HERE FOR YOU

FINANCIAL STATEMENTS

For the year ended December 31, 2015

La Mutuelle des municipalités du Québec

MANAGEMENT'S RESPONSIBILITY WITH RESPECT TO THE PRESENTATION OF FINANCIAL INFORMATION

La Mutuelle des municipalités du Québec (MMQ) management is responsible for the preparation and accurate presentation of its financial statements in accordance with International Financial Reporting Standards (IFRS).

In order to provide the most reliable and pertinent financial information, the MMQ maintains rigorous internal accounting and administrative control systems.

For its part, the Audit and Investments Committee examines the MMQ's financial statements before they are presented to the Board of Directors. The Committee also reviews control and financial risk management mechanisms, and it assures the effectiveness and respect of operational control measures. In addition, the Committee oversees the organization's investment strategies and ensures that proper accounting and actuarial practices are adhered to in prudent fashion.

The MMQ's financial statements have been audited on behalf of Mutual Members by the external audit firm KPMG LLP in accordance with Canadian generally accepted auditing standards. Subsequent to a call for tenders, this firm was recommended by the Board of Directors and selected for the period spanning fiscal 2014 to 2018 inclusively during the Annual General Meeting of Mutual Members held in May 2014.

Policy and claims liabilities were certified by the appointed actuary, Mr. Jean-Pierre Paquet, FCIA, FCAS, of the firm Willis Towers Watson in accordance with Canadian accepted actuarial practices. Mr. Paquet was designated for the period spanning fiscal 2014 to 2017 inclusively by the MMQ's Board of Directors at their meeting in September 2014 subsequent to a call for tenders.

The designated external auditors and appointed actuary had free access to the Audit and Investments Committee. Upon completion of their audit, they presented the conclusions of their analysis to the members of the Committee.

After examination of the auditors' report, the Audit and Investments Committee recommended approval of the financial statements by the Board of Directors, which approved them at their meeting held on February 24, 2016.

The audited financial statements and related reports were then filed with the *Autorité des marchés financiers* (AMF).

LINDA DAOUST
PRESIDENT AND CHIEF EXECUTIVE OFFICER

FRANÇOIS DUFAULT
CHIEF FINANCIAL OFFICER

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INDEPENDENT AUDITORS' REPORT

To Mutual Members of *La Mutuelle des municipalités du Québec*

We have audited the accompanying financial statements of *La Mutuelle des municipalités du Québec*, which comprise the statement of financial position as at December 31, 2015, the statements of comprehensive income, surplus and Mutual Member's shares and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of *La Mutuelle des municipalités du Québec* as at December 31, 2015, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

KPMG LLP (signed)*

February 24, 2016
Montréal, Canada

* FCPA auditor, FCA Public accountancy permit No. A110618

ACTUARY'S CERTIFICATE

I have valued the policy liabilities and reinsurance recoverables of *La Mutuelle des municipalités du Québec* for its statement of financial position at December 31, 2015 and their changes in the statement of income for the year then ended in accordance with accepted actuarial practice in Canada, including selection of appropriate assumptions and methods.

I am satisfied that the data utilized for the valuation of these liabilities are reliable and sufficient. I verified the consistency of the valuation data with the insurer's financial records.

In my opinion, the amount of policy liabilities net of reinsurance recoverables makes appropriate provision for all policy obligations and the financial statements fairly present the result of the valuation.

