from the rating agencies. An issuer credit rating downgrade could result in materially higher borrowing costs. A financial strength rating downgrade could result in a reduction in the number of insurance contracts we write and in a significant loss of business; as such business could move to other competitors with higher ratings, thus causing premiums and earnings to decrease.

Liquidity risk

Liquidity risk is the risk that the company will encounter difficulty in raising funds to meet obligation associated with financial liabilities. To manage its cash flow requirements, the company maintains a portion of its invested assets in liquid securities.

The company's liquidity management is governed by establishing a prudent policy that identifies oversight responsibilities as well as by setting limits and implementing effective techniques to monitor measure and control exposure to liquidity risk. A portion of invested assets is maintained in short-term (less than one year) highly liquid money market securities, which are used to manage the operational requirements of the company. A large portion of the invested assets are held in highly liquid federal and provincial government debt to protect against any unanticipated large cash requirements. The company also has an unsecured committed credit facility.

Limit on dividend and capital distribution risk

As a holding company, IFC is a legal entity and is separate and distinct from its operating subsidiaries, most of which are regulated insurance companies. Canadian insurance regulations limit the ability of our insurance subsidiaries to pay dividends and require our insurance subsidiaries to maintain specified levels of statutory capital and surplus. In addition, for competitive reasons, our insurance subsidiaries need to maintain financial strength ratings which require us to sustain minimum capital levels in our insurance subsidiaries. These restrictions affect the ability of our insurance subsidiaries to pay dividends and use their capital in other ways. The inability of our subsidiaries to pay dividends to us could have a material adverse effect on our business and financial condition.

Dependency on key employees risk

Our success has been, and will continue to be, dependent on our ability to retain the services of our existing key employees and to attract and retain additional qualified personnel in the future. The loss of the services of any of our key employees, or the inability to identify, hire and retain other highly qualified personnel in the future, could adversely affect the quality and profitability of our business operations.

The company has developed a focused recruiting strategy to aggressively market careers and opportunities at Intact. The strategy includes an updated web site, focused external recruiting, campaigns, rebranding and targeted advertising. It also includes partnering with four universities on graduate recruiting as well as commercial and personal lines trainee program recruiting. Talent identification and development programs have been implemented to retain and grow existing talent and ingrain succession planning.

SECTION 12 – Other matters

12.1 Cautionary note regarding forward-looking statements

Certain of the statements in this MD&A about the company's current and future plans, expectations and intentions, results, levels of activity, performance, goals or achievements or any other future events or developments constitute forward-looking statements. The words "may", "will", "would", "should", "could", "expects", "plans", "intends", "trends", "indications", "anticipates", "believes", "estimates", "predicts", "likely" or "potential" or the negative or other variations of these words or other similar or comparable words or phrases, are intended to identify forward-looking statements.

Forward-looking statements are based on estimates and assumptions made by management based on management's experience and perception of historical trends, current conditions and expected future developments, as well as other factors that management believes are appropriate in the circumstances. Many factors could cause the company's actual results, performance or achievements or future events or developments to differ materially from those expressed or implied by the forward-looking statements, including, without limitation, the following factors: the company's ability to implement its strategy or operate its business as management currently expects; its ability to accurately assess the risks associated with the insurance policies that the company writes; unfavourable capital market developments or other factors which may affect the company's investments and funding obligations under its pension plans; the cyclical nature of the P&C insurance industry; management's ability to accurately predict future claims frequency; government regulations; litigation and regulatory actions; periodic negative publicity regarding the insurance industry; intense competition; the company's reliance on brokers and third parties to sell its products; the company's ability to successfully pursue its acquisition strategy; its ability to execute its business strategy; the company's participation in the Facility Association (a mandatory pooling arrangement among all industry participants); terrorist attacks and ensuing events; the occurrence of catastrophic events; the company's ability to maintain its financial strength ratings; the company's ability to alleviate risk through reinsurance; the company's ability to successfully manage credit risk (including credit risk related to the financial health of reinsurers); the company's reliance on information technology and telecommunications systems; the company's dependence on key employees; general economic, financial and political conditions; the company's dependence on the results of operations of its subsidiaries; the volatility of the stock market and other factors affecting the company's share price; and future sales of a substantial number of its common shares.

All of the forward-looking statements included in this MD&A are qualified by these cautionary statements and those made in the "Risk Management" section of our MD&A for the year ended December 31, 2009. These factors are not intended to represent a complete list of the factors that could affect the company; however, these factors should be considered carefully, and readers should not place undue reliance on forward-looking statements made herein. The company and management have no intention and undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

SECTION 13 – Additional information

The following tables present the income (loss) and comprehensive income (loss) information, shareholders' equity and cash flows.

TABLE 41 – CONSOLIDATED STATEMENTS OF INCOME

	For the quarter ended December 31		For the year ended December 31	
(in millions of dollars, except as noted)	**2009**	2008	**2009**	2008
Revenues				
Premiums written				
Direct	**$ 1,006.5**	$ 970.5	**$ 4,261.7**	$ 4,170.5
Ceded	**(24.1)**	(25.4)	**(110.4)**	(98.4)
Net	**982.4**	945.1	**4,151.3**	4,072.1
Changes in net unearned premiums				
Direct	**53.7**	74.2	**(96.8)**	(33.3)
Ceded	**0.4**	(0.1)	**0.9**	0.6
Net premiums earned	**1,036.5**	1,019.2	**4,055.4**	4,039.4
Interest income	**46.5**	46.9	**178.7**	187.8
Dividend income	**35.9**	35.4	**130.8**	157.3
Net investment losses	**(13.3)**	(152.2)	**(172.5)**	(288.0)
Distribution income and other	**19.1**	6.8	**48.9**	35.2
	1,124.7	956.0	**4,241.3**	4,131.7
Expenses				
Underwriting				
Claims	**660.7**	760.5	**2,877.2**	2,806.3
Commissions, premium taxes and general expenses	**306.9**	295.1	**1,165.8**	1,166.1
	967.6	1,055.6	**4,043.0**	3,972.4
Distribution and other	**27.2**	8.6	**52.9**	35.7
Interest on debt outstanding	**4.5**	–	**5.6**	–
	999.3	1,064.2	**4,101.5**	4,008.1
Income (loss) before income taxes	**125.4**	(108.2)	**139.8**	123.6
Income tax expense (benefit)	**28.7**	(44.1)	**13.1**	(4.6)
Net income (loss)	**$ 96.7**	$ (64.1)	**$ 126.7**	$ 128.2
Earnings per share, basic and diluted (dollars)	**$ 0.81**	$ (0.53)	**$ 1.06**	$ 1.05
Dividends per share (dollars)	**$ 0.32**	$ 0.31	**$ 1.28**	$ 1.24
Basic and diluted average number of common shares (in millions)	**119.9**	119.9	**119.9**	122.0

TABLE 42 – CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(in millions of dollars)	For the quarter ended December 31 2009	For the quarter ended December 31 2008	For the year ended December 31 2009	For the year ended December 31 2008
Net income (loss)	**$ 96.7**	$ (64.1)	**$ 126.7**	$ 128.2
Net decrease (increase) in unrealized losses on AFS securities	**35.8**	(431.8)	**425.2**	(801.2)
Income taxes	**(27.6)**	118.7	**(140.6)**	236.0
	8.2	(313.1)	**284.6**	(565.2)
Reclassification to income of net (gains) losses on available-for-sale securities	**4.5**	216.4	**105.5**	344.6
Income taxes	**18.6**	(65.3)	**(8.4)**	(107.2)
	23.1	151.1	**97.1**	237.4
Other comprehensive income (loss)	**31.3**	(162.0)	**381.7**	(327.8)
Comprehensive income (loss)	**$ 128.0**	$ (226.1)	**$ 508.4**	$ (199.6)

TABLE 43 – CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(in millions of dollars)	Share capital	Contributed surplus	Retained earnings	Accumulated other comprehensive loss	Total
Balance as at December 31, 2008	**$ 1,061.5**	**$ 88.3**	**$ 1,928.9**	**$ (446.1)**	**$ 2,632.6**
Net income	**–**	**–**	**126.7**	**–**	**126.7**
Other comprehensive income (loss)	**–**	**–**	**–**	**381.7**	**381.7**
Common shares repurchased for cancellation	**–**	**–**	**–**	**–**	**–**
Dividends paid	**–**	**–**	**(153.4)**	**–**	**(153.4)**
Long-term incentive plan	**–**	**(5.0)**	**–**	**–**	**(5.0)**
Balance as at December 31, 2009	**$ 1,061.5**	**$ 83.3**	**$ 1,902.2**	**$ (64.4)**	**$ 2,982.6**
Balance as at December 31, 2007	$ 1,101.9	$ 97.2	$ 2,091.3	$ (118.3)	$ 3,172.1
Net income	–	–	128.2	–	128.2
Other comprehensive income (loss)	–	–	–	(327.8)	(327.8)
Common shares repurchased for cancellation	(40.4)	–	(135.6)	–	(176.0)
Dividends paid	–	–	(151.0)	–	(151.0)
Long-term incentive plan	–	(8.9)	(4.0)	–	(12.9)
Balance as at December 31, 2008	$ 1,061.5	$ 88.3	$ 1,928.9	$ (446.1)	$ 2,632.6

TABLE 44 – CONSOLIDATED STATEMENTS OF CASH FLOW

	For the quarter ended December 31		For the year ended December 31	
(in millions of dollars)	**2009**	2008	**2009**	2008
Cash flows from (used in) operating activities				
Net income (loss)	**$ 96.7**	$ (64.1)	**$ 126.7**	$ 128.2
Adjustments for non-cash items	**104.6**	37.4	**315.3**	378.3
Changes in net claims liabilities	**(84.2)**	43.8	**169.4**	125.8
Changes in other operating assets and liabilities	**(39.8)**	213.4	**(73.4)**	(12.6)
Cash provided by operating activities	**77.3**	230.5	**538.0**	619.7
Cash flows from (used in) investing activities				
Proceeds from sale of invested assets	**1,888.7**	991.8	**6,151.6**	5,278.7
Purchase of invested assets	**(2,246.7)**	(730.3)	**(7,281.7)**	(5,014.9)
Purchase of brokerages and books of business, net of sales	**(11.1)**	(1.3)	**(51.9)**	(6.5)
Purchase of property and equipment	**(16.7)**	(11.8)	**(50.6)**	(47.7)
Cash provided by (used in) investing activities	**(385.8)**	248.4	**(1,232.6)**	209.6
Cash flows from (used in) financing activities				
Common shares repurchased for cancellation	**–**	–	**–**	(176.0)
Net proceeds from debt issuance	**148.9**	–	**397.7**	–
Dividends paid	**(38.3)**	(37.2)	**(153.4)**	(151.0)
Cash provided by (used in) financing activities	**110.6**	(37.2)	**244.3**	(327.0)
Net increase (decrease) in cash and cash equivalents	**(197.9)**	441.7	**(450.3)**	502.3
Cash and cash equivalents, beginning of period	**258.0**	68.7	**510.4**	8.1
Cash and cash equivalents, end of period	**$ 60.1**	$ 510.4	**$ 60.1**	$ 510.4

Management's responsibility for financial reporting

Management is responsible for the preparation and presentation of the consolidated financial statements of Intact Financial Corporation and its subsidiaries, collectively known as "the Company". This responsibility includes selecting appropriate accounting policies and making estimates and informed judgments based on the anticipated impact of current transactions, events and trends, consistent with Canadian generally accepted accounting principles.

In meeting its responsibility for the reliability of consolidated financial statements, the Company maintains and relies on a comprehensive system of internal control comprising organizational procedural controls and internal accounting controls. The Company's system of internal control includes the communication of policies and of the Company's Code of Conduct, comprehensive business planning, proper segregation of duties, delegation of authority for transactions and personal accountability, selection and training of personnel, safeguarding of assets and maintenance of records. The Company's internal auditors review and evaluate the system of internal control.

The Company's Board of Directors, acting through the Audit and Risk Review Committee, which is composed entirely of Directors, who are neither officers nor employees of the Company, oversees management's responsibility for the design and operation of effective financial reporting and internal control systems, the preparation and presentation of financial information and the management of risk areas.

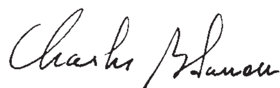
The Audit and Risk Review Committee conducts such review and inquiry of management and the internal and external auditors as it deems necessary to establish that the Company employs an appropriate system of internal control, adheres to legislative and regulatory requirements and applies the Company's Code of Conduct. The internal and external auditors, as well as the Actuary, have full and unrestricted access to the Audit and Risk Review Committee, with and without the presence of management.

Pursuant to the Insurance Companies Act of Canada or to the Insurance Act ("Quebec") ("the Acts"), the Actuary, who is a member of management, is appointed by the Board of Directors. The Actuary is responsible for discharging the various actuarial responsibilities required by the Acts and conducts a valuation of policy liabilities, in accordance with Canadian generally accepted actuarial standards, reporting his results to management and the Audit and Risk Review Committee.

The Office of the Superintendent of Financial Institutions Canada for the federally regulated property and casualty ("P&C") subsidiaries and l'Autorité des marchés financiers for the Quebec regulated P&C subsidiary make such examinations and inquiries into the affairs of the P&C subsidiaries as deemed necessary.

The Company's external auditors, Ernst & Young LLP, Chartered Accountants, are appointed by the shareholders to conduct an independent audit of the consolidated financial statements of the Company and meet separately with both management and the Audit and Risk Review Committee to discuss the results of their audit, financial reporting and related matters. The auditors' report to shareholders appears on the following page.

February 12, 2010



Charles Brindamour
President and Chief Executive Officer

Mark A. Tullis
Chief Financial Officer

To the Shareholders of Intact Financial Corporation

We have audited the consolidated balance sheets of **Intact Financial Corporation** [the "Company"] as at December 31, 2009 and 2008 and the consolidated statements of income, comprehensive income (loss), changes in shareholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2009 and 2008 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Chartered Accountants
Licensed Public Accountants

Toronto, Canada
February 12, 2010

Intact Financial Corporation
Audited consolidated financial statements
December 31, 2009

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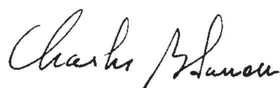
Consolidated balance sheets

(in millions of Canadian dollars)

As at December 31,	2009	2008
Assets		
Cash and cash equivalents	$ 60.1	$ 510.4
Invested assets (note 4)		
Debt securities	4,784.3	3,832.5
Equity securities	2,893.7	2,019.5
Loans	318.5	242.3
	7,996.5	6,094.3
Accrued interest and dividend income	43.0	34.7
Premium receivables	1,640.5	1,469.4
Income taxes receivable	40.4	221.0
Other receivables	244.9	247.0
Reinsurance assets (note 8)	260.6	224.2
Deferred acquisition costs	396.2	382.4
Future income tax asset (note 9)	38.0	66.0
Other assets (note 10)	292.9	238.6
Intangibles (note 11)	159.6	136.4
Goodwill (note 11)	178.6	160.8
Total assets	$11,351.3	$ 9,785.2
Liabilities		
Claims liabilities (note 8)	$ 4,270.0	$ 4,064.9
Unearned premiums (note 8)	2,463.6	2,366.8
Income taxes payable	102.5	7.4
Future income tax liability (note 9)	25.8	11.8
Financial liabilities (note 4)	278.8	9.1
Other liabilities	830.3	692.6
Debt outstanding (note 13)	397.7	–
	8,368.7	7,152.6
Contingencies, commitments and guarantees (note 18)		
Shareholders' equity		
Share capital (note 14)	1,061.5	1,061.5
Contributed surplus	83.3	88.3
Retained earnings	1,902.2	1,928.9
Accumulated other comprehensive loss	(64.4)	(446.1)
	2,982.6	2,632.6
Total liabilities and equity	$11,351.3	$ 9,785.2

See accompanying notes to audited Consolidated financial statements.

On behalf of the Board:



Charles Brindamour
Director

Eileen Mercier
Director

Consolidated statements of income

(in millions of Canadian dollars, except as otherwise noted)

For the years ended December 31,	2009	2008
Revenues		
Premiums written		
Direct	$ 4,261.7	$ 4,170.5
Ceded	(110.4)	(98.4)
Net	4,151.3	4,072.1
Changes in net unearned premiums	(95.9)	(32.7)
Net premiums earned	4,055.4	4,039.4
Interest income (note 4)	178.7	187.8
Dividend income (note 4)	130.8	157.3
Net investment losses (note 4)	(172.5)	(288.0)
Distribution income and other	48.9	35.2
	4,241.3	4,131.7
Expenses		
Underwriting		
Claims	2,877.2	2,806.3
Commissions, premium taxes and general expenses	1,165.8	1,166.1
	4,043.0	3,972.4
Distribution expenses and other	52.9	35.7
Interest on debt outstanding	5.6	–
	4,101.5	4,008.1
Income before income taxes	139.8	123.6
Income tax expense (benefit) (note 9)	13.1	(4.6)
Net income	$ 126.7	$ 128.2
Earnings per share, basic and diluted (dollars)	$ 1.06	$ 1.05
Dividends per share (dollars)	$ 1.28	$ 1.24
Basic and diluted average number of common shares (in millions)	119.9	122.0

See accompanying notes to audited Consolidated financial statements.

Consolidated statements of comprehensive income (loss)

(in millions of Canadian dollars)

For the year ended December 31,	2009	2008
Net income	$ 126.7	$ 128.2
Net decrease (increase) in unrealized losses on available-for-sale securities	425.2	(801.2)
Income taxes (note 9)	(140.6)	236.0
	284.6	(565.2)
Reclassification to income of net (gains) losses on available-for-sale securities	105.5	344.6
Income taxes (note 9)	(8.4)	(107.2)
	97.1	237.4
Other comprehensive income (loss)	381.7	(327.8)
Comprehensive income (loss)	$ 508.4	$ (199.6)

See accompanying notes to audited Consolidated financial statements.

Consolidated statements of changes in shareholders' equity

(in millions of Canadian dollars)

	Share capital	Contributed surplus	Retained earnings	Accumulated other comprehensive income (loss)	Total
Balance as at December 31, 2008	**$ 1,061.5**	**$ 88.3**	**$ 1,928.9**	**$ (446.1)**	**$ 2,632.6**
Net income	–	–	**126.7**	–	**126.7**
Other comprehensive income (loss)	–	–	–	**381.7**	**381.7**
Common shares repurchased for cancellation (note 14)	–	–	–	–	–
Dividends paid	–	–	**(153.4)**	–	**(153.4)**
Long-term incentive plan	–	**(5.0)**	–	–	**(5.0)**
Balance as at December 31, 2009	**$ 1,061.5**	**$ 83.3**	**$ 1,902.2**	**$ (64.4)**	**$ 2,982.6**
Balance as at December 31, 2007	$ 1,101.9	$ 97.2	$ 2,091.3	$ (118.3)	$ 3,172.1
Net income	–	–	128.2	–	128.2
Other comprehensive income (loss)	–	–	–	(327.8)	(327.8)
Common shares repurchased for cancellation (note 14)	(40.4)	–	(135.6)	–	(176.0)
Dividends paid	–	–	(151.0)	–	(151.0)
Long-term incentive plan	–	(8.9)	(4.0)	–	(12.9)
Balance as at December 31, 2008	$ 1,061.5	$ 88.3	$ 1,928.9	$ (446.1)	$ 2,632.6

See accompanying notes to audited Consolidated financial statements.

Consolidated statements of cash flows

(in millions of Canadian dollars)

For the years ended December 31,	**2009**	2008
Cash flows from (used in) operating activities		
Net income	**$ 126.7**	$ 128.2
Adjustments for non-cash items (note 16)	**315.3**	378.3
Changes in net claims liabilities	**169.4**	125.8
Changes in other operating assets and liabilities (note 16)	**(73.4)**	(12.6)
Cash provided by operating activities	**538.0**	619.7
Cash flows from (used in) investing activities		
Proceeds from sale of invested assets	**6,151,6**	5,278.7
Purchase of invested assets	**(7,281.7)**	(5,014.9)
Purchase of brokerages and books of business, net of sales	**(51.9)**	(6.5)
Purchase of property and equipment	**(50.6)**	(47.7)
Cash provided by (used in) investing activities	**(1,232.6)**	209.6
Cash flows from (used in) financing activities		
Common shares repurchased for cancellation	**–**	(176.0)
Net proceeds from debt issuance	**397.7**	–
Dividends paid	**(153.4)**	(151.0)
Cash provided by (used in) financing activities	**244.3**	(327.0)
Net increase (decrease) in cash and cash equivalents	**(450.3)**	502.3
Cash and cash equivalents, beginning of year	**510.4**	8.1
Cash and cash equivalents, end of year (note 16)	**$ 60.1**	$ 510.4

See accompanying notes to audited Consolidated financial statements.

NOTE 1 – Status of the Company

Intact Financial Corporation (formerly ING Canada Inc.) ("Intact" "IFC" or the "Company") incorporated under the *Canada Business Corporations Act*, is domiciled in Canada and its shares are publicly traded on the Toronto Stock Exchange. The Company has investments in wholly-owned subsidiaries which operate principally in the Canadian property and casualty ("P&C") insurance market. The Company's significant subsidiaries are Intact Insurance Company, Belair Insurance Company Inc., The Nordic Insurance Company of Canada, Novex Insurance Company, Trafalgar Insurance Company of Canada, Equisure Financial Network Inc., Canada Brokerlink Inc. and Grey Power Insurance Brokers Inc.

On February 19, 2009, ING Groep completed the disposal of its entire 70% shareholding in the Company via the sale of 36,183,480 of the Company's common shares to a number of institutional investors on a private placement basis and the sale of 47,757,920 common shares pursuant to a secondary public offering. The Special share owned by ING Groep was immediately converted into one common share and was also disposed of through the secondary offering. Effective May 19, 2009, following approval by the shareholders, the name of the Company was changed to Intact Financial Corporation (TSX: IFC).

NOTE 2 – Basis of presentation

These Consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The accounting policies used to prepare the financial statements of the Company's regulated insurance subsidiaries also comply with the accounting requirements of their respective regulators. Generally, in preparing their financial statements, the subsidiaries apply the same accounting policies as the Company.

The Company consolidates the financial statements of all subsidiary companies and eliminates on consolidation all intercompany balances and transactions.

The equity method is used to account for investments in entities over which the Company exerts significant influence. Gains and losses on sales of these investments are reported in Net investment losses on the Consolidated statements of income only when realized, while expected losses due to other than temporary impairments are recognized immediately. All related-party transactions are with entities subject to significant influence. These transactions are made in the normal course of business and are recorded at the exchange amount.

Earnings per share are computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflects the potential dilution that could occur if the holders of securities or contracts entitling them to obtain common shares in exchange for their securities or contracts exercised their right to obtain common shares.

In preparing these Consolidated financial statements, the Company has adopted certain presentation standards. All amounts in these statements are in millions of Canadian dollars except as otherwise noted. Certain comparative figures have been reclassified to conform to the presentation adopted in the current period. Captions used in these Consolidated financial statements and notes have words such as "Income", "Earnings" and "Gains" always placed before the words "Expense", "Loss" and "Losses".

NOTE 3 – Summary of significant accounting policies

The preparation of Consolidated financial statements in accordance with Canadian GAAP requires management to make assumptions and estimates that affect the reported amounts of assets and liabilities at the dates of the Consolidated financial statements, the reported amounts of revenue and expenses for the years presented, as well as the disclosure of contingent assets and liabilities (note 18). These estimates are subject to uncertainty. Significant estimates include policy liabilities (note 8), fair value measurement (note 6), impairment of financial assets (note 4), income taxes (note 9), employee future benefits (note 12), and goodwill and intangible assets (note 11). Changes in estimates are recorded in the accounting period in which they occur.

The significant accounting policies used in preparing these Consolidated financial statements, including those specified by the insurance regulators, are, in all material respects, in accordance with Canadian GAAP and are summarized below. These policies have been consistently applied except as described in the significant accounting changes section below.

a) Significant accounting changes

Goodwill and intangible assets

Effective January 1, 2009, the Company applied the *Canadian Institute of Chartered Accountants* ("CICA") *Handbook* Section 3064, *Goodwill and Intangible Assets*. This Section replaced CICA Handbook Section 3062, *Goodwill and Other Intangible Assets*, and Section 3450, *Research and Development Costs*, and established standards for the recognition, measurement and disclosure of goodwill and intangible assets. The provisions relating to the definition and initial recognition of intangible assets, including internally generated intangible assets, are equivalent to the corresponding provisions of IAS 38, *Intangible Assets*, of International Financial Reporting Standards ("IFRS").

In applying Section 3064, the Company reclassified certain assets from Other assets to Intangibles on the Consolidated balance sheets. The comparative amount reclassified as at December 31, 2008 was $79.4. This reclassification had no impact on the Company's net income for 2009. (See note 11.)

Credit risk and the fair value of financial assets and financial liabilities

Effective January 20, 2009, the Company applied the Emerging Issues Committee ("EIC") abstract 173, *Credit Risk and the Fair Value of Financial Assets and Financial Liabilities*, requiring an entity to take into account its own credit risk and that of the relevant counterparties when determining the fair value of financial assets and financial liabilities, including derivative instruments. The adoption of this CICA abstract has not had a significant impact on the Company's results or financial condition as credit risks associated with the Company's financial assets and liabilities are incorporated into the Company's valuation methodology.

Impairment of financial assets – Amendments to: Financial Instruments – Recognition and Measurement

On August 20, 2009, the CICA issued various amendments to Section 3855, *Financial instruments, recognition and measurement*, and Section 3025, *Impaired loans*, which further reduced differences with IFRS. As a result of these amendments debt instruments not quoted in an active market may be classified as loans and receivables, measured at amortized cost and impairment is assessed using the same model as for impaired loans. In addition, the guidance requires reversing an impairment loss relating to an available-for-sale debt instrument when, in a subsequent period, the fair value of the instrument increased and if the increase can be objectively related to an event occurring after the loss was recognized.

The Company adopted these amendments, which required retroactive application to January 1, 2009, in the fourth quarter of fiscal year 2009. The impact of adopting these amendments on the Company's Consolidated financial statements was the reversal of $2.8 of impairments that were originally recognized in the first quarter of 2009. The Company has decided not to change the classification of any of its debt securities.

Financial Instruments – Disclosures

Effective for the period ended December 31, 2009, the Company applied the amended CICA Handbook Section 3862, *Financial Instruments – Disclosures*. This section provides improvements to fair value and liquidity risk disclosures and requires specific disclosure of the fair values hierarchy. Refer to Note 6 Fair value measurements.

b) Significant accounting policies

Insurance policy contracts

Revenue recognition

Premiums written are deferred as unearned premiums and recognized as revenue, net of reinsurance, on a pro rata basis over the terms of the underlying policies, usually twelve months and generally no longer than twenty-four months. Distribution income, mainly consisting of commissions is recorded on an accrual basis.

Policy liabilities and unearned premiums

Policy liabilities consist of unearned premiums and claims liabilities, net of the reinsurers' share. The appointed actuary, using appropriate actuarial techniques, evaluates the adequacy of policy liabilities.

Claims liabilities are first determined on a case-by-case basis as claims are reported and then reassessed as additional information becomes known. Included in claims liabilities is a provision to account for the future development of these claims, including claims incurred but not reported by policy holders ("IBNR"), as well as a provision for adverse deviations, as required by accepted actuarial practice in Canada. Claims liabilities are discounted to take into account the time value of money.

In estimating claims liabilities, standard actuarial techniques are used. These techniques are based on historical loss development factors and payment patterns. They require the use of assumptions such as loss and payment development factors, future rates of claims frequency and severity, inflation, reinsurance recoveries, expenses, changes in the legal environment, changes in tax legislation, changes in the regulatory environment and other matters, taking into consideration the circumstances of the Company and the nature of the insurance policies.

Unearned premiums are calculated on a pro rata basis, from the unexpired portion of the premiums written. The unearned premiums estimate is validated through standard actuarial techniques to ensure that these premiums are sufficient to cover the estimated future costs of servicing these policies and related claims.

Net claims liabilities are discounted using a rate that reflects the estimated market yield of the underlying assets backing these claims liabilities. Several actuarial assumptions are used to calculate this discount rate. These may change from period to period in order to arrive at the most accurate and representative market yield based discount rate.

Structured settlements

The Company enters into annuity agreements with various Canadian life insurance companies, that have credit ratings of at least A- or higher to provide for fixed and recurring payments to claimants. Under such arrangements, the Company derecognizes the liability from its Consolidated balance sheet as the liability to its claimants is substantially discharged, although the Company remains exposed to the credit risk that life insurers fail to fulfill their obligations. Refer to Note 7 Risk and capital management for further details.

Industry pools

When certain automobile owners are unable to obtain insurance via the voluntary insurance market, they are insured via the Facility Association ("FA"). In addition, entities can choose to cede certain risks to FA administered risk sharing pools ("RSP"). The related risks associated with FA insurance policies and policies ceded by companies to the RSP are aggregated and shared by the entities in the P&C insurance industry, generally in proportion to market share and volume of business ceded to the RSP. The Company applies the same accounting policies to FA and RSP insurance it assumes as it does to insurance polices issued by the Company directly to policyholders.

In accordance with the Office of the Superintendent of Financial Institutions Canada ("OSFI") guidelines, ceded and assumed RSP premiums are reported in Direct written premiums on the Consolidated income statement.

In addition, IFC acts as a "facility carrier" responsible for the administration of a portion of the FA policies. In exchange for providing these services the Company receives fees. Policy issuance fees are earned immediately while claims handling fees are deferred and earned as claims are opened and settled.

Reinsurance

Reinsurance assets include reinsurers' share of claims liabilities and unearned premiums. The Company presents third party reinsurance balances in the Consolidated balance sheets on a gross basis to indicate the extent of credit risk related to third party reinsurance and its obligations to policyholders and on a net basis in the Consolidated statements of income. 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. Refer to Note 7 Risk and capital management for further details.

Reinsurance liabilities are reported in Other liabilities and relate to ceded premiums written as well as reinstatement premiums payable.

Deferred acquisition costs

Deferred acquisition costs comprise commissions, premium taxes and expenses directly related to policy issuance. Such costs are deferred to the extent that they are recoverable from unearned premiums, after considering the anticipated claims, expenses and interest and dividend income in respect of these premiums. They are amortized on the same basis as the premiums and are reported in Commissions, premium taxes and general expenses on the Consolidated statements of income.

Financial instruments contracts

The Company has classified or designated all its financial assets and liabilities in the following categories:

– available-for-sale ("AFS")
– held-for-trading ("HFT")
– loans and receivables
– other financial liabilities

The table below summarizes the Company's initial and subsequent measures of financial instruments, as well as the reporting of related changes in fair value based on classification category.

TABLE 3.1 – FINANCIAL INSTRUMENTS MEASUREMENT BASIS AND CLASSIFICATION OF RELATED CHANGES IN FAIR VALUE

Classification category	Initial measurement	Subsequent measurement	Changes in fair value
Financial assets			
AFS instruments	Fair value using bid prices at the trade date	Fair value using bid prices at balance sheet date	Reported on the Consolidated statements of other comprehensive income ("OCI") when unrealized or on the Consolidated statement of income (Net investment losses) when realized or impaired
HFT instruments	Fair value using bid prices at the trade date	Fair value using bid prices at balance sheet date	Reported on the Consolidated statements of income (Net investment losses)
Loans and receivables	Fair value at the issuance date	Amortized cost using the effective interest method	Reported on the Consolidated statements of income (Net investment losses) when realized or impaired
Financial liabilities			
HFT instruments	Fair value using ask prices at the trade date	Fair value using ask prices at balance sheet date	Reported on the Consolidated statements of income (Net investment losses)
Other financial liabilities	Fair value at the issuance date	Amortized cost using the effective interest method	Reported on the Consolidated statements of income (Net investment losses) when the liability is extinguished

Invested assets

AFS financial assets

As described in table 3.1, AFS financial assets are recorded at fair value on the Consolidated balance sheet on the trade date and changes in fair values are recorded, net of income taxes, in other comprehensive income (loss) ("OCI") until the financial asset is disposed of, or has become other than temporarily impaired (see Fair value and unrealized gains and losses in table 4.2). When the asset is disposed of, or has become other than temporarily impaired, the gain or loss is reported in Net investment losses on the Consolidated statement of income and the amount is deducted from OCI. Gains and losses on the sale of AFS fixed income and equity securities are calculated on a first in, first out basis and on an average cost basis, respectively.

HFT financial assets

HFT financial assets and liabilities are purchased or incurred with the intention of generating profits in the near term ("classified as HFT") or are voluntarily so designated by the Company ("designated as HFT").

The Company designated a portion of its fixed income securities that are backing its net claims liabilities as HFT. This designation aims to reduce the volatility of the Consolidated statement of income related to the fluctuations in fair values of underlying net claims liabilities due to changes in discount rates. To comply with regulatory guidelines, the Company ensures that the weighted dollar duration of the fixed income securities designated as HFT is approximately equal to the weighted dollar duration of the net claims liabilities. The rate used to discount claims liabilities is calculated based on an exact dollar match of the invested assets backing these claims liabilities.

Loans and receivables

Loans issued to third parties and affiliates are designated as loans and receivables. These financial assets are accounted for at amortized cost using the effective interest rate method. As long as a loan or receivable is held and not impaired changes in fair value are not recognized in the Consolidated statement of income.

Financial liabilities

Other financial liabilities

The Company's medium term notes together with associated issuance costs are classified as Debt outstanding and accounted for at amortized cost using the effective interest method.

Derivative financial instruments

Derivative financial instruments are used for risk management purposes. Currency swaps, options, forwards, and total return swaps are held for non-trading purposes to mitigate foreign exchange and market risks.

Derivative financial instruments are recognized at their fair value, with changes in the fair value reflected on the Consolidated statement of income and reported in Net investment losses during the period in which they arise. Refer to Note 5 for further details.

Embedded derivatives

A derivative instrument may be embedded in another financial instrument (the "host instrument"). Embedded derivatives are treated as separate derivative financial instruments when their economic characteristics and risks are not clearly and closely related to those of the host instrument. The terms of the embedded derivatives are the same as those of a stand-alone derivative financial instrument, and the combined contract is not designated or classified as HFT. Embedded derivatives are classified as HFT financial assets and liabilities

Fair value measurement

The fair value of a financial instrument on initial recognition is normally the transaction price, i.e. the fair value of the consideration given or received.

Subsequent to initial recognition, the fair values of financial instruments are determined based on available information and a three-level fair values hierarchy. The split of the Company's financial instruments between each of the fair value hierarchy levels is described in note 6.

If the fair value of a financial asset measured at fair value becomes negative, it is recorded as a financial liability until its fair value becomes positive at which time it is recorded as a financial asset, or it is extinguished. These changes in classifications occur mainly to derivative financial instruments. Derivative financial instruments with positive fair values are reported in Other receivables and those with negative fair values are reported in Other financial liabilities. See table 5.1 for more details.

Impairment of financial assets

The Company assesses impairment, as follows:

Financial assets other than held-for-trading are assessed for impairment at each balance sheet date. Impairment exists when there is objective evidence of an other-than-temporary ("OTT") decline in fair value below cost.

Common shares: A quantitative assessment is made to identify shares which have had a significant or prolonged decline in fair value. Management then applies judgment based on each issuer's financial condition to determine whether objective evidence of impairment exists.

Fixed income securities and preferred shares: These financial assets are impaired when there is evidence which suggests that the issuer will fail to make the contractual interest or principal payments due under the terms of the instrument. Possible impairment indicators include significant financial difficulty, a downgrade in credit rating or bankruptcy and financial reorganization. An impairment loss relating to an available-for-sale fixed income security is reversed when, in a subsequent period, the fair value of the instrument increased and the increase can be objectively related to an event occurring after the impairment loss was recognized.

All impairment losses and reversals are recognized in Net investment losses in the Consolidated statements of income in the period in which they occur.

Revenue and expense recognition

Dividends are recognized when the shareholder's right to receive payment is established, which is the ex-dividend date and are reported in Dividend income on the Consolidated statements of income. Interest income from fixed income securities and loans are recognized on an accrual basis and reported in Interest income on the Consolidated statements of income.

Transaction costs associated with financial instruments classified or designated as HFT, are recognized in the Consolidated statement of income as incurred. For other financial instruments, transaction costs, together with premiums or discounts are capitalized on initial recognition and amortized using the effective interest method.

Other significant accounting policies

Cash and cash equivalents

Cash and cash equivalents consist of cash as well as highly liquid invested assets that are readily convertible into a known amount of cash, are subject to insignificant risk of changes in value and have an original maturity of three months or less from the date of acquisition.