Jean-Pierre Paquet, FCIA, FCAS (signed)
Willis Towers Watson

February 9, 2016

STATEMENT OF COMPREHENSIVE INCOME

For the year ended December 31, 2015, with comparative information for 2014

	2015	2014
	$	$
REVENUES		
Written premiums		
Gross premiums	38,137,132	36,175,018
Ceded premiums	(6,283,894)	(5,802,202)
Net premiums (Note 10)	31,853,238	30,372,816
Net change in unearned premiums	(1,184,238)	(1,752,601)
Net earned premiums (Note 10)	30,669,000	28,620,215
Investment income (Note 12)	1,045,851	1,047,557
Total revenues	**31,714,851**	29,667,772
POLICY BENEFITS AND EXPENSES		
Policyholders benefits and claims expenses (Note 6)	17,482,146	17,243,756
Ceded benefits and claims expenses (Note 6)	(2,039,961)	(2,718,771)
Policyholders benefits and claims expenses - net	15,442,185	14,524,985
Commissions (Note 7)	5,542,931	5,164,600
Risk Management for Mutual Members (Notes 11 & 21)	1,052,318	941,695
Operating expenses (Notes 11 & 21)	3,553,860	3,255,644
Total policy benefits and expenses	**25,591,294**	23,886,924
Income for the year before experience refund to Mutual Members	**6,123,557**	5,780,848
Experience refund to Mutual Members (Note 13)	4,000,000	4,000,000
Experience refund to withdrawn Mutual Members (Note 13)	–	(3,020)
	4,000,000	3,996,980
Net income and comprehensive income attributable to Mutual Members	**2,123,557**	1,783,868

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

STATEMENT OF SURPLUS AND OF MUTUAL MEMBERS' SHARES

For the year ended December 31, 2015, with comparative information for 2014

	2015	2014
	$	$
Surplus at beginning	24,212,923	22,428,855
Withdrawals of Mutual Members during the year (Note 14)	–	200
Net income and comprehensive income	2,123,557	1,783,868
Surplus at end	**26,336,480**	24,212,923
Mutual Members' shares at beginning	102,100	99,600
Contributions from Mutual Members during the year (Note 14)	2,900	2,700
Withdrawals of Mutual Members during the year (Note 14)	–	(200)
Mutual Members' shares at end	**105,000**	102,100
Total Mutual Members' equity	**26,441,480**	24,315,023

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

STATEMENT OF FINANCIAL POSITION

December 31, 2015, with comparative information for 2014

	2015	2014
	$	$
ASSETS		
Cash	2,861,936	1,690,531
Investments (Note 4)	54,632,674	50,925,297
Premiums receivable (Note 5)	12,484,531	11,719,778
Accounts receivable	232,714	316,800
Prepaid reinsurance premiums	1,025,050	811,236
Reinsurers' share in claims and settlement expenses paid	149,886	545,171
Reinsurers' share in the provision for unpaid claims and settlement expenses (Note 6)	8,812,914	11,063,482
Prepaid expenses	69,411	127,336
Deferred commissions costs (Note 7)	2,954,350	2,776,712
Fixed assets (Note 8)	416,872	407,112
Intangible assets (Note 9)	929,185	976,488
	84,569,523	81,359,943
LIABILITIES		
Provision for unpaid claims and settlement expenses (Note 6)	33,401,150	33,432,505
Unearned premiums (Note 10)	19,695,646	18,511,408
Accounts payable and accrued liabilities	824,937	876,197
Experience refund payable to Mutual Members (Note 13)	4,000,000	4,000,000
Deferred lease obligation and lease inducement	206,310	224,810
	58,128,043	57,044,920
MUTUAL MEMBERS' EQUITY		
Surplus	26,336,480	24,212,923
Mutual Members' shares (Note 14)	105,000	102,100
	26,441,480	24,315,023
	84,569,523	81,359,943