Income taxes

The Company provides for income taxes using the liability method of tax allocation. Under this method, the income tax expense is calculated based on income tax laws and rates substantively enacted as at the Consolidated balance sheet dates. The income tax expense is comprised of two components: current income taxes and future income taxes. Current income taxes are amounts expected to be payable or recoverable as a result of operations in the current year. Future income taxes arise from changes during the year in cumulative temporary differences between the accounting carrying values of assets and liabilities and their respective tax bases. A future income tax asset is recognized to the extent that future realization of the tax benefit is more likely than not.

Employee future benefits

Pension and post retirement plans

For defined benefit pension and other retirement plans, the accrued benefit obligations, net of the fair value of plan assets and unamortized items are recognized on the balance sheet. The unamortized items are the past service costs, the transitional asset, the transitional valuation allowance and the net actuarial gains or losses. To match costs and services, these items are amortized on a straight-line basis over the expected average remaining service lifetime ("EARSL") of active members expected to receive benefits under the pension plans and over the expected average lifetime of the retirees receiving benefits under the other retirement plans. Changes in the valuation allowance are not deferred.

For each plan, the Company has adopted the following policies:

- The actuarial determination of the accrued obligations for pensions and other retirement benefits uses the projected benefit method based on services provided by employees and management's best estimate assumptions. See Note 12 Employee future benefits.
- For the purpose of calculating the expected return on plan assets, plan assets are valued at fair value.
- Only actuarial gains or losses in excess of 10% of the greater of the accrued benefit obligations or the fair value of plan assets are amortized over the EARSL for pension plans and over the expected average lifetime of the retirees receiving benefits under the other retirement plans.
- Past service costs arising from plan amendments are amortized on a straight-line basis over the EARSL for pension plans and over the expected average lifetime of the retirees receiving benefits under the other retirement plans.
- The Company amortizes the transitional asset/obligation arising from the adoption on January 1, 2000 of the CICA Handbook Section 3461 using the prospective application method on a straight-line basis over the EARSL as of January 1, 2000.
- When the restructuring of a benefit plan gives rise to both a curtailment and a settlement of obligations, the curtailment is accounted for prior to the settlement.

Post employment benefits

Health and dental benefits continue to be provided to eligible employees who are absent from work due to disability (or other approved leave) for the duration of their leave. The estimated present value of these benefits is charged to income in the year the absence commences.

Stock-based compensation

The Company has three types of stock-based compensation plans:

Long-term incentive plan

Certain key employees are entitled to a long-term incentive plan ("LTIP"). Under this plan, these employees are granted awards to receive IFC common shares as a portion of their compensation. Each award vests and is paid out at the end of a three-year performance cycle. The value of the actual award varies based on a performance measure which compares the Company's three-year average return on equity relative to that of the Canadian P&C insurance industry. The common shares received are restricted for two years. The Company re-estimates the number of awards that are expected to vest at each reporting period. At the time of the payout, the Company purchases on the market the equivalent amount of common shares. This type of compensation is measured at the fair value of the award at the grant date and recognized as an expense over the vesting period with a corresponding increase reported in contributed surplus.

Employee share purchase plan

Employees who are not eligible for the LTIP are entitled to make contributions in accordance with a voluntary employee share purchase plan ("ESPP"). Under the ESPP, eligible employees can contribute up to 10% of their annual base salary through a payroll deduction. As an incentive to participate to the plan, the Company contributes to the plan an amount equal to 50% of the employee contribution. The common shares are purchased on the market by an independent broker at the end of each month and are held by a custodian on behalf of the employees. The common shares purchased with the Company's contributions vest upon continued employment for a period of twelve months. The Company's contributions under the ESPP are accrued and expensed over the vesting period.

Deferred share unit plan

Non-employee directors of the Company are eligible to participate to the Company's deferred share unit ("DSU") Plan. The directors are given the choice of cash, IFC shares, DSUs, or a combination of the three for their compensation. Both the shares and the DSUs vest at the time of the grant. The DSUs are redeemed upon director termination and are settled for cash at that time. When directors elect to receive shares, the Company makes instalments to the share agent for the purchase of IFC shares on behalf of the directors. The Company records the expense for cash payments when paid, and for share payments when instalments are made to the share agent. The DSUs are cash-settled awards which are accounted for as an expense at the time of granting with a corresponding financial liability reported in Other liabilities. This liability is re-measured at each reporting date with any fluctuations in the liability also recorded as an expense until it is settled in cash.

Acquisitions and divestitures

Acquisitions of businesses for which the Company obtains control are accounted for using the purchase method. This involves allocating the purchase price paid for a business to the assets acquired, including identifiable intangible assets and the liabilities assumed, based on their fair values at the date of acquisition. Any excess is then recorded as goodwill.

Goodwill and intangibles

Goodwill is initially measured as the excess of the fair value of the consideration transferred over the acquisition-date fair value of identifiable assets acquired and the liabilities assumed. After initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is tested annually for impairment or whenever there is an indication that the goodwill may be impaired. Impairment, if any, identified through this assessment is reported on the Consolidated statements of income.

Intangibles acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition. The useful lives of intangible assets are assessed to be either finite or indefinite. Substantially all of the Company's intangible assets were assessed to have a finite life and are amortized over this period.

The Company's intangible assets consist of customer relationships, rights to offer renewals, and internally generated software. Amortization methods and rates are shown below.

	Method	Rate or term
Customer relationships including rights to offer renewals	Straight-line	10 years
Internally generated software	Straight-line	3 to 5 years

Long-term investments

The Company reports its long-term investments in Other assets on the Consolidated balance sheets.

The Company uses the equity method to report its significant influence investments in companies operating in the corporate and distribution segment. Under this method, the Company's share of the investee's net income is reported in Distribution income and other on the Consolidated statements of income.

The Company reports at cost its long-term investments for which it does not exercise significant influence. Income from these investments is reported only to the extent received or receivable in Dividend income on the Consolidated statements of income.

Property and equipment

Property and equipment are carried at cost less accumulated amortization. Amortization rates are established to depreciate the cost of the assets over their estimated useful lives. Amortization methods and rates are shown below.

	Method	Rate or term
Computer equipment	Straight-line	30–36 months
Furniture and equipment	Declining balance and straight-line	20% and 60 months, respectively
Leasehold improvements	Straight-line	Over the terms of related leases

c) Future accounting changes

Business combinations, consolidated financial statements and non-controlling interest

In January 2009, the CICA issued three accounting standards: Section 1582, *Business Combinations*, Section 1601, *Consolidated Financial Statements*, and Section 1602, *Non-controlling Interests,* to converge the accounting for business combinations and the reporting of non-controlling interest to IFRS.

The recommendations of Section 1582, *Business Combinations*, which replaces Section 1581, *Business Combinations*, will be effective for acquisitions completed on or after January 1, 2011. This section establishes guidance on the recognition and measurement basis of all assets and all liabilities acquired through a business combination.

The recommendations of Section 1601, *Consolidated Financial Statements*, and Section 1602, *Non-controlling Interests*, which together replace Section 1600, *Consolidated Financial Statements*, also become effective on January 1, 2011. These standards establish guidance on the accounting and presentation for non-controlling interests and for transactions affecting non-controlling interests. Early adoption is permitted but standards must be adopted concurrently.

The Company plans to adopt these sections effective January 1, 2011.

NOTE 4 – **Invested assets and financial liabilities**

The following tables summarize the Company's invested assets.

TABLE 4.1 – INVESTED ASSETS BY CLASSIFICATION

As at December 31, 2009	AFS	Classified as HFT	Designated as HFT	Loans and receivables	Total
Debt securities					
Short-term notes	**210.7**	–	–	–	**210.7**
Fixed income					
Investment grade					
Government, government-guaranteed and supranational	**1,627.6**	–	**1,630.8**	–	**3,258.4**
Corporate	**522.4**	–	**689.7**	–	**1,212.1**
Asset-backed	**103.1**	–	–	–	**103.1**
Total fixed income	**2,253.1**	–	**2,320.5**	–	**4,573.6**
Equity securities					
Preferred shares					
Investment grade					
Retractable	**320.7**	–	–	–	**320.7**
Fixed rate perpetual	**822.1**	–	–	–	**822.1**
Other perpetual	**438.8**	–	–	–	**438.8**
Total preferred shares	**1,581.6**	–	–	–	**1,581.6**
Common shares	**743.8**	**183.7**	**384.6**	–	**1,312.1**
Loans	–	–	–	**318.5**	**318.5**
Total	**4,789.2**	**183.7**	**2,705.1**	**318.5**	**7,996.5**

As at December 31, 2008	AFS	Classified as HFT	Designated as HFT	Loans and receivables	Total
Debt securities					
Short-term notes	293.8	–	–	–	293.8
Fixed income					
Investment grade					
Government, government-guaranteed and supranational	1,058.9	–	1,099.7	–	2,158.6
Corporate	437.3	–	657.8	–	1,095.1
Asset-backed	285.0	–	–	–	285.0
Total fixed income	1,781.2	–	1,757.5	–	3,538.7
Equity securities					
Preferred shares					
Investment grade					
Retractable	329.9	–	–	–	329.9
Fixed rate perpetual	624.1	–	–	–	624.1
Other perpetual	266.1	–	–	–	266.1
Total preferred shares	1,220.1	–	–	–	1,220.1
Common shares	727.7	–	71.7	–	799.4
Loans	–	–	–	242.3	242.3
Total	4,022.8	–	1,829.2	242.3	6,094.3

TABLE 4.2 – CARRYING VALUE OF INVESTED ASSETS

	HFT invested assets	Other invested assets				Total invested assets
As at December 31, 2009	At fair value	Unamortized cost	Unrealized gains	Unrealized losses	Net unrealized gains (losses)	At carrying value
Debt securities						
Short-term notes	–	210.7	–	–	–	210.7
Fixed income						
Investment grade						
Government, government-guaranteed and supranational	1,630.8	1,624.8	12.5	(9.7)	2.8	3,258.4
Corporate	689.7	506.3	16.5	(0.4)	16.1	1,212.1
Asset-backed	–	100.6	2.8	(0.3)	2.5	103.1
Total fixed income	2,320.5	2,231.7	31.8	(10.4)	21.4	4,573.6
Equity securities						
Preferred shares						
Investment grade						
Retractable	–	323.3	10.5	(13.1)	(2.6)	320.7
Fixed rate perpetual	–	924.2	13.4	(115.5)	(102.1)	822.1
Other perpetual	–	494.4	24.2	(79.8)	(55.6)	438.8
Total preferred shares	–	1,741.9	48.1	(208.4)	(160.3)	1,581.6
Common shares	568.3	707.1	56.5	(19.8)	36.7	1,312.1
Loans	–	318.5	–	–	–	318.5
Total	2,888.8	5,209.9	136.4	(238.6)	(102.2)	7,996.5
As at December 31, 2008						
Debt securities						
Short-term notes	–	293.8	–	–	–	293.8
Fixed income						
Investment grade						
Government, government-guaranteed and supranational	1,099.7	1,014.9	47.9	(3.9)	44.0	2,158.6
Corporate	657.8	449.4	7.6	(19.7)	(12.1)	1,095.1
Asset-backed	–	286.6	1.6	(3.2)	(1.6)	285.0
Total fixed income	1,757.5	1,750.9	57.1	(26.8)	30.3	3,538.7
Equity securities						
Preferred shares						
Investment grade						
Retractable	–	402.5	1.7	(74.3)	(72.6)	329.9
Fixed rate perpetual	–	914.9	0.2	(291.0)	(290.8)	624.1
Other perpetual	–	425.0	4.3	(163.2)	(158.9)	266.1
Total preferred shares	–	1,742.4	6.2	(528.5)	(522.3)	1,220.1
Common shares	71.7	868.5	10.5	(151.3)	(140.8)	799.4
Loans	–	242.3	–	–	–	242.3
Total	1,829.2	4,897.9	73.8	(706.6)	(632.8)	6,094.3

The Company reports its mutual funds and income trust unit investments with its common shares.

As of December 31, 2009, asset-backed securities consisted of auto loan receivables, credit card receivables and commercial mortgage-backed securities. All of these asset-backed securities are AAA rated (December 31, 2008 – 98.5%).

As at December 31, 2009, Loans' fair value was $334.1 (December 31, 2008 – $268.8). The fair value was established using valuation techniques that used both input parameters based on observable market data and input parameters not based on observable market data. The Company uses Dominion Bond Rating Services ("DBRS") and Standard & Poor's ("S&P") to rate fixed income securities and preferred shares. Fixed income securities with a rating equal to or above BBB- are classified as investment grade and other rated fixed income securities are classified as below investment grade. Preferred shares with a rating equal to or above P3 low are classified as investment grade and other rated preferred shares are classified as below investment grade.

Securities lending

The Company participates in a securities lending program to generate fee income. This program is managed by the Company's custodian, a major Canadian financial institution, whereby the Company lends securities it owns to other financial institutions to allow them to meet their delivery commitments. As at December 31, 2009 the Company has loaned securities (which are reported in Invested assets) with a fair value of $1,002.2 (2008 – $1,587.9)

Collateral, is provided by the counterparty and is held in trust by the custodian for the benefit of the Company until the underlying security has been returned to the Company. The collateral cannot be sold or re-pledged externally by the Company, unless the counterparty defaults on its financial obligations. Additional collateral is obtained or refunded on a daily basis as the market value of the underlying loaned securities fluctuates. The collateral consist of government securities with an estimated fair value of 105% of the fair value of the securities loaned and amounts to $1,052.3 at December 31, 2009 (2008 – $1,688.0).

Equities sold short

During 2009 the company recommenced its market neutral equity investment strategy. The objective of this strategy, which consists of having both long and short equity positions, is to maximize the value added from active equity portfolio management while at the same time using short positions to mitigate overall equity market volatility. Long positions are reported in Equity securities and short positions are reported in Other financial liabilities on the Consolidated balance sheet.

The Company has secured its short positions by pledging Government Fixed income securities as collateral.

TABLE 4.3 – LONG AND SHORT POSITIONS

	2009		2008	
	Fair value	Fixed income securities pledged as collateral	Fair value	Fixed income securities pledged as collateral
Long positions	183.7	–	–	–
Short positions	(183.4)	183.2	–	–

The following table shows the terms to maturity of the Company's invested assets portfolio.

TABLE 4.4 – MATURITY OF INVESTED ASSETS

As at December 31, 2009	One year or less	One year to five years	Over five years	No specific maturity	Total
Short-term notes	210.7	–	–	–	210.7
Fixed income securities	141.6	3,045.3	1,386.7	–	4,573.6
Preferred shares	18.9	191.3	114.5	1,256.9	1,581.6
Common shares	–	–	–	1,312.1	1,312.1
Loans	33.0	154.1	121.2	10.2	318.5
Total	404.2	3,390.7	1,622.4	2,579.2	7,996.5
As at December 31, 2008					
Short-term notes	293.8	–	–	–	293.8
Fixed income securities	179.2	2,236.8	1,122.7	–	3,538.7
Preferred shares	17.1	208.9	104.6	889.5	1,220.1
Common shares	–	–	–	799.4	799.4
Loans	22.3	114.7	77.2	28.1	242.3
Total	512.4	2,560.4	1,304.5	1,717.0	6,094.3

The following table details the Company's financial liabilities.

TABLE 4.5 – FINANCIAL LIABILITIES

	2009	2008
Accounts payable to investment brokers on unsettled trades	13.0	–
Short investment positions (Table 4.3)	183.4	–
Derivative liabilities (Table 5.1)	15.6	4.2
Embedded derivatives (note 5b)	66.8	4.9
Total	**278.8**	9.1

The following table provides additional details about the items reported in Interest income, Dividend income and Net investment losses.

TABLE 4.6 – INTEREST INCOME, DIVIDEND INCOME AND NET INVESTMENT LOSSES

	2009	2008
Amounts reported in interest and dividend income		
Interest income		
Interest income from HFT financial instruments	85.4	79.8
Interest income from AFS financial instruments	75.3	93.8
Interest income from loans and receivables	18.0	14.2
Interest from impaired fixed income securities	–	–
Total interest income	178.7	187.8
Net dividend income from HFT financial instruments	18.4	12.7
Dividend income from AFS financial instruments	112.4	144.6
Total dividend income	130.8	157.3
Expenses	(16.8)	(16.3)
Interest and dividend income, net of expenses	**292.7**	328.8
Amounts reported in net investment losses:		
Net realized gains (losses) from financial instruments classified as HFT	8.3	(4.5)
Net realized gains (losses) from financial instruments designated as HFT	140.5	(76.9)
Net realized gains (losses) from derivative financial instruments	(151.6)	81.8
Net realized losses from AFS financial instruments	(54.6)	(64.4)
Net realized gains (losses) from embedded derivatives	(62.9)	36.8
Impairments of fixed income securities	(5.6)	(10.9)
Impairments of common share equity securities	(46.2)	(250.5)
Other net gains (losses)	(0.4)	0.6
Net investment losses	**(172.5)**	(288.0)

NOTE 5 – Derivative financial instruments

a) Types of derivatives

Derivative financial instruments are financial contracts whose value is derived from an underlying interest rate, foreign exchange rate, equity or commodity instrument or index.

The company uses derivatives principally to mitigate certain risks described in note 7.

Forwards and futures

Forward contracts are tailor-made agreements that are transacted between counterparties in the over-the-counter market. Futures are standardized contracts with respect to amounts and settlement dates, and are traded on regular future exchanges.

Interest rate forwards and futures are contractual obligations to buy or sell an interest-rate sensitive financial instrument on a predetermined future date at a specified price.

Currency forwards and futures are contractual obligations to exchange one currency for another on a predetermined future date.

The Company uses forwards and futures for risk management purposes. Forwards are used to mitigate the risk arising from foreign currency fluctuations and futures are used to alter exposure to interest rate fluctuations.

Swaps

Total return swaps are over-the-counter contracts in which two counterparties exchange a series of cash flows based on agreed upon rates or value of an index, a basket of stocks or a single stock, applied to a notional amount.

Currency swaps include single currency, cross currency and cross currency interest rate swaps. Single currency swaps are agreements where two counterparties exchange a series of payments based on different interest rates (such as fixed rates for floating rates) applied to a notional amount in a single currency. Cross currency swaps involve the exchange of fixed payments in one currency for the receipt of fixed payments in another currency. Cross currency interest rate swaps involve the exchange of both interest and principal amounts in two different currencies.

The Company uses swaps for risk management purposes; mainly in conjunction with other financial instruments to synthetically alter the cash flows of certain of its financial assets and financial liabilities.

Credit derivatives

Credit derivatives are over-the-counter contracts that transfer credit risk related to an underlying financial instrument from one counterparty to another.

The Company uses credit derivatives for risk management purposes, mainly to alter credit exposure to specific bond issuers.

The following table shows the fair values and the notional amounts of derivatives by terms of maturity. Positive fair values are reported in Other receivables and negative fair values are reported in Other financial liabilities.

TABLE 5.1 – FAIR VALUES AND NOTIONAL AMOUNTS OF DERIVATIVES BY TERM TO MATURITY AND NATURE OF RISK

	Fair value		Notional amount			
As at December 31, 2009	Positive	Negative	One year or less	One year to five years	Over five years	Total
Held for non-trading purposes						
Where hedge accounting is applied						
Foreign currency exposure						
Swaps	1.6	–	–	22.9	–	22.9
Where hedge accounting is not applied						
Foreign currency exposure						
Forwards	–	–	29.3	–	–	29.3
Swaps	0.7	–	–	5.0	–	5.0
Interest rate exposure						
Total return swaps	–	–	–	–	–	–
Equity exposure						
Total return swaps	–	14.5	385.1	–	–	385.1
Options	0.7	–	1.1	11.9	2.9	15.9
Credit default swaps	0.3	1.1	–	52.4	–	52.4
Held for trading purposes						
Where hedge accounting is not applied						
Interest rate exposure						
Swaps	–	–	–	–	–	–
Futures	–	–	–	–	–	–
Credit exposure						
Credit default swaps	–	–	–	–	–	–
Total	3.3	15.6				
As at December 31, 2008						
Held for non-trading purposes						
Where hedge accounting is applied						
Foreign currency exposure						
Swaps	–	1.9	–	22.9	–	22.9
Where hedge accounting is not applied						
Foreign currency exposure						
Forwards	–	0.2	20.3	–	–	20.3
Swaps	0.1	–	0.4	–	–	0.4
Interest rate exposure						
Total return swaps	1.5	–	76.4	–	–	76.4
Equity exposure						
Total return swaps	2.2	–	75.0	–	–	75.0
Options						
Credit default swaps	–	–	–	–	–	–
Held for trading purposes						
Where hedge accounting is not applied						
Interest rate exposure						
Swaps	4.4	–	–	103.0	–	103.0
Futures	–	–	28.9	–	–	28.9
Credit exposure						
Credit default swaps	0.8	2.1	–	61.7	–	61.7
Total	9.0	4.2				

b) Embedded derivatives

An embedded derivative is a component of a hybrid (combined) instrument that also includes a non-derivative host contract. Some of the cash flows of the combined instrument vary in a way similar to a stand-alone derivative. An embedded derivative causes some or all of the cash flows that otherwise would be required by the contract to be modified according to a specified financial variable. The fair value of the embedded derivatives as at December 31, 2009 amounted to $66.8 (December 31, 2008 – $4.9) and is linked entirely to the Company's investment in perpetual preferred shares. The Company did not attempt to establish a notional amount for these embedded derivatives but a proxy for that amount could be the original cost of these perpetual preferred shares which amounted to $1,160.3 at December 31, 2009 (December 31, 2008 – $1,177.0). Embedded derivatives are reported in Other financial liabilities on the Consolidated balance sheet.

NOTE 6 – Fair value measurement

a) Determination of fair value and fair values hierarchy

In accordance with amendments to Section 3862 for financial instruments measured at fair value on the balance sheet, the Company categorizes its fair value measurements according to a three level hierarchy as described below.

Level 1

Level 1 are financial assets and liabilities that the Company measures by reference to published quotes in an active market (i.e the bid price for a financial asset and the ask price for financial liabilities). A financial instrument is regarded as quoted in an active market if quoted prices for that financial instrument are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis. When a quoted active market exists, the fair values of financial assets are based on bid prices and the fair values of financial liabilities are based on ask prices.

Level 2

In the absence of an active market, fair values are based on inputs other then quoted prices included in the Level 1 that are observable for the asset or liability directly or indirectly such as prevailing market rates for instruments with similar characteristics and risk profiles or the fair values are determined by using valuation techniques commonly used by the market participant, which refer to observable market data. Fair values determined using valuation models require the use of assumptions concerning the amount and timing of estimated future cash flows and discount rates. In determining those assumptions, the external readily observable market inputs are primarily looked at, including factors such as interest rate yield curves, currency rates, and price and rate volatilities, as applicable. Valuation techniques commonly used by the Company includes comparisons with similar instruments where observable market prices exist, discounted cash flow analysis and option pricing models.

Level 3

In limited circumstances, the Company uses input parameters that are not based on observable market data with an adjustment to reflect the uncertainty and to ensure that financial instruments are reported at fair values. Liquidity risks, relating to market prices that are not observable due to insufficient trading volume or a lack of recent trades in a less active or inactive market, will be inherent in the cash flows of an asset or liability that are factored into the valuation techniques when measuring fair value.

The split of the Company's financial instruments between each of the above mentioned levels is presented below.

TABLE 6.1 – FAIR VALUES HIERARCHY OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

As at December 31, 2009	Level 1	Level 2	Level 3	Total
Invested assets				
Debt securities				
Short-term notes	210.7	–	–	210.7
Fixed income				
Investment grade				
Government, government-guaranteed and supranational	2,691.9	566.5	–	3,258.4
Corporate	262.1	950.0	–	1,212.1
Asset-backed	–	103.1	–	103.1
Total fixed income	2,954.0	1,619.6	–	4,573.6
Equity securities				
Preferred shares				
Investment grade				
Retractable	320.7	–	–	320.7
Fixed rate perpetual	787.3	–	34.8	822.1
Other perpetual	406.8	–	32.0	438.8
Total preferred shares	1,514.8	–	66.8	1,581.6
Common shares	1,312.1	–	–	1,312.1
Total invested assets measured at fair value	5,991.6	1,619.6	66.8	7,678.0
Derivatives				
Derivative assets	–	3.3	–	3.3
Derivative liabilities	–	(15.6)	–	(15.6)
Embedded derivatives	–	–	(66.8)	(66.8)
Total derivatives	–	(12.3)	(66.8)	(79.1)
Short investment positions	183.4	–	–	183.4
Total other financial liabilities measured at fair value	183.4	–	–	183.4

Level 3 financial instruments represent embedded derivatives related to the Company's perpetual preferred shares which are reported as a derivative liability in Financial liabilities and also reported with the Equity securities in Invested assets (asset component) on the Consolidated balance sheet.

To determine the fair value of embedded derivatives, the Company uses several input parameters. The majority of these parameters are based on observable market data. One significant parameter, the implied volatility, is unobservable and is calculated using an internally developed valuation model.

Changes in the derivative liability are reported in Net investment losses on the Consolidated income statements. An equal change in the asset component is reported in OCI.

The following table shows a reconciliation of the opening and closing carrying value of the Company's embedded derivatives.

TABLE 6.2 – RECONCILIATION OF LEVEL 3 FINANCIAL INSTRUMENTS

	Carrying value at January 1, 2009	Gains (losses) reported in Net investment losses	Gains (losses) reported in OCI	Purchases	Sales	Carrying value at December 31, 2009
Asset component (Equity securities)	4.9	–	62.9	–	(1.0)	66.8
Embedded derivatives (Financial liabilities)	(4.9)	(62.9)	–	–	1.0	(66.8)

Losses reported in Net investment losses for embedded derivatives still held at December 31, 2009 amounted to $62.5.

The following table shows the impact of changing the implied volatility by 10% on the carrying value of the Company's embedded derivatives and the resulting gains (losses). The Company believes that this percentage change provides a fair indication of how the Company's Consolidated results would be impacted in the event of a significant change in volatility.

TABLE 6.3 – SENSITIVITY ANALYSIS FOR LEVEL 3 FINANCIAL INSTRUMENTS

	10% increase in volatility	10% decrease in volatility
Asset component		
Change in Equity securities	13.0	(12.3)
Change in OCI	13.0	(12.3)
Embedded derivatives		
Change in Financial liabilities	13.0	(12.3)
Additional Net investment gains (losses)	(13.0)	12.3

NOTE 7 – Risk and capital management

We have a comprehensive risk management framework and internal control procedures designed to manage and monitor various risks in order to protect our business, clients, shareholders and employees. Our risk management programs aim at avoiding risks that could materially impair our financial position, accepting risks that contribute to sustainable earnings and growth and disclosing these risks in a full and complete manner.

Effective risk management rests on identifying, understanding and communicating all risks the Company is exposed to in the course of its operations. In order to make sound business decisions, both strategically and operationally, management must have continual direct access to the most timely and accurate information possible. Either directly or through its committees, the Board of Directors ensures that the Company's management has put appropriate risk management programs in place. The Board of Directors, directly and in particular through its Audit and Risk Review Committee ("Audit Committee"), oversees the Company's risk management programs, procedures and controls and, in this regard, receives periodic reports from, among others, the risk management department through the Chief Risk Officer, internal auditors and the independent auditors. A summary of the Company's key risks arising from its financial instruments and the processes for managing and mitigating them is outlined below. For more information on the risks arising from the Company's financial instruments and its operations all together, refer to the Risk management section of the 2009 Management Discussion and Analysis related to these Consolidated financial statements.

The majority of the invested assets portfolio is invested in well-established, active and liquid markets. See note 6 Fair value measurement to see how the Company categorizes its fair value measurements according to a three level hierarchy.

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: currency risk, interest rate risk and other market price risk, such as equity price risk. The Company's exposures to market risk together with the Company's risk management practices used to mitigate these risks are explained below. The Company's investment policies establish principles and limits pertaining to these risks. The Investment Committee regularly monitors compliance with these investment policies.

a) Equity price risk

Equity price risk is the risk of losses arising from movements in equity market prices. The Company is significantly exposed to changes in equity market prices.

Sensitivity analysis is one risk management technique that assists management in ensuring that risks assumed remain within the company's risk tolerance level. Sensitivity involves varying a single factor to assess the impact that this would have on the Company's results and financial condition.

For example, a 10% increase in equity markets, excluding the impact of any impairment, would have no impact on income before taxes. However, it would result in a linear increase of OCI by $53.6 million. A 10% decrease in equity prices would have the corresponding opposite effect, lowering OCI by the same amount.

The above sensitivity analysis was prepared using key assumptions as described below:

– the securities in the Company's portfolio are not impaired;

– interest rates and equity prices move independently.

To mitigate these risks, the Company's investment policies set forth limits for each type of investment and compliance with the policies is closely monitored by the Investment Committee. The Company manages market risk through asset class and economic sector diversification and, in some cases, the use of derivatives.

b) Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company is significantly exposed to changes in interest rates. Movements in short-term and long-term interest rates, including change in credit spreads cause changes in the realized and unrealized gains/losses.

For example, a 100 basis point increase in interest rates would increase income before taxes by approximately $21.9 million for the Company's AFS fixed income securities or preferred securities, as a result of marking to market the written call option liabilities embedded in the Company's redeemable preferred shares. A 100 basis point increase would also decrease OCI by approximately $219.3 million. Conversely, a 100 basis point decrease in interest rates would lower income before taxes and increase OCI by the same amounts, respectively.

The above sensitivity analysis was prepared using key assumptions as described below:

– the securities in the Company's portfolio are not impaired;

– interest rates and equity prices move independently;

– shifts in the yield curve are parallel;

– credit and liquidity risks have not been considered.

For our HFT debt securities, the estimated impact on income before taxes is assumed to be offset by the MYA. In addition, it is important to note that AFS securities in an unrealized loss position, as reflected in OCI, may at some point in the future be realized either through a sale or impairment.

The Company's exposure to the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates is detailed in table 7.1.

Interest rate risk exposures are reported based on the earlier of financial instruments contractual repricing date or maturity date. Effective interest rates have been disclosed where applicable. The effective rates shown in the table below represent historical rates for fixed-rate instruments carried at amortized cost and current market rates for floating-rate instruments or instruments carried at fair value. The following table does not incorporate management's expectation of future events where expected repricing or maturity dates differ significantly from the contractual dates.

TABLE 7.1 – EXPOSURE TO INTEREST RATE RISK

		Fixed rate				
As at December 31, 2009	Floating rates	Under 12 months	Over 1 to 5 years	Over 5 years	Non-rate sensitive	Total
Assets						
Cash on hand net of overdrafts	(32.4)	–	–	–	–	(32.4)
Cash and cash equivalents	–	92.5	–	–	–	92.5
Effective interest rate		0.19%				
Short-term notes	–	210.7	–	–	–	210.7
Effective interest rate		0.21%				
Fixed income securities	14.4	141.6	3,030.9	1,386.7	-	4,573.6
Effective interest rate		1.38%	2.62%	4.04%		
Preferred shares	118.8	12.3	513.9	936.6	–	1,581.6
Effective interest rate		5.08%	5.00%	5.50%		
Common shares	–	–	–	–	1,312.1	1,312.1
Loans	–	33.0	154.1	131.4	–	318.5
Effective interest rate		5.94%	5.90%	5.76%		
Reinsurance assets	–	100.4	107.4	34.7	18.1	260.6
Effective interest rate		3.71%	3.71%	3.71%		
Other assets	–	–	3.3	0.1	3,030.7	3,034.1
Total assets	100.8	590.5	3,809.6	2,489.5	4,360.9	11,351.3
Liabilities and shareholders' equity						
Claims liabilities	–	1,767.8	1,891.6	610.6	–	4,270.0
Effective interest rate		3.71%	3.71%	3.71%		
Debt outstanding	–	–	–	397.7	–	397.7
Effective interest rate				5.78%		
Financial liabilities	16.9	210.9	16.2	34.8	–	278.8
Effective interest rate	–	1.95%	4.66%	5.50%		
Other liabilities	–	–	–	–	3,422.2	3,422.2
Shareholders' equity	–	–	–	–	2,982.6	2,982.6
Total liabilities and shareholders' equity	16.9	1,978.7	1,907.8	1,043.1	6,404.8	11,351.3
Net long (short) exposure	83.9	(1,388.2)	1,901.8	1,446.4	(2,043.9)	–

As at December 31, 2008	Floating rates	Fixed rate Under 12 months	Fixed rate Over 1 to 5 years	Fixed rate Over 5 years	Non-rate sensitive	Total
Assets						
Cash on hand net of overdrafts	27.3	–	–	–	–	27.3
Cash and cash equivalents	–	483.1	–	–	–	483.1
Effective interest rate		1.29%				
Short–term notes	–	293.8	–	–	–	293.8
Effective interest rate		1.24%				
Fixed income securities	170.0	173.5	2,072.5	1,122.7	–	3,538.7
Effective interest rate		3.40%	3.02%	5.03%		
Preferred shares	71.5	9.0	410.9	728.7	–	1,220.1
Effective interest rate		4.95%	6.17%	7.21%		
Common shares	–	–	–	–	799.4	799.4
Loans	–	22.3	114.7	105.3		242.3
Effective interest rate		6.28%	6.27%	6.21%		
Reinsurance assets	–	68.1	104.5	34.4	17.2	224.2
Effective interest rate		4.24%	4.24%	4.24%		
Other assets	8.1	–	0.9	–	2,947.3	2,956.3
Total assets	276.9	1,049.8	2,703.5	1,991.1	3,763.9	9,785.2
Liabilities and shareholders' equity						
Claims liabilities	–	1,337.3	2,052.8	674.8	–	4,064.9
Effective interest rate		4.24%	4.24%	4.24%		
Debt outstanding	–	–	–	–	–	–
Effective interest rate	–	–	–	–	–	–
Financial liabilities	0.9	0.2	5.1	2.9	–	9.1
Effective interest rate	–	0.00%	1.70%	7.21%		
Other liabilities	–	–	–	–	3,078.6	3,078.6
Shareholders' equity	–	–	–	–	2,632.6	2,632.6
Total liabilities and shareholders' equity	0.9	1,337.5	2,057.9	677.7	5,711.2	9,785.2
Net long (short) exposure	276.0	(287.7)	645.6	1,313.4	(1,947.3)	–

c) 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. The Company is not significantly exposed to changes in exchange rates. Although the Company is exposed to some foreign exchange risks arising from securities in some of its U.S. dollar–denominated assets, the general policy is to minimize foreign currency exposure. The Company mitigates foreign exchange rate risks by buying or selling successive monthly foreign exchange forward contracts or entering into foreign exchange swaps.

d) Basis risk

The Company's use of derivatives exposes it to a number of risks, including credit risk, interest rate and equity market fluctuations. The hedging of certain risks with derivatives results in basis risk. Basis risk is the risk that offsetting investments in a hedging strategy will not experience price changes in entirely opposite directions from each other. This imperfect correlation between the two investments creates the potential for excess gains or losses in a hedging strategy, thus adding risk to the position. The Company monitors the effectiveness of its hedges on a regular basis.

e) Credit risk

Credit risk is the possibility that counterparties may not be able to meet payment obligations when they become due. A counterparty is any person or entity from which cash or other forms of consideration are expected to extinguish a liability or obligation to us. The Company's credit risk exposure is concentrated primarily in its fixed income, preferred share portfolios, over the counter derivatives and, to a lesser extent, in its reinsurance recoverable and annuity agreements entered into with various life insurance companies.

Maximum exposure to credit risk

The table below details the Company's maximum exposure to credit risk without taking into account any collateral held or other credit enhancements available to the Company to mitigate this risk. For on-balance sheet exposures, maximum credit exposure is defined as the carrying value of the asset net of any impairment losses. Detail on these credit risk exposures including information on how the Company mitigates these, is given in the remaining part of the note.

TABLE 7.2 – MAXIMUM EXPOSURE TO CREDIT RISK

	2009	2008
On-balance sheet credit risk exposure		
Cash and cash equivalents	60.1	510.4
Debt securities	4,784.3	3,832.5
Equity securities	2,893.7	2,019.5
Loans	318.5	242.3
Derivative assets (Table 5.1)	3.3	9.0
Premium receivable	1,640.5	1,469.4
Reinsurance assets	260.6	224.2
Other financial assets[1]	325.0	493.7
Total on-balance sheet credit risk exposure	10,286.0	8,801.0
Off-balance sheet credit risk exposure		
Original price of annuities purchased[2]	425.9	391.1
Total off-balance sheet credit risk exposure	425.9	391.1

1 Other financial assets include the following amounts as reported on the Consolidated balance sheets: Accrued interest and dividend income, Other receivables less derivative assets and Income taxes receivable.
2 See paragraph titled Structured settlements below for details.

Structured settlements

The Company enters into annuity agreements with various Canadian life insurance companies which have credit ratings of at least A- or higher, to provide for fixed and recurring payments to claimants. Under such arrangements, the Company derecognizes the liability from its Consolidated balance sheet as the liability to its claimants is substantially discharged, although the Company remains exposed to the credit risk may life insurers fail to fulfill their obligations.