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

On behalf of the Board,

Jacques Bolduc, Director

Rémi Moreau, Director

STATEMENT OF CASH FLOWS

For the year ended December 31, 2015, with comparative information for 2014

	2015	2014
	$	$
Cash provided by (used in)		
OPERATING		
Net income	2,123,557	1,783,868
Items not affecting cash:		
Depreciation of fixed assets	86,685	82,203
Amortization of intangible assets	190,158	165,774
Deferred lease obligation and lease inducement	(18,500)	(14,107)
	2,381,900	2,017,738
Reinsurers' share in the provision for unpaid claims and settlement expenses	2,250,568	(1,045,802)
Deferred commissions costs	(177,638)	(263,153)
Unearned premiums	1,184,238	1,752,601
Provision for unpaid claims and settlement expenses	(31,355)	1,872,003
Interest earned	(1,045,851)	(1,047,557)
Change in non-cash operating working capital items (Note 15)	(586,254)	375,460
	3,975,608	3,661,290
INVESTING		
Acquisition of investments	(27,691,797)	(51,361,533)
Proceeds from the sale of investments	23,836,481	47,412,000
Interest received	1,287,513	1,348,245
Acquisition of fixed assets	(96,445)	(379,521)
Acquisition of intangible assets	(142,855)	(78,666)
Lease inducements	–	199,115
	(2,807,103)	(2,860,360)
FINANCING		
Contributions from Mutual Members	2,900	2,700
Net increase in cash and cash equivalents	1,171,405	803,630
Cash and cash equivalents at beginning	1,690,531	886,901
Cash and cash equivalents at end	**2,861,936**	1,690,531

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

La Mutuelle des municipalités du Québec was incorporated on November 17, 2003 under the *Cities and Towns Act* and the *Municipal Code of Québec*. In the normal course of its business, the core activities of *La Mutuelle des municipalités du Québec* consists in underwriting property and casualty insurance products (P&C) as well as to assist its Mutual Members in their own risk management. Its Mutual Members are comprised of municipalities within the meaning of articles 465.1 of *Cities and Towns Act* and 711.2 of *Municipal Code of Québec*. The head office of *La Mutuelle des municipalités du Québec* is located at 7100 Jean-Talon Street East, Suite 805, Montreal, Quebec, H1M 3S3, Canada.

Under the *Income Tax Act* (Canada) and the *Taxation Act* (Quebec), *La Mutuelle des municipalités du Québec* is exempt from federal and provincial income tax as well as from compensation tax payable by financial institutions.

The publication of these financial statements was authorized by the Board of Directors of *La Mutuelle des municipalités du Québec* on February 24, 2016.

1. Role of the appointed actuary and the independent auditor

The appointed actuary is designated by the Board of Directors of *La Mutuelle des municipalités du Québec*. The appointed actuary is responsible for making sure that the assumptions and methods used for purposes of valuating policy liabilities comply with recognized actuarial practices, the legislation in force, and any regulations or guidelines in this field. The appointed actuary must also express an opinion regarding the appropriateness of the policy liabilities as at the statement of financial position date with respect to the totality of obligations toward policyholders. This review, which seeks to verify the accuracy and completeness of the valuation data and the analysis of the assets, is an important element to be considered when establishing an opinion.

Policy liabilities are made up of two components: the claims liability and the premium liability. The claims liability includes provisions for indemnifications, provisions for non-settlement-related expenses and settlement expenses, provisions for claims incurred but not declared as well as reinsurers' share in such settlements. The premium liability represents the costs that will have to be incurred to acquire the premiums.

The services of the independent auditor were retained by Mutual Members at the time of the annual general meeting. The engagement of the independent auditor consists in conducting an independent audit of the financial statements in accordance with Canadian generally accepted auditing standards. Within the context of this audit engagement, the independent auditor considers the work of the appointed actuary and his report on the policy liabilities of *La Mutuelle des municipalités du Québec*. The independent auditor's report indicates management's responsibility for the financial statements, the auditor's responsibility as well as his opinion on the financial statements.

2. Significant accounting policies

Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and reflect the following significant accounting policies:

a) Basis of preparation

The financial statements, reported in Canadian dollars, have been prepared on a historical cost basis, as explained in the following accounting policies. Historical cost is generally based on the fair value of the consideration given in exchange for the assets.

b) Current and non-current classification

Assets expected to be realized and liabilities expected to be settled within *La Mutuelle des municipalités du Québec*'s normal operating cycle of one year are typically considered as current. All other assets and liabilities are classified as non-current. The statement of financial position does not make a distinction as to the current or non-current nature of assets and liabilities. However the following items are typically considered as current: cash, premiums receivable, accounts receivable, prepaid reinsurance premiums, reinsurers' share in claims and settlement expenses paid, prepaid expenses, deferred commissions costs, unearned premiums, accounts payable and accrued liabilities and experience refunds