At December 31, 2009, none of the life insurers from which the Company had purchased annuities was in default and no provision for credit risk was required. The original purchase price of the annuities totalled $425.9 (2008 – $391.1). The risk-adjusted balance is determined by applying the standard OSFI defined measures of counterparty risk to the credit equivalent amount and is $1.1 at December 31, 2009 (2008 – $1.0).

Invested assets

The Company's risk management strategy is to invest in fixed income instruments and preferred shares of high credit quality issuers and to limit the amount of credit exposure with respect to any one issuer by imposing limits based upon credit quality. The Company's investment policy requires that, at the time of the investment, substantially all fixed income securities have a minimum credit rating of BBB and preferred shares have a minimum credit rating of P3. Management monitors subsequent credit rating changes on a regular basis.

For subsidiaries of the Company who are regulated by OSFI, the assets invested in any entity or group of related entities are limited to 5% of the subsidiaries' assets by OSFI. The Company also monitors aggregate concentrations of credit risk by country of issuance and by industry. See table 7.4 below.

The Company receives guarantees for loans.

Derivative-related

Credit risk from derivative transactions reflects the potential for the counterparty to default on its contractual obligations when one or more transactions have a positive market value to the Company. Therefore, derivative-related credit risk is represented by the positive fair value of the instrument and is normally a small fraction of the contract's notional amount.

The Company subjects its derivative-related credit risk to the same credit approval, limit and monitoring standards that it uses for managing other transactions that create credit exposure. This includes evaluating the creditworthiness of counterparties, and managing the size, diversification and maturity structure of the portfolio. Credit utilization for all products is compared with established limits on a continual basis and is subject to quarterly review by the Investment Committee.

Netting is a technique that can reduce credit exposure from derivatives and is generally facilitated through the use of netting clauses in master derivative agreements. The netting clauses in a master derivative agreement provide for a single net settlement of all financial instruments covered by the agreement in the event of default. However, credit risk is reduced only to the extent that the Company's financial obligations toward the counterparty to such an agreement can be set off against obligations such counterparty has toward us. The Company uses netting clauses in master derivative agreements to reduce derivative-related credit exposure. The overall exposure to credit risk that is reduced through the netting clauses may change substantially following the reporting date as the exposure is affected by each transaction subject to the agreement as well as by changes in underlying market rates and values.

The use of collateral is another significant credit mitigation technique for managing derivative-related counterparty credit risk. Mark-to-market provisions in the Company's agreements with some counterparties provide the Company with the right to request that the counterparty pay down or collateralize the current market value of its derivatives positions when the value passes a specified threshold amount.

Replacement cost represents the total fair value of all outstanding contracts in a gain position, before factoring in the master netting agreements. The amounts in the table below exclude fair value relating to exchange-traded instruments as they are subject to daily margining and are deemed to have no credit risk.

The credit equivalent amount is the sum of the replacement cost plus an add-on amount for potential future credit exposure as defined by OSFI. The risk-adjusted balance is determined by applying the standard OSFI-defined measures of counterparty risk to the credit equivalent amount.

TABLE 7.3 – DERIVATIVE-RELATED CREDIT RISK

As at December 31, 2009	Replacement cost	Credit equivalent amount	Risk adjusted balance
Total derivative assets	**3.3**	**34.9**	**0.1**
Less: Impact of master netting agreements	**(0.3)**	–	–
Less: cash collateral	–	–	–
Total after netting agreements	**3.0**	**34.9**	**0.1**
As at December 31, 2008			
Total derivative assets	9.0	28.8	0.1
Less: Impact of master netting agreements	(2.0)	–	–
Less: cash collateral	(1.6)	–	–
Total after netting agreements	5.4	28.8	0.1

Reinsurance

The Company relies on reinsurance to manage the underwriting risk. Although reinsurance makes the assuming reinsurer liable to us to the extent of the risk ceded, we are not relieved of our primary liability to our policyholders as the direct insurer. As a result, we bear credit risk with respect to our reinsurers. There is no certainty that our reinsurers will pay all reinsurance claims on a timely basis or at all.

The Company assesses the financial soundness of the reinsurers before signing any reinsurance treaties and monitors their situation on a regular basis. In addition, the Company has minimum rating requirements for its reinsurers. Substantially, all reinsurers are required to have a minimum credit rating of A- at inception of the treaty. Rating agencies used are A.M. Best and Standard & Poors. The Company also requires that most of its treaties have a security review clause allowing the Company to replace a reinsurer during the treaty period should the reinsurer's credit rating fall below the level acceptable to the Company. Management concluded that the Company was not exposed to significant loss from reinsurers for potentially uncollectible reinsurance as at the Consolidated balance sheet dates.

The Company is the assigned beneficiary of collateral consisting of cash, trust accounts and letters of credit totalling $67.7 at December 31, 2009 (2008 – $84.5) as guarantee from unlicensed reinsurers. There were no amounts from affiliated reinsurers in 2009 (2008 – $56.9). This collateral is held in support of policy liabilities of $51.9 at December 31, 2009 (2008 – $48.8) and could be used should these reinsurers be unable to meet their obligations.

Concentration of credit risk

Concentration of credit risk exists where a number of borrowers or counterparties are engaged in similar activities, are located in the same geographic area or have comparable economic characteristics. Their ability to meet contractual obligations may be similarly affected by changing economic, political or other conditions. The Company's invested assets could be sensitive to changing conditions in specific geographic regions or specific industries. The Company has a significant concentration of its invested assets in the financial sector. This risk concentration is closely monitored by the Company and it hedges some of the risk as it deems necessary.

TABLE 7.4 – CONCENTRATIONS OF CREDIT RISK FOR INVESTED ASSETS

As at December 31	2009	2008
By country of issuer		
Canada	92.8%	89.3%
US	0.7%	1.1%
Other	6.5%	9.6%
Total	100.0%	100.0%
By industry		
Government	43.4%	40.4%
Banks, insurance and diversified financial services	37.3%	41.2%
Energy	5.0%	5.0%
Other	14.3%	13.4%
Total	100.0%	100.0%

f) Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in raising funds to meet obligations associated with financial liabilities. To manage its cash flow requirements, the Company maintains a portion of its invested assets in liquid securities. A maturity analysis for non-derivative financial invested assets is presented in table 4.4 and a maturity analysis of derivative assets (corresponding to the fair value positive amounts) presented in table 5.1. See note 13 for the maturity profile of the Company's medium term notes.

The Company's liquidity management is governed by establishing a prudent policy that identifies oversight responsibilities as well as by setting limits and implementing effective techniques to monitor, measure and control exposure to liquidity risk. A portion of invested assets is maintained in short-term (less than one year) highly liquid money market securities, which are used to manage the operational requirements of the Company. A large portion of the invested assets are held in highly liquid federal and provincial government debt to protect against any unanticipated large cash requirements. The Company also has an unsecured committed credit facility, see note 13 b.

g) Fair value disclosure

The fair values of financial instruments and policy liabilities are disclosed in notes 4, 5, 6, 7 and 8 respectively. The fair value of other financial assets and liabilities approximates their carrying amount due to their short-term nature.

h) Capital management

The Company's objectives when managing capital consist of maintaining sufficient capital to support claims liabilities and ensure the confidence of policyholders, support competitive pricing strategies, meet regulatory capital requirements, provide returns for its shareholders and maintain a leadership position in the Canadian P&C insurance industry.

The P&C insurance subsidiaries of the Company are subject to the regulatory capital requirements defined by OSFI and the Insurance Companies Act ("ICA"). OSFI has established a Minimum Capital Test guideline ("MCT") which sets out 100% as the minimum and 150% as the supervisory target MCT standards for P&C insurance companies.

The following table presents the aggregate minimum capital test for the Company's P&C insurance subsidiaries.

TABLE 7.5 – MCT

As at December 31	2009	2008
Total capital available	**2,729.2**	2,096.5
Total capital required	**1,176.9**	1,023.0
Excess capital	**1,552.3**	1,073.5
MCT %	**231.9%**	205.0%
Excess capital at 150%	**963.8**	562.0

Total capital available and total capital required represent amounts applicable to the Company's P&C insurance subsidiaries and are determined in accordance with prescribed OSFI rules. Total capital available mostly represents total equity less specific deductions for disallowed assets including goodwill and intangibles. Total capital required is calculated by allocating assets and liabilities into categories and applying prescribed risk factors to each category. As at December 31, 2009, the Company's P&C insurance subsidiaries were in compliance with both OSFI and ICA requirements as well as internal targets.

Annually the Company performs Dynamic Capital Adequacy Testing on the MCT to ensure that the Company has sufficient capital to withstand significant adverse event scenarios. These scenarios are reviewed each year to ensure appropriate risks are included in the testing process. The 2009 results indicated that the Company's capital position is strong. In addition, the target, actual and forecasted capital position of the Company is subject to ongoing monitoring by management using stress and scenario analysis to ensure its adequacy.

NOTE 8 – Policy liabilities

Policy liabilities are established to reflect the estimate of the total amount of all liabilities associated with the insurance policies at the Consolidated balance sheet dates, including claims IBNR. The ultimate cost of these liabilities will vary from the best estimate for a variety of reasons, including additional information with respect to the facts and circumstances of the claims incurred.

a) Movements of net claims liabilities

The following table shows the movements of the Company's net claims liabilities during the year.

TABLE 8.1 – MOVEMENTS OF NET CLAIMS LIABILITIES

	Direct claims liabilities	Reinsurers' share	Net claims liabilities
As at December 31, 2009			
Balance, beginning of year	**4,064.9**	**207.0**	**3,857.9**
Claims incurred	**3,018.6**	**59.3**	**2,959.3**
Prior year (favourable) claims development	**(121.5)**	**2.2**	**(123.7)**
Increase due to changes in discount rate	**44.3**	**2.7**	**41.6**
Claims paid	**(2,736.3)**	**(28.6)**	**(2,707.7)**
Balance, end of year	**4,270.0**	**242.6**	**4,027.4**
As at December 31, 2008			
Balance, beginning of year	3,989.0	256.9	3,732.1
Claims incurred	2,931.6	23.2	2,908.4
Prior year (favourable) claims development	(161.9)	(23.3)	(138.6)
Increase due to changes in discount rate	38.7	2.3	36.4
Claims paid	(2,732.5)	(52.1)	(2,680.4)
Balance, end of year	4,064.9	207.0	3,857.9

b) Amounts by line of business

The following table details net claims liabilities by line of business.

TABLE 8.2 – NET CLAIMS LIABILITIES

	Direct claims liabilities	Reinsurers' share	Net claims liabilities
December 31, 2009			
Personal lines			
Auto: liability	**1,477.7**	**6.1**	**1,471.6**
Auto: personal accident	**856.6**	**11.5**	**845.1**
Auto: other	**78.6**	**5.9**	**72.7**
Property	**489.8**	**90.8**	**399.0**
Other	**5.1**	**1.0**	**4.1**
Total	**2,907.8**	**115.3**	**2,792.5**
Commercial lines			
Auto: liability	**283.8**	**2.0**	**281.8**
Auto: personal accident	**47.3**	**0.5**	**46.8**
Auto: other	**12.0**	**0.9**	**11.1**
Property	**207.2**	**23.3**	**183.9**
Liability	**803.9**	**98.0**	**705.9**
Other	**8.0**	**2.6**	**5.4**
Total	**1,362.2**	**127.3**	**1,234.9**
Balance, end of year	**4,270.0**	**242.6**	**4,027.4**
December 31, 2008			
Personal lines			
Auto: liability	1,466.2	8.7	1,457.5
Auto: personal accident	727.3	15.8	711.5
Auto: other	105.9	2.2	103.7
Property	472.2	61.3	410.9
Other	8.0	1.5	6.5
Total	2,779.6	89.5	2,690.1
Commercial lines			
Auto: liability	302.3	4.0	298.3
Auto: personal accident	43.1	1.2	41.9
Auto: other	13.1	0.1	13.0
Property	170.8	9.4	161.4
Liability	749.0	101.1	647.9
Other	7.0	1.7	5.3
Total	1,285.3	117.5	1,167.8
Balance, end of year	4,064.9	207.0	3,857.9

The following table details unearned premiums by line of business.

TABLE 8.3 – UNEARNED PREMIUMS

	Unearned premiums	Reinsurers' share	Net unearned premiums
December 31, 2009			
Personal lines			
Auto: liability	563.5	–	563.5
Auto: personal accident	214.3	–	214.3
Auto: other	475.7	–	475.7
Property	612.2	–	612.2
Other	3.3	–	3.3
Total	1,869.0	–	1,869.0
Commercial lines			
Auto: liability	87.9	0.3	87.6
Auto: personal accident	12.9	–	12.9
Auto: other	62.7	–	62.7
Property	252.7	3.5	249.2
Liability	147.0	1.3	145.7
Other	31.4	12.9	18.5
Total	594.6	18.0	576.6
Balance, end of year	2,463.6	18.0	2,445.6
December 31, 2008			
Personal lines			
Auto: liability	539.3	–	539.3
Auto: personal accident	191.6	–	191.6
Auto: other	483.1	–	483.1
Property	576.7	–	576.7
Other	6.9	–	6.9
Total	1,797.6	–	1,797.6
Commercial lines			
Auto: liability	85.6	0.3	85.3
Auto: personal accident	12.2	–	12.2
Auto: other	61.2	–	61.2
Property	240.1	3.6	236.5
Liability	144.6	1.5	143.1
Other	25.5	11.8	13.7
Total	569.2	17.2	552.0
Balance, end of year	2,366.8	17.2	2,349.6

c) Fair value of net claims liabilities

The Company estimates that the fair value of net claims liabilities approximate their carrying amounts. There was no premium deficiency at the Consolidated balance sheet dates.

The following table shows the impact of both the time value of money and the provision for adverse deviation on the carrying amount of claims liabilities.

TABLE 8.4 – DISCOUNTING OF CLAIMS LIABILITIES

	2009			2008		
	Claims liabilities	**Reinsurers' share**	**Net**	Claims liabilities	Reinsurers' share	Net
Undiscounted value	**4,218.0**	**239.0**	**3,979.0**	4,004.7	212.5	3,792.2
Effect of time value of money using a rate of 3.71% (2008 – 4.24%)	**(345.3)**	**(17.0)**	**(328.3)**	(370.5)	(25.6)	(344.9)
Provision for adverse deviation	**397.3**	**20.6**	**376.7**	430.7	20.1	410.6
Carrying amount	**4,270.0**	**242.6**	**4,027.4**	4,064.9	207.0	3,857.9

Since the time value of money is considered when determining the claims liabilities estimate, an increase or decrease in the discount rate would result in a decrease or increase in claims liabilities, respectively. A 1% change in the discount rate would have an impact of $91.8 on the fair value of claims liabilities at December 31, 2009 (2008 – $85.0).

d) Reinsurance

In the ordinary course of business, the Company reinsures certain risks with other reinsurers to limit its maximum loss in the event of catastrophes or other major losses. The following table shows the Company's net retention and coverage limits by nature of risk.

TABLE 8.5 – REINSURANCE NET RETENTION AND COVERAGE LIMITS BY NATURE OF RISK

	2009	2008
Single risk events[1]		
Net retentions:		
On property policies	**5.0**	5.0
On liability policies		
From January 1st to June 30th	**7.0**	7.0
From July 1st to December 31st	**10.0**	7.0
Multi-risk events and catastrophes		
Net retentions:	**25.0**	25.0
Coverage limit:	**1,500.0**	1,250.0
Risk retained based on the loss exposure:		
$0–$25 million	**100.00%**	100.00%
$25–$50 million	**16.75%**	10.00%
$50–$750 million	**10.00%**	10.00%

1 For certain special classes of business or types of risks, the retention would be lower through specific treaties or the use of facultative reinsurance.

TABLE 8.6 – NET IMPACT OF REINSURANCE ON THE CONSOLIDATED STATEMENTS OF INCOME

	2009	2008
Reduction in:		
Premiums earned	**(109.5)**	(97.8)
Claims incurred	**64.2**	2.2
Commissions expense	**15.7**	15.6
Net impact before income taxes	**(29.6)**	(80.0)

NOTE 9 – Income taxes

a) Income tax expense (benefit)

The following table shows the current and future portion of the Company's income tax expense reported on the Consolidated statements of income.

TABLE 9.1 – CONSOLIDATED STATEMENTS OF INCOME

	2009	2008
Current	(10.4)	(28.9)
Future	23.5	24.3
Income tax expense (benefit)	13.1	(4.6)

The following table shows the current and future portion of the Company's income tax expense reported on the Consolidated statements of comprehensive income (loss).

TABLE 9.2 – CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

	2009	2008
Current	131.4	(123.5)
Future	17.6	(5.3)
Income tax expense (benefit)	149.0	(128.8)

b) Effective income tax rate

The effective rates of income tax on the Consolidated statements of income are different from the combined Canadian federal and provincial income tax rate of 31.8% (2008: 32.2%) as set out in the following table:

TABLE 9.3 – EFFECTIVE TAX RATE RECONCILIATION

	2009 %	2008 %
Income tax expense calculated at statutory tax rates	31.8	32.2
Increase (decrease) in income tax rates resulting from:		
Non-taxable dividend income	(26.4)	(35.8)
Benefit from tax rate differential applicable to losses carry back to prior years	–	(9.9)
Losses for which a benefit is not recognized or written off	1.2	7.9
Non-deductible (non-taxable) other loss (income)	(1.2)	3.3
(Non-taxable) non-deductible portion of capital (gains) losses	5.1	(0.5)
Recovery of tax asset not recognized	(2.5)	(1.0)
Other	1.4	–
Effective income tax rate	9.4	(3.8)

c) Components of future income tax asset and liability

The following table shows the components of future tax assets and liabilities by source of temporary difference as reported on the Company's Consolidated balance sheets.

TABLE 9.4 – COMPONENTS OF FUTURE INCOME TAX ASSET AND LIABILITY

	2009	2008
Future income tax asset		
Net claims liabilities	57.7	58.9
Invested assets	2.6	13.2
Expenses deferred for tax purposes	36.0	36.7
Property and equipment	3.6	1.2
Losses available for carry-forward	15.5	4.5
Other	1.4	–
Total future income tax asset	116.8	114.5
Future income tax liability		
Deferred income for tax purposes	41.9	–
Deferred gains and losses on specified debt obligations	27.7	37.1
Pension and post retirement benefit plans	19.7	15.8
Property and equipment	6.4	–
Other	8.9	7.4
Total future income tax liability	104.6	60.3
Net future income tax asset	12.2	54.2
Reported in:		
Future income tax asset	38.0	66.0
Future income tax liability	25.8	11.8

The Company recognized a future tax asset for all of its unused non-capital losses as at December 31, 2009 and 2008.

At December 31, 2009 the Company had allowable capital losses of $56.7 (2008 – $67.7), which had not been recognized when computing the future tax asset because it is more likely than not that the Company would not be able to recover the tax asset in the foreseeable future. These losses, which have no expiry date, can be used to reduce future taxable capital gains.

NOTE 10 – Other assets

The following table shows the components of other assets.

TABLE 10.1– COMPONENTS OF OTHER ASSETS

	2009	2008
Property and equipment (table 10.2)	**46.3**	49.2
Prepaid pension asset (note 12)	**118.4**	102.2
Long-term investments (table 10.3)		
In affiliates	**98.3**	64.1
Carried at cost	**20.3**	14.6
Prepaids	**8.3**	7.3
Other	**1.3**	1.2
Total other assets	**292.9**	238.6

The following table details the property and equipment as well as the related accumulated amortization.

TABLE 10.2 – PROPERTY AND EQUIPMENT DETAILS

	2009			2008		
	Cost	Accumulated amortization	Carrying amount	Cost	Accumulated amortization	Carrying amount
Computer equipment	**78.8**	**72.3**	**6.5**	73.0	64.5	8.5
Furniture and equipment	**64.5**	**42.3**	**22.2**	59.3	36.4	22.9
Leasehold improvements	**34.7**	**17.2**	**17.5**	31.8	14.1	17.7
Land and buildings	**0.1**	**–**	**0.1**	0.1	–	0.1
Total	**178.1**	**131.8**	**46.3**	164.2	115.0	49.2

Long-term investments in affiliates

The following table presents the movements in the long-term investments in affiliates during the year.

TABLE 10.3 – MOVEMENT OF LONG-TERM INVESTMENTS

	2009	2008
Balance, beginning of year	**64.1**	51.1
Net acquisitions	**30.5**	9.1
Income	**10.8**	9.7
Dividends	**(7.1)**	(5.8)
Balance, end of year	**98.3**	64.1

During the year, there were no events or changes in circumstances that indicated that the carrying amounts of these investments may not be recoverable. Total dividends received from investments carried at cost amounted to $1.1 for the year ended December 31, 2009 (December 31, 2008 – $1.0). These dividends are reported in dividend income on the Consolidated statements of income.

NOTE 11 – Goodwill and intangible assets

The following table shows the changes in goodwill and intangible assets that occurred during the year.

TABLE 11.1 – GOODWILL AND INTANGIBLE ASSETS CONTINUITY SCHEDULE

		Intangibles		
As at December 31, 2009	Goodwill	Customer relationships and rights to offer renewals	Interanlly developed software	Total intangibles
Cost, beginning of year	**160.8**	**83.4**	**106.2**	**189.6**
Accumulated amortization, beginning of year	**–**	**(26.4)**	**(26.8)**	**(53.2)**
Carrying value, beginning of year	**160.8**	**57.0**	**79.4**	**136.4**
Acquisitions and costs capitalized (note 17)	**17.8**	**11.0**	**37.0**	**48.0**
Dispositions	**–**	**–**	**–**	**–**
Amortization expense	**–**	**(8.9)**	**(15.9)**	**(24.8)**
Cost, end of year	**178.6**	**94.4**	**143.2**	**237.6**
Accumulated amortization end of year	**–**	**(35.3)**	**(42.7)**	**(78.0)**
Carrying value, end of year	**178.6**	**59.1**	**100.5**	**159.6**
As at December 31, 2008				
Cost, beginning of year	159.9	80.2	75.8	156.0
Accumulated amortization, beginning of year	–	(18.4)	(16.0)	(34.4)
Carrying value, beginning of year	159.9	61.8	59.8	121.6
Acquisitions and costs capitalized (note 17)	2.8	4.4	30.4	34.8
Dispositions	(1.9)	(1.2)	–	(1.2)
Amortization expense	–	(8.0)	(10.8)	(18.8)
Cost, end of year	160.8	83.4	106.2	189.6
Accumulated amortization end of year	–	(26.4)	(26.8)	(53.2)
Carrying value, end of year	160.8	57.0	79.4	136.4

No impairment of goodwill and intangibles was identified in either 2009 or 2008.

NOTE 12 – Employee future benefits

The Company has several defined benefit pension plans. For these plans, the measurement date is December 31 and, for most plans, the latest actuarial valuations were performed as of December 31, 2008.

The Company offers employer paid post retirement benefit ("PRB") plans offering life insurance and health benefits to certain retirees, which are closed to active employees. The post retirement benefits are unfunded. The measurement date for post retirement benefits is December 31 and the latest actuarial valuations were performed as of December 31, 2006.

The following table shows the details of the movements in the Company's pension plans.

TABLE 12.1 – PENSION PLAN MOVEMENTS

	Benefit obligation	Plan assets	Unrecognized liabilities (assets) amounts	Total net assets (liabilities)	Expenses (revenue)
Balance as at December 31, 2008	**(448.7)**	**459.7**	**68.0**	**79.0**	**–**
Employer current service cost	**(17.9)**	**–**	**–**	**(17.9)**	**17.9**
Interest costs on benefit obligation	**(30.6)**	**–**	**–**	**(30.6)**	**30.6**
Actuarial assumptions movements					
Net actuarial gains (losses)	**(80.3)**	**–**	**80.3**	**–**	**–**
Actual return on assets	**–**	**99.2**	**(99.2)**	**–**	**–**
Expected return on assets	**–**	**–**	**32.6**	**32.6**	**(32.6)**
Change in valuation allowance	**–**	**–**	**–**	**–**	**–**
Amortization	**–**	**–**	**4.5**	**4.5**	**(4.5)**
Cash movements					
Employees contributions	**(6.4)**	**6.4**	**–**	**–**	**–**
Employer contributions	**–**	**28.5**	**–**	**28.5**	**–**
Benefits paid	**23.1**	**(23.1)**	**–**	**–**	**–**
Settlements	**–**	**–**	**–**	**–**	**–**
Balance as at December 31, 2009	**(560.8)**	**570.7**	**86.2**	**96.1**	**11.4**
Balance as at December 31, 2007	(553.2)	586.4	44.1	77.3	–
Employer current service cost	(27.2)	–	–	(27.2)	27.2
Interest costs on benefit obligation	(29.4)	–	–	(29.4)	29.4
Actuarial assumptions movements					
Net actuarial gains (losses)	133.7	–	(133.7)	–	–
Actual return on assets	–	(113.4)	113.4	–	–
Expected return on assets	–	–	40.3	40.3	(40.3)
Change in valuation allowance	–	–	0.1	0.1	(0.1)
Amortization	–	–	7.1	7.1	(7.1)
Cash movements					
Employees contributions	(6.0)	6.0	–	–	–
Employer contributions	–	14.1	–	14.1	–
Benefits paid	21.9	(21.9)	–	–	–
Settlements	11.5	(11.5)	(3.3)	(3.3)	3.3
Balance as at December 31, 2008	(448.7)	459.7	68.0	79.0	12.4

The following table shows the Company's pension plans and post retirement benefits funding status as well as the split of the Net prepaid assets as reported in Other assets and Other liabilities.

TABLE 12.2 – FUNDING STATUS

	Pension plans		Post retirement benefits	
	2009	2008	**2009**	2008
Benefit obligation	**(560.8)**	(448.7)	**(14.8)**	(15.3)
Fair value of plan assets	**570.7**	459.7	**–**	–
Surplus (deficit)	**9.9**	11.0	**(14.8)**	(15.3)
Unrecognized amounts:				
Actuarial losses	**105.7**	97.9	**2.8**	3.5
Past service costs	**2.2**	2.6	**(4.2)**	(4.7)
Transition (asset) obligation	**(21.1)**	(31.6)	**0.6**	0.7
Valuation allowance	**(0.6)**	(0.8)	**–**	–
Net prepaid asset (accrued liability) at the end of the year	**96.1**	79.1	**(15.6)**	(15.8)
Reported in:				
Other assets (note 11)	**118.4**	102.2	**–**	–
Other liabilities	**22.3**	23.1	**15.6**	15.8

Some of the Company's pension plans are not fully funded. For these plans, the aggregate amount of benefit obligation is $347.0 in 2009 ($272.6 in 2008), and the fair value of plan assets is $296.2 in 2009 ($227.7 in 2008), which results in a net deficit of $50.8 in 2009 ($44.9 in 2008).

The following table shows the details of the movements in the Company's post retirement benefit plans.

TABLE 12.3 – POST RETIREMENT BENEFITS PLAN MOVEMENTS

	Benefit obligation	Plan assets	Unrecognized liabilities (assets) amounts	Total net assets (liabilities)	Expenses (revenue)
Balance as at December 31, 2008	**(15.3)**	**–**	**(0.5)**	**(15.8)**	**–**
Interest costs on benefit obligation	**(0.9)**	**–**	**–**	**(0.9)**	**0.9**
Actuarial gains (losses)	**0.5**	**–**	**(0.5)**	**–**	**–**
Amortization	**–**	**–**	**0.2**	**0.2**	**(0.2)**
Cash movements					
Employer contributions	**–**	**0.9**	**–**	**0.9**	**–**
Benefits paid	**0.9**	**(0.9)**	**–**	**–**	**–**
Balance as at December 31, 2009	**(14.8)**	**–**	**(0.8)**	**(15.6)**	**0.7**
Balance as at December 31, 2007	(15.8)	–	(0.2)	(16.0)	–
Interest costs on benefit obligation	(0.8)	–	–	(0.8)	0.8
Actuarial gains or losses	0.4	–	(0.4)	–	–
Amortization	–	–	0.1	0.1	(0.1)
Cash movements					
Employer contributions	–	0.9	–	0.9	–
Benefits paid	0.9	(0.9)	–	–	–
Balance as at December 31, 2008	(15.3)	–	(0.5)	(15.8)	0.7

The following table shows the composition of the Company's pension plan assets.

TABLE 12.4 – COMPOSITION OF PENSION PLAN ASSETS

	2009	2008
Equity securities	**50.3%**	49.4%
Debt securities	**45.1%**	50.1%
Cash and cash equivalents	**4.6%**	0.5%

The pension plan assets composition does not take into account the impact of the pension plans' derivatives and short securities held in the pension plans invested assets portfolio.

The following table shows the details of the expense for both the Company's pension plans and post retirement benefit plans.

TABLE 12.5 – COMPOSITION OF THE EXPENSE (REVENUE)

	Pension plans		Post retirement benefits	
	2009	2008	**2009**	2008
Current service cost	**17.9**	27.2	**–**	–
Interest cost on benefit obligation	**30.6**	29.4	**0.9**	0.8
Past service costs	**–**	–	**–**	–
Actual return on plan assets	**(99.2)**	113.4	**–**	–
Net actuarial (gains) losses	**80.3**	(133.7)	**(0.5)**	(0.4)
Accrued benefit expense before adjustments to recognize the long–term nature of employee future benefit costs	**29.6**	36.3	**0.4**	0.4
Excess of actual return over expected return on plan assets for the year	**66.6**	(153.6)	**–**	–
Net actuarial gains (losses) arising during the year (table 12.6)	**(80.3)**	133.7	**0.5**	0.4
Change in valuation allowance	**–**	(0.1)	**–**	–
Amortization of past service cost	**0.4**	0.4	**(0.5)**	(0.4)
Amortization of transitional (asset) obligation	**(10.5)**	(10.5)	**0.1**	0.1
Amortization of net actuarial losses	**5.8**	3.2	**0.2**	0.2
Amortization of valuation allowance	**(0.2)**	(0.3)	**–**	–
Settlement loss	**–**	3.3	**–**	–
Total	**11.4**	12.4	**0.7**	0.7

The following table shows the net actuarial gains and losses that arose during the year.

TABLE 12.6 – COMPONENTS OF NET ACTUARIAL GAINS OR LOSSES ARISING DURING THE YEAR

	Pension plans		Post retirement benefits	
	2009	2008	**2009**	2008
Actuarial gains (losses) arising from the:				
Change in the discount rate used to measure the benefit obligation	**(52.5)**	135.0	**(0.5)**	1.2
Experience	**(27.8)**	(1.3)	**1.0**	(0.8)
Total net actuarial gains (losses)	**(80.3)**	133.7	0.5	0.4

The following table summarizes the key weighted average assumptions used for the measurement of the benefit obligations and benefit expense (revenue).

TABLE 12.7 – ASSUMPTIONS

	Pension plans		Post retirement benefits	
	2009	2008	**2009**	2008
To determine benefit obligation at end of year				
Discount rate	**6.1%**	6.7%	**5.6%**	6.0%
Rate of increase in future compensation	**3.5%**	3.5%	**n/a**	n/a
Health care cost trend rate	**n/a**	n/a	**8.5%**	9.0%
Dental care cost trend rate	**n/a**	n/a	**4.5%**	4.5%
To determine benefit expense (revenue) for the year				
Discount rate	**6.7%**	5.2%	**6.0%**	5.2%
Rate of increase in future compensation	**3.5%**	3.5%	**n/a**	n/a
Expected long-term rate of return on plan assets	**7.0%**	7.0%	**n/a**	n/a
Health care cost trend rate	**n/a**	n/a	**9.0%**	10.0%
Dental care cost trend rate	**n/a**	n/a	**4.5%**	5.0%

The impact of a 1% increase or decrease in the health care and dental care cost trend rate would not be significant on the Company's results or financial position.

NOTE 13 – Debt outstanding

a) Medium term notes

During 2009, the Company completed two offerings (Series 1 and Series 2) of unsecured medium term notes (the "Notes"). The following table details the two offerings:

TABLE 13.1 – MEDIUM TERM NOTES OFFERINGS

	Medium term notes	
	Series 1	Series 2
Date issued	**August 31, 2009**	**November 23, 2009**
Maturity date	**September 3, 2019**	**November 23, 2039**
Principal amount outstanding	**$ 250.0**	**$ 150.0**
Carrying value	**$ 248.7**	**$ 149.0**
Fair value	**$ 252.8**	**$ 146.5**
Fixed annual rate	**5.41%**	**6.40%**
Semi-annual coupon payment due each year on:	**March 3, September 3**	**May 23, November 23**

The Notes may be redeemed at the option of the issuer, in whole or in part at any time, at a redemption price equal to the greater of (i) the Government of Canada Yield at the date of redemption plus a margin and (ii) par.

b) Credit facility

Effective December 1, 2009, the Company extended its unsecured committed credit facility of $150.0 (2008 – $150.0). This credit facility may be drawn as prime loans at the prime rate plus a margin or as bankers' acceptances at the bankers' acceptance rate plus a margin. As at December 31, 2009 the Company had not drawn down under the facility.

NOTE 14 – Share capital

a) Share capital authorized, issued and outstanding

The following table shows the Company's share capital, authorized, issued and outstanding.

TABLE 14.1 – AUTHORIZED, ISSUED AND OUTSTANDING

	As at December 31, 2009			As at December 31, 2008		
	Authorized (number of shares)	Issued and outstanding (number of shares)	Share capital	Authorized (number of shares)	Issued and outstanding (number of shares)	Share capital
Common shares	**Unlimited**	**119,906,567**	**$ 1,061.5**	Unlimited	119,906,566	$ 1,061.5
Class A	**Unlimited**	**–**	**–**	Unlimited	–	–
Special share	**–**	**–**	**–**	One	1	–

Issued and outstanding Class A Shares would rank both with regards to dividends and return on capital in priority to Common shares.

Common shares have no nominal or par value.

The special share was owned by ING Groep and was immediately converted into one common share and disposed of through the secondary offering. See note 1. The beneficial owner of the special share was entitled to nominate and elect a certain number of directors on the Board of Directors.

b) Normal course issuer bid

During 2008, the Company repurchased 4,566,195 common shares under its normal course issuer bid at an average price of $38.53 per share for a total consideration of $176.0. Total cost paid, including fees, was first charged to share capital to the extent of the average carrying value of the common shares purchased for cancellation and the excess of $135.6 was charged to retained earnings.

NOTE 15 – Stock-based compensation

a) Long-term incentive plan

The following table shows the outstanding units fair value for each of the Company's performance cycles.

TABLE 15.1 – OUTSTANDING UNITS AND FAIR VALUE BY PERFORMANCE CYCLE

As at December 31, 2009	Number of units	Per unit fair value at grant date (in $)	Amount
2007–2009 performance cycle	**–**	**44.27**	**–**
2008–2010 performance cycle	**5,600**	**32.76**	**0.2**
2009–2011 performance cycle	**157,460**	**23.06**	**3.6**
Total	**163,060**	**23.39**	**3.8**
As at December 31, 2008			
2006–2008 performance cycle	91,907	36.79	3.4
2007–2009 performance cycle	71,262	44.27	3.2
2008–2010 performance cycle	143,695	32.76	4.7
Total	306,864	36.64	11.3

The following table shows the movement in LTIP share units during the year.

TABLE 15.2 – UNITS ESTIMATE

	2009 units	2008 units
LTIP (share equivalents)		
Outstanding, beginning of year	306,864	616,115
Net change in estimate during the year	(143,804)	(309,251)
Outstanding, end of year	163,060	306,864
LTIP (restricted common shares)		
Outstanding, end of year	342,731	289,236

The amount charged to compensation expense was a reversal of $2.7 for the year ended December 31, 2009, (2008 – reversal of $0.4).

b) Employee share purchase plan

The following table shows the movement in ESPP restricted common shares during the year.

TABLE 15.3 – UNITS ESTIMATE

	2009 units	2008 units
ESPP (restricted common shares)		
Outstanding, beginning of year	**89,906**	66,228
Awarded during the year	**102,974**	87,144
Vested or forfeited during the year	**(84,334)**	(63,466)
Outstanding, end of year	**108,546**	89,906

The amount charged to compensation expense for the ESPP was $3.4 for the year ended December 31, 2009, (2008 – $3.0).

NOTE 16 – Additional information on the Consolidated statements of cash flows

The following table provides additional details on the items included in the cash from operating activities.

TABLE 16.1 – ADDITIONAL INFORMATION ON THE STATEMENT OF CASH FLOWS

	2009	2008
Adjustment for non-cash items:		
Change in unearned premiums, net	96.0	32.7
Net investment losses	172.5	288.0
Change in deferred acquisition costs, net	(13.5)	(2.3)
Future income taxes	23.5	24.3
Amortization of:		
Property and equipment	17.0	19.3
Intangible assets	24.8	18.8
Premiums net of discounts on fixed income securities	5.5	1.8
Increase (decrease) in loan provision	(1.9)	0.5
Interest on debt outstanding	5.6	–
Other	(14.2)	(4.8)
Total as reported on the Consolidated statement of cash flows	315.3	378.3
Changes in other operating assets and liabilities:		
Premium and other receivables	(172.6)	1.8
Income taxes	275.7	(77.7)
Other assets	(43.7)	7.0
Payables and other liabilities	(132.8)	56.3
Total as reported on the Consolidated statement of cash flows	(73.4)	(12.6)
Income taxes recovered	(152.8)	(70.4)
Composition of cash and cash equivalents as at December 31:		
Cash, net of bank overdrafts	(32.4)	27.3
Cash equivalents	92.5	483.1
Total	60.1	510.4

NOTE 17 – Acquisitions and divestitures

The following table shows the details of the business combinations that occurred during the year. The results of the acquired companies since their respective acquisition date are included in the Company's Consolidated statements of income.

The allocation of the net purchase price was established as follows:

TABLE 17.1 – ACQUISITIONS

	2009	2008
Purchase price	22.5	6.9
Fair value of net assets (liabilities) acquired	(6.3)	(0.3)
Excess of purchase price over fair value	28.8	7.2
Allocated to:		
Intangibles	11.0	4.4
Goodwill	17.8	2.8

The following divestitures occurred during the year:

TABLE 17.2 – DIVESTITURES

	2009	2008
Sales price	–	4.8
Book value of net assets sold	0.2	3.8
Gain (loss) on disposal	(0.2)	1.0

NOTE 18 – Contingencies, commitments and guarantees

In the normal course of operations, various claims and legal proceedings are instituted against the Company. Legal proceedings are often subject to numerous uncertainties and it is not possible to predict the outcome of individual cases. In management's opinion, the Company has made adequate provision for, or has adequate insurance to cover all claims and legal proceedings. Consequently, any settlements reached should not have a material adverse effect on the Company's consolidated future operating results and financial position.

The Company provides indemnification agreements to directors and officers, to the extent permitted by law, against certain claims made against them as a result of their services to the Company. The Company has insurance coverage for these agreements.

As part of certain long-term equity investments in affiliates the Company has sold equity put options to the principal equity owners. If exercised by the equity holders, the Company is obliged to acquire the equity ownership of these affiliates at a price established by the parties as representative of fair value.

The following table presents future minimum payments under long-term leases for premises and equipment.

TABLE 18.1 – FUTURE MINIMUM PAYMENTS UNDER LONG-TERM LEASE FOR PREMISES AND EQUIPMENT

Year	Premises	Equipment
2010	**44.2**	**18.5**
2011	**43.8**	**17.1**
2012	**43.3**	**15.6**
2013	**37.6**	**6.1**
2014	**33.2**	**2.2**
Thereafter	**100.0**	**0.1**
Total	**302.1**	**59.6**

NOTE 19 – Related-party transactions

Subsequent to the disposal by ING Groep of its shareholding in the Company (see note 1), all related-party transactions are with entities associated with the Company's distribution segment. These transactions consist mainly of commissions for brokerage services and interest revenue from loans.

a) Revenues and expenses with related parties

The following table shows the revenues and expenses that were incurred with related parties.

TABLE 19.1 – REVENUE AND EXPENSES WITH RELATED PARTIES

	Reported in:	2009	2008
Income			
Interest income	Interest income	**11.0**	7.4
Ceded premiums earned	Ceded premiums earned	**–**	14.8
Expenses			
Commissions	Commissions, premium taxes and general expenses	**42.0**	39.2
Ceded claims expenses	Claims	**–**	0.6
General expenses	Commissions, premium taxes and general expenses	**3.0**	8.2

b) Balance sheet amounts with related parties

The following table shows the amounts receivable from/payable to related parties.

TABLE 19.2 – BALANCE SHEET AMOUNTS WITH RELATED PARTIES

	Reported in:	2009	2008
Reinsurance (payable) receivable	Other receivables	**–**	(0.4)
Interest receivable	Accrued interest and dividend income	**0.5**	0.3
Loans	Loans	**224.1**	127.0

NOTE 20 – Segmented information

The Company has two reportable segments, the underwriting segment and the corporate and distribution segment.

The Company's core business activity is P&C insurance underwriting. The underwriting segment includes two lines of business: personal lines and commercial lines. Personal lines include automobile and property while commercial lines include automobile and property and liability.

The corporate and distribution segment includes primarily the results of the Company's broker operations.

a) Results of the Company's reportable segments

The following table splits the Company's results by reportable segment.

TABLE 20.1 – RESULTS OF THE COMPANY'S REPORTABLE SEGMENTS

	Underwriting	Corporate and distribution	Inter-segment eliminations	Total
As at December 31, 2009				
Revenues	**4,055.4**	**129.1**	**(80.1)**	**4,104.4**
Expenses	**4,043.0**	**112.1**	**(75.9)**	**4,079.2**
Subtotal	**12.4**	**17.0**	**(4.2)**	**25.2**
Interest and dividend income, net of expenses				**292.7**
Interest on debt outstanding				**(5.6)**
Net investment losses				**(172.5)**
Total income before income taxes				**139.8**
As at December 31, 2008				
Revenues	4,039.4	109.9	(74.6)	4,074.7
Expenses	3,972.4	94.0	(74.6)	3,991.8
Subtotal	67.0	15.9	–	82.9
Interest and dividend income, net of expenses				328.7
Interest on debt outstanding				–
Net investment losses				(288.0)
Total income before income taxes				123.6

b) Company's assets by reportable segment

The following table splits the Company's assets by reportable segment.

TABLE 20.2 – ASSETS OF THE COMPANY'S REPORTABLE SEGMENTS

	Underwriting	Corporate and distribution	Inter-segment eliminations	Total
As at December 31, 2009				
Invested assets	**7,815.6**	**184.8**	**(3.9)**	**7,996.5**
Other assets	**2,823.7**	**202.5**	**(9.6)**	**3,016.6**
Intangibles	**107.4**	**52.2**	**–**	**159.6**
Goodwill	**74.4**	**104.2**	**–**	**178.6**
Total assets	**10,821.1**	**543.7**	**(13.5)**	**11,351.3**
As at December 31, 2008				
Invested assets	6,044.4	49.9	–	6,094.3
Other	3,214.3	186.5	(7.1)	3,393.7
Intangibles	86.9	49.5	–	136.4
Goodwill	74.4	86.4	–	160.8
Total assets	9,420.0	372.3	(7.1)	9,785.2

C) Results by line of business

TABLE 20.3 – RESULTS BY LINE OF BUSINESS

	2009	2008
Direct premiums written		
Personal	3,107.4	3,034.5
Commercial	1,154.3	1,136.0
Total	4,261.7	4,170.5
Underwriting income (loss)		
Personal	(5.5)	(68.4)
Commercial	17.9	135.4
Total	12.4	67.0

NOTE 21 – Disclosures on rate regulation

The Company's insurance subsidiaries are licensed under insurance legislation in each of the provinces and territories in which they conduct business. Automobile insurance is a compulsory product and is subject to different regulations across the provinces and territories in Canada, including those with respect to rate setting. Rate setting mechanisms generally fall under three categories:

Category	Description
File and use	Insurers file their rates with the relevant authorities and wait for a prescribed period of time and then implement the proposed rates.
File and approve	Insurers must wait for specific approval of filed rates before they may be used.
Use and file	Rates are filed following use.

Table 21.1 lists the provincial authorities which regulate automobile insurance rates. Automobile direct written premiums in these provinces totalled $2,413.1 in 2009 (2008 – $2,375.8) and represented approximately 99.1% (2008 – 99.0%) of direct automobile premiums written.

TABLE 21.1 – PROVINCIAL AUTHORITIES AND RATE FILINGS

Province	Rate filing	Regulatory authority
Alberta	File and approve or file and use	Alberta Automobile Insurance Rate Board
Ontario	File and approve	Financial Services Commission of Ontario
Quebec	Use and file	L'Autorité des marchés financiers
Nova Scotia	File and approve	Nova Scotia Utility and Review Board
New Brunswick	File and approve	New Brunswick Insurance Board
Prince Edward Island	File and approve	Island Regulatory Appeals Commission
Newfoundland	File and approve	Board of Commissioners of Public Utilities

Relevant regulatory authorities may, in some circumstances, require retroactive rate adjustments, which could result in a regulatory asset or liability. At December 31, 2009 and 2008, the Company had no significant regulatory asset or liability.

Five-year financial history (for annual review)

(in millions of Canadian dollars, except as noted)

	2009	2008	2007	2006	2005
Consolidated performance					
Written insured risks (thousands)	**4,603.6**	4,601.5	4,679.9	4,565.1	4,417.9
Direct written premiums (excluding pools)	**4,274.9**	4,145.5	4,108.6	3,993.6	3,905.9
Net premiums earned	**4,055.4**	4,039.4	3,932.0	3,826.6	3,840.2
Prior year claims reserve development (favourable)	**(94.4)**	(113.9)	(115.9)	(169.9)	(277.6)
Net underwriting income (excluding MYA)	**54.0**	117.0	189.1	403.8	537.7
Combined ratio (excluding MYA)	**98.7%**	97.1%	95.2%	89.4%	86.0%
Interest and dividend income, net of expenses	**292.7**	328.8	344.8	321.3	307.5
Net gains (losses) on invested assets and other gains	**(172.5)**	(288.0)	73.6	193.5	223.5
Corporate and distribution income	**7.2**	15.6	44.3	33.4	22.3
Income before income taxes	**139.8**	123.6	671.6	952.0	1091.0
Effective tax rate %	**9.4%**	(3.8%)	24.3%	30.9%	28.3%
Net operating income (excluding MYA)	**281.6**	360.7	457.0	530.5	612.3
Net income	**126.7**	128.2	508.3	658.1	781.8
Earnings per share (dollars)	**1.06**	1.05	4.01	4.92	5.85
Average number of shares outstanding	**119.9**	122.0	126.7	133.7	133.5
Return on equity %	**4.5%**	4.4%	15.4%	20.8%	31.6%
Personal lines – total					
Written insured risks (thousands)	**4,097.9**	4,103.7	4,190.5	4,077.6	3,927.4
Direct written premiums (excluding pools)	**3,120.8**	3,009.9	2,962.1	2,810.7	2,657.1
Net premiums earned	**2,992.9**	2,958.8	2,845.0	2,696.7	2,680.7
Combined ratio (excluding MYA)	**99.3%**	101.2%	96.7%	91.0%	85.7%
Net underwriting income (excluding MYA)	**21.3**	(36.0)	92.7	242.2	382.1
Personal auto					
Written insured risks (thousands)	**2,454.7**	2,449.3	2,514.4	2,440.1	2,336.0
Direct written premiums (excluding pools)	**2,126.6**	2,057.0	2,057.7	1,969.2	1,877.2
Net premiums earned	**2,066.5**	2,067.5	2,008.0	1,911.2	1,946.9
Combined ratio (excluding MYA)	**94.9%**	95.9%	94.5%	87.3%	78.8%
Net underwriting income (excluding MYA)	**105.0**	84.7	111.4	242.5	411.5
Personal property					
Written insured risks (thousands)	**1,643.2**	1,654.4	1,676.1	1,637.4	1,591.5
Direct written premiums (excluding pools)	**994.2**	952.9	904.4	841.5	779.9
Net premiums earned	**926.4**	891.3	837.0	785.5	733.8
Combined ratio (excluding MYA)	**109.0%**	113.6%	102.2%	100.0%	104.0%
Net underwriting income (excluding MYA)	**(83.7)**	(120.7)	(18.7)	(0.3)	(29.4)
Commercial lines – total					
Written insured risks (thousands)	**505.8**	497.8	489.3	487.5	490.6
Direct written premiums (excluding pools)	**1,154.1**	1,135.6	1,146.5	1,182.9	1,248.9
Net premiums earned	**1,062.5**	1,080.7	1,087.1	1,129.9	1,159.5
Combined ratio (excluding MYA)	**96.9%**	85.9%	91.1%	85.7%	86.6%
Net underwriting income (excluding MYA)	**32.7**	153.0	96.2	161.7	155.6
Commercial auto					
Written insured risks (thousands)	**269.4**	263.8	255.8	253.6	254.4
Direct written premiums (excluding pools)	**321.9**	317.8	321.2	327.5	331.2
Net premiums earned	**315.2**	318.9	320.2	326.8	334.4
Combined ratio (excluding MYA)	**79.8%**	87.2%	93.7%	86.9%	87.0%
Net underwriting income (excluding MYA)	**63.6**	40.8	20.1	43.0	43.6
Commercial P&C					
Written insured risks (thousands)	**236.4**	234.0	233.5	233.9	236.4
Direct written premiums (excluding pools)	**832.2**	817.8	825.3	855.4	917.6
Net premiums earned	**747.3**	761.8	766.9	803.1	825.1
Combined ratio (excluding MYA)	**104.1%**	85.3%	90.1%	85.2%	86.4%
Net underwriting income (excluding MYA)	**(30.9)**	112.2	76.2	118.7	112.0
Financial condition					
Excess capital in P&C companies (over 170% MCT)	**728.4**	357.5	214.1	463.7	500.0
MCT %	**231.9%**	205.0%	187.9%	210.0%	215.8%
Cash generated from operations	**538.0**	619.7	620.3	431.0	637.4
Debt to total capital	**11.8%**	0%	0%	0%	4.2%
Book value per share (dollars)	**24.88**	21.96	25.48	25.58	21.63
Invested assets					
Performance					
Market-based investment yield	**4.5%**	5.0%	5.1%	4.8%	4.7%
Portfolio mix					
Total invested assets and cash	**8,056.6**	6,604.7	7,245.9	7,367.8	7,062.1
Cash and short-term investments	**3.3%**	12.1%	0.4%	11.4%	11.1%
Fixed income securities	**56.8%**	53.6%	53.4%	44.2%	49.9%
Common shares	**16.3%**	12.1%	23.6%	21.5%	17.9%
Preferred shares	**19.6%**	18.5%	19.7%	19.8%	17.8%
Other	**4.0%**	3.7%	2.9%	3.1%	3.3%

Two-year quarterly review

(in millions of Canadian dollars, except as noted)

	2009				2008			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Consolidated performance								
Written insured risks (thousands)	1,046.0	1,244.4	1,376.0	937.2	1,034.3	1,240.7	1,380.6	945.8
Direct written premiums (excluding pools)	1,011.4	1,144.1	1,250.6	868.8	968.2	1,100.3	1,216.7	860.3
Net premiums earned	1,036.5	1,019.0	1,011.3	988.7	1,019.2	1,032.3	996.1	991.8
Prior year claims reserve development (favourable)	(78.8)	25.1	(17.0)	(23.7)	(19.3)	(62.7)	(70.3)	38.4
Net underwriting income (excluding MYA)	56.0	(53.2)	43.2	7.9	11.0	61.9	43.4	0.7
Combined ratio (excluding MYA)	94.6%	105.2%	95.7%	99.2%	98.9%	94.0%	95.6%	99.9%
Interest and dividend income, net of expenses	77.3	72.9	72.6	72.5	78.3	83.1	81.7	85.6
Net gains (losses) on invested assets and other gains	(13.3)	11.7	(35.1)	(135.8)	(152.2)	(81.3)	(28.7)	(25.8)
Corporate and distribution income	(7.5)	3.6	6.7	1.8	2.0	(2.1)	12.8	3.1
Income before income taxes	125.4	(16.0)	97.2	(66.9)	(108.2)	68.7	140.8	22.2
Effective tax rate %	22.9%	(50.0%)	23.7%	(45.8%)	40.7%	16.7%	20.5%	(3.8%)
Net operating income (excluding MYA)	98.1	21.6	92.9	69.1	75.1	106.3	109.3	70.2
Net income	96.7	(8.0)	74.2	(36.3)	(64.1)	57.3	112.0	23.0
Earnings per share (dollars)	0.81	(0.07)	0.62	(0.30)	(0.53)	0.47	0.91	0.19
Average number of shares outstanding	119.9	119.9	119.9	119.9	119.9	120.8	122.8	124.4
Return on equity %	4.5%	(1.2%)	1.1%	2.4%	4.4%	9.5%	10.3%	13.0%
Personal lines – total								
Written insured risks (thousands)	920.5	1,125.3	1,225.8	826.2	914.3	1,123.6	1,230.6	835.2
Direct written premiums (excluding pools)	714.3	871.3	921.8	613.4	679.1	835.1	891.2	604.5
Net premiums earned	771.2	748.4	745.8	727.4	748.5	758.0	728.1	724.2
Combined ratio (excluding MYA)	94.9%	106.2%	95.3%	101.0%	106.3%	97.2%	98.7%	102.8%
Net underwriting income (excluding MYA)	39.7	(46.3)	35.4	(7.3)	(46.9)	21.4	9.4	(19.9)
Personal auto								
Written insured risks (thousands)	535.1	663.5	751.2	504.9	528.7	659.0	751.8	509.8
Direct written premiums (excluding pools)	474.6	589.8	635.2	426.9	452.5	564.4	615.1	425.0
Net premiums earned	531.0	517.3	516.2	502.0	520.6	531.2	509.2	506.5
Combined ratio (excluding MYA)	98.0%	95.9%	89.6%	96.1%	102.9%	90.8%	89.2%	100.9%
Net underwriting income (excluding MYA)	10.4	21.4	53.6	19.6	(14.9)	49.0	55.1	(4.6)
Personal property								
Written insured risks (thousands)	385.4	461.8	474.6	321.3	385.6	464.6	478.8	325.4
Direct written premiums (excluding pools)	239.7	281.5	286.6	186.5	226.6	270.7	276.1	179.5
Net premiums earned	240.2	231.1	229.6	225.4	227.9	226.8	218.9	217.7
Combined ratio (excluding MYA)	87.8%	129.3%	107.9%	112.0%	114.0%	112.2%	120.9%	107.0%
Net underwriting income (excluding MYA)	29.3	(67.7)	(18.2)	(26.9)	(32.0)	(27.6)	(45.7)	(15.3)
Commercial lines – total								
Written insured risks (thousands)	125.6	119.1	150.2	110.9	120.0	117.2	150.1	110.6
Direct written premiums (excluding pools)	297.0	272.8	328.8	255.4	289.2	265.2	325.5	255.8
Net premiums earned	265.2	270.6	265.4	261.1	270.8	274.3	268.0	267.6
Combined ratio (excluding MYA)	93.8%	102.6%	97.0%	94.1%	78.7%	85.3%	87.3%	92.3%
Net underwriting income (excluding MYA)	16.4	(7.0)	8.0	15.4	57.8	40.4	34.1	20.6
Commercial auto								
Written insured risks (thousands)	66.5	61.2	83.8	57.9	63.0	60.5	83.0	57.3
Direct written premiums (excluding pools)	80.4	73.6	97.2	70.7	77.2	72.8	97.8	70.1
Net premiums earned	80.4	79.5	78.0	77.2	80.1	80.8	79.3	78.7
Combined ratio (excluding MYA)	70.4%	87.1%	73.9%	88.1%	91.6%	77.9%	86.9%	92.7%
Net underwriting income (excluding MYA)	23.8	10.2	20.4	9.2	6.7	17.9	10.5	5.7
Commercial P&C								
Written insured risks (thousands)	59.1	57.9	66.4	53.0	57.0	56.7	67.1	53.3
Direct written premiums (excluding pools)	216.6	199.2	231.6	184.7	211.9	192.4	227.7	185.7
Net premiums earned	184.8	191.1	187.4	183.9	190.7	193.5	188.7	188.9
Combined ratio (excluding MYA)	104.0%	109.0%	106.7%	96.6%	73.2%	88.4%	87.5%	92.1%
Net underwriting income (excluding MYA)	(7.4)	(17.2)	(12.4)	6.2	51.0	22.6	23.7	14.9
Financial condition								
Excess capital in P&C companies (over 170% MCT)	728.4	580.9	444.1	385.4	357.5	339.0	328.4	238.5
MCT %	231.9%	219.2%	211.1%	208.2%	205.0%	199.9%	197.8%	190.2%
Cash generated from operations	77.3	215.7	228.0	17.0	230.5	191.0	240.5	(42.3)
Debt to total capital	11.8%	8.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Book value per share (dollars)	24.88	24.13	23.36	21.56	21.96	24.15	25.19	25.19
Invested assets								
Performance								
Market-based investment yield	4.4%	4.4%	4.4%	4.7%	5.1%	4.9%	4.9%	5.1%
Portfolio mix								
Total invested assets and cash	8,056.6	7,839.9	6,992.4	6,495.9	6,604.7	6,884.5	7,077.9	7,077.5
Cash and short-term investments	3.3%	5.5%	12.8%	11.8%	12.1%	3.9%	0.9%	0.0%
Fixed income securities	56.8%	53.9%	49.5%	53.5%	53.6%	50.9%	49.8%	52.2%
Common shares	16.3%	16.0%	12.6%	11.2%	12.1%	19.9%	24.6%	24.3%
Preferred shares	19.6%	20.6%	20.9%	19.1%	18.5%	22.0%	21.7%	20.7%
Other	4.0%	4.0%	4.2%	4.4%	3.7%	3.3%	3.0%	2.8%

Asset-backed security A financial security whose value and income payments are derived from and collateralized (or "backed") by a specified pool of underlying assets such as auto loans and credit card receivables.

Actuarial gains (losses) Effect of changes in actuarial assumptions and experience adjustments (the effects of differences between the previous actuarial assumptions and what has actually occurred).

Basis risk Basis risk is the risk that offsetting investments in a hedging strategy will not experience price changes in entirely opposite directions from each other.

Book value per share Represents shareholders' equity at the end of the period divided by the number of outstanding common shares on the same date. Shareholders' equity is determined in accordance with GAAP.

Case reserves The liability established to reflect the estimated cost of unpaid claims that have been reported and claims expenses that the insurer will ultimately be required to pay.

Catastrophe A catastrophe is defined as a single event resulting in $5.0 million or more in aggregate claims.

Claims expenses The direct and indirect expenses of settling claims.

Claims ratio Claims incurred, net of reinsurance, during a defined period and expressed as a percentage of net premiums earned for the same period.

Claims liabilities Claims liabilities are technical accounting provisions comprised of three main elements: 1) case reserves 2) claims that are incurred but not reported (IBNR) and 3) provision for adverse development as required by accepted actuarial practice in Canada. Claims liabilities are discounted to take into account the time value of money.

Combined ratio The sum of the claims ratio and the expenses ratio. A combined ratio below 100% indicates profitable underwriting results. A combined ratio over 100% indicates unprofitable results.

Corporate sustainability Corporate sustainability represents the way a company achieves enhanced ethical standards and a balance of economic, environmental and social imperatives addressing the concerns and expectations of its stakeholders.

Corridor method or approach Systematic method for recognizing into the statement of income the net cumulative unrecognized actuarial gains and losses. Under this method, the portion of actuarial gains and losses to be recognized for a specific pension plan is the excess of the greater of: (a) 10% of the present value of the defined benefit obligation and (b) 10% of the fair value of the plan assets, both established at the same date, divided by the expected average remaining working lives of the employees participating to the plan.

Collateral Assets pledged as security for a loan or other obligation. Collateral can take many forms, such as cash, highly rated securities, receivables, etc.

Counterparty A counterparty is any person or entity from which cash or other forms of consideration are expected to extinguish a liability or obligation of the company.

Credit derivatives Credit derivatives, such as credit default swaps, are over-the-counter contracts that transfer credit risk related to an underlying financial instrument (referenced asset) from one counterparty to another.

Credit risk Credit risk is the possibility that one counterparty may not be able to meet payment obligations when they become due.

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.

Derivative A contract between two parties, which requires little or no initial investment and where payments between the parties are dependent upon the movements in price of an underlying instrument, index or financial rate. The notional amount of the derivative is the contract amount used as a reference point to calculate the payments to be exchanged between the two parties, and the notional amount itself is generally not exchanged by the parties.

Derivative-related credit risk Credit risk from derivative transactions is generated by the potential for the counterparty to default on its contractual obligations when one or more transactions have a positive market value to the company. Therefore, derivative-related credit risk is represented by the positive fair value of the instrument and is normally a small fraction of the contract's notional amount.

Direct premiums written The total amount of premiums for new and renewal policies billed (written) during a specific reporting period from the primary insured.

Earnings per share (EPS), basic Calculated as net income less preferred share dividends divided by the average number of shares outstanding.

Earnings per share (EPS), diluted Calculated as net income less preferred share dividends divided by the average number of shares outstanding adjusted for the dilutive effects of stock options and other convertible securities.

Equity price risk Equity price risk is the risk of losses arising from movements in equity market prices.

Excess capital Excess capital in the P&C insurance subsidiaries at 170% minimum capital test ("MCT") plus excess liquid assets in the holding company and other subsidiaries.

Expense ratio Underwriting expenses including commissions, premium taxes and all general and administrative expenses, incurred in underwriting income during a defined period and expressed as a percentage of net premiums earned for the same period.

Facility Association The Facility Association is an entity 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 private insurance market. The Facility Association serves the following provinces and territories: Alberta, New Brunswick, Newfoundland and Labrador, Northwest Territories, Nova Scotia, Nunavut, Ontario, Prince Edward Island and Yukon.

Fair value The amount of consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act.

Forwards derivatives Forward contracts are effectively tailor-made agreements that are transacted between counterparties in the over-the-counter market.

Futures derivatives Futures contracts are standardized contracts with respect to amounts and settlement dates, and are traded on regular future exchanges.

Interest rate forwards and futures contracts Contractual obligations to buy or sell an interest-rate sensitive financial instrument at a predetermined future date at a specified price.

Currency forwards and futures contracts Contractual obligations to exchange one currency for another at a specified price for settlement at a predetermined future date.

Frequency (of claims) Total number of claims reported in a specific period.

Hedge A risk management technique used to insulate financial results from market, interest rate or foreign currency exchange risk (exposure) arising from normal investing operations. The elimination or reduction of such exposure is accomplished by establishing offsetting or 'hedging' positions.

IFRS International Financial Reporting Standards (IFRS) as published by the International Accounting Standards Board (IASB). The term 'IFRS' includes IFRS standards and Interpretations developed by the International Financial Reporting Interpretations Committee (IFRIC) or its predecessor, the former Standing Interpretations Committee (SIC).

Incurred but not reported (IBNR) claims reserve Reserves (accounting provisions) for estimated claims that have been incurred but not yet reported by policyholders including a reserve for future developments on claims which have been reported.

Industry pools Industry pools consist of the "residual market" as well as risk-sharing pools ("RSP") in Alberta, Ontario, Quebec, New Brunswick and Nova Scotia. These pools are managed by the Facility Association except for the Quebec RSP.

Invested assets or investment portfolio Financial instrument assets owned by the company including debt and equity securities and loans.

Interest rate risk Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

Liquidity risk Liquidity risk is the risk that an entity will encounter difficulty in raising funds to meet obligations associated with financial liabilities.

Market-based yield The market-based yield is a non-GAAP measure defined as the annualized total pre-tax dividend and interest income (before expenses) divided by the average fair values of equity and fixed income securities held during the reporting period.

Market yield adjustment ("MYA") The impact of changes in the discount rate used to discount claims liabilities based on the change in the market based yield of the underlying assets.

Market yield effect The difference between the MYA and the gains and losses on "held-for-trading" debt securities (the objective is that these two items offset each other with a minimal overall impact to net income).

Master netting agreement An agreement between the company and a counterparty designed to reduce the credit risk of derivative transactions through the creation of a legal right to offset the exposure in the event of a default.

Minimum capital test ("MCT") Ratio of available capital to required capital. Federally regulated property and casualty insurers, including our Canadian insurance subsidiaries, must meet a minimum capital test ("MCT") that assesses the insurer's available capital in relation to its required capital and requires that available capital equal at least the minimum capital requirement. OSFI expects insurers to establish a target capital level above the minimum requirement, and maintain ongoing capital, at no less than the supervisory target of 150% of required capital under MCT. The company has an internal operating target of 170%.

Net operating income After-tax net income from underwriting activities (excluding MYA), corporate and distribution activities and interest and dividend income from invested assets.

Net premiums earned Premiums written that are recognized for accounting purposes as revenue earned during a period.

Net premiums written Direct premiums written for a given period less premiums ceded to reinsurers and retrocessionaires during such period.

Net underwriting income Net premiums earned less net claims incurred, commissions, premium taxes and general expenses (excluding MYA).

Normal course issuer bid A program for the repurchase of the company's own common shares, for cancellation through a stock exchange, that is subject to the various rules of the relevant stock exchange and securities commission.

Notional amount The contract amount used as a reference point to calculate cash payments for derivatives.

Office of the Superintendent of Financial Institution of Canada (OSFI) The primary regulator of federally chartered financial institutions and federally administered pension plans in Canada. OSFI's mission is to safeguard policyholders, depositors and pension plan members from undue loss.

Operating return on equity Net operating income for the last 12-months divided by the average shareholders' equity (excluding accumulated other comprehensive income) over the same 12-month period. The average shareholders' equity is the mean of shareholders' equity at the beginning and the end of the period.

Options Contractual agreements under which the seller (writer) grants the purchaser the right, but not the obligation, either to buy (call option) or sell (put option) an asset (underlying asset) at a predetermined price, at or by a specified future date.

Prior year claims development Prior year claims development is the change in total prior year claims liabilities in a given period. A reduction to claims liabilities is called favourable prior year claims development. An increase in claims liabilities is called unfavourable prior year claims development.

Provision for adverse deviation An amount added to undiscounted case reserves and IBNR to account for adverse deviation from claims reserve estimates.

Reinsurer An insurance company that agreed to indemnify another insurance or reinsurance company, the ceding company, against all or a portion of the insurance or reinsurance risks underwritten by the ceding company, under one or more policies.

Return on equity (ROE) Net income for a 12-month period divided by the average shareholders' equity over the same 12-month period. Net income and shareholders' equity are determined in accordance with GAAP. The average shareholders' equity is the mean of shareholders' equity at the beginning and end of the period.

Risk Financial institutions, including insurance companies, face a number of different risks that expose them to possible losses including market risk, interest rate risk, currency risk, basis risk, credit risk, liquidity risk, insurance related risk, operational risk, strategy implementation risk, regulation and legal risk, solvency risk, reputation risk and other risks.

Securities lending Transactions in which the owner of a security agrees to lend it under the terms of a prearranged contract to a borrower for a fee. The borrower must collateralize the security loan at all times.

Securities sold short A transaction in which the seller sells securities and then borrows the securities in order to deliver them to the purchaser upon settlement. At a later date, the seller buys identical securities in the market to replace the borrowed securities.

Severity (of claims) Average cost of a claim calculated by dividing the total cost of claims by the total number of claims.

Shareholders' equity Capital invested by the shareholders via share capital and contributed surplus, plus retained earnings and accumulated other comprehensive income (loss).

Structured settlements Periodic payments to an injured person or survivor for a determined number of years of for life, typically in settlement for a claim under a liability policy, usually funded through the purchase of an annuity.

Swaps, including currency and total return swaps Over-the-counter contracts in which two counterparties exchange a series of cash flows based on agreed upon rates such as exchange rates or value of an equity index applied to a contract notional amount.

Written insured risks The number of vehicles in automobile insurance, the number of premises in personal property insurance and the number of policies in commercial insurance (excluding commercial auto insurance).

Board of Directors

Charles Brindamour [4]
President and Chief Executive Officer

Yves Brouillette [1,2]
Corporate Director and President, Placements Beluca Inc.

Paul Cantor [3,4]
Director and Chair, Public Sector Pension Investment Board
and Senior Advisor, Bennett Jones LLP

Marcel Côté [2,3]
Partner, Secor Consulting Inc.

Robert W. Crispin [1,4]
Corporate Director

Claude Dussault
Chairman of the Board

Ivan E.H. Duvar [2,3]
President and Chief Executive Officer, MIJAC Inc.

Eileen Mercier [1,4]
Chair and Board Member, Ontario Teachers' Pension Plan

Robert Normand [1,4]
Corporate Director

Louise Roy [2,3]
Chancellor, Université de Montréal and Associate Fellow,
Center for Interuniversity Research and Analysis on Organizations

Stephen Snyder [1,2]
President and CEO of TransAlta Corporation

Carol Stephenson [2,3]
Dean, Richard Ivey School of Business, University of Western Ontario

Notes:
(1) Denotes member of the Audit & Risk Review Committee
(2) Denotes member of the Conduct Review & Corporate Governance Committee
(3) Denotes member of the Human Resources Committee
(4) Denotes member of the Investment Committee

For complete biographies of the members of the Board of Directors, please see the Annual Information form which may be found online at www.sedar.com.

Executive management

Charles Brindamour
President and Chief Executive Officer

Martin Beaulieu
Senior Vice-President, Personal Lines

Susan Black
Chief Human Resources Officer

Alan Blair
Senior Vice-President, Atlantic Canada

Debbie Coull-Cicchini
Senior Vice-President, Ontario

Claude Désilets
Chief Risk Officer

Louis Gagnon
President, Intact Insurance

Denis Garneau
Senior Vice-President, Quebec

Françoise Guénette
Senior Vice-President, Corporate and Legal Services and Secretary

Denis Guertin
President, Direct to Consumers Distribution

Byron Hindle
Senior Vice-President, Commercial Lines

Derek Iles
Senior Vice-President, Western Canada and
Vice Chair of the Operations Committee

David Lincoln
Senior Vice-President, Corporate Audit Services

Jack Ott
Senior Vice-President and Chief Information Officer

Marc Pontbriand
Executive Vice-President, Claims and IT

Marc Provost
Senior Vice-President, Managing Director and
Chief Investment Officer, Intact Investment Management Inc.

Mark Tullis
Chief Financial Officer

Pete Weightman
President, Canada Brokerlink

For complete biographies of the executive management, please see the corporate governance section of the www.intactfc.com web site.

DESIGN: BRYAN MILLS IRADESSO WWW.BMIR.COM

Credit rating

IFC's long-term issuer rating with Moody's Investors Services is A3 and the Company's five principal operating insurance subsidiaries are rated Aa3 for insurance financial strength (IFS). IFC's primary insurance subsidiaries are rated A+ by A.M. Best for financial strength rating (FSR), and the Company's senior unsecured debt is rated A (low) by DBRS.

Toronto Stock Exchange (TSX) listing

Ticker symbol: IFC

Annual Meeting of Shareholders

Date: Wednesday May 5, 2010
Time: 2:00 pm ET
Palais des congrès de Montréal
1001, Place Jean-Paul-Riopelle
Montreal, Quebec H2Z 1H2

Version française

Il existe une version française du présent rapport annuel à la section Relations investisseurs de notre site Web intactcf.com. Les intéressés peuvent obtenir une version imprimée en appelant au 1 866 778 0774 ou en envoyant un courriel à ir@intact.net.

Transfer agent and registrar

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Auditors

Ernst & Young LLP

Investor Relations

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Vice-President, Finance and Treasurer
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Media inquiries

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Director, External Communications
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Dividend reinvestment

Shareholders can reinvest their cash dividends in common shares of Intact Financial Corporation on a commission-free basis either through a broker, subject to eligibility as determined by the broker, or through Canadian ShareOwner Investments Inc. Full details can be obtained by visiting the Investor Relations section of the www.intactfc.com web site.

Eligible dividend designation

For purposes of the enhanced dividend tax credit rules contained in the Income Tax Act (Canada) and any corresponding provincial and territorial tax legislation, all dividends (and deemed dividends) paid by Intact Financial Corporation to Canadian residents on our common shares after December 31, 2005, are designated as eligible dividends. Unless stated otherwise, all dividends (and deemed dividends) paid by the Company hereafter are designated as eligible dividends for the purposes of such rules.

Information for shareholders outside of Canada

Dividends paid to residents in countries with which Canada has bilateral tax treaties are generally subject to the 15% Canadian non-resident withholding tax. There is no Canadian tax on gains from the sale of shares (assuming ownership of less than 25%) or debt instruments of the Company owned by non-residents not carrying on business in Canada. No government in Canada levies estate taxes or succession duties.

Common share prices and volume

	High	Low	Close	Volume
Q1	$ 37.50	$ 26.17	$ 36.00	54,684,783
Q2	$ 37.63	$ 32.67	$ 34.05	24,407,951
Q3	$ 36.37	$ 31.28	$ 33.98	19,054,203
Q4	$ 37.82	$ 32.37	$ 37.15	16,313,412
Year 2009	**$ 37.82**	**$ 26.17**	**$ 37.15**	**114,460,349**
Q1	$ 41.51	$ 33.03	$ 36.49	13,873,578
Q2	$ 41.50	$ 34.24	$ 35.55	8,786,544
Q3	$ 43.04	$ 35.05	$ 35.96	9,970,713
Q4	$ 40.00	$ 26.03	$ 31.61	10,433,907
Year 2008	$ 43.04	$ 26.03	$ 31.61	43,064,742

Source: Toronto Stock Exchange

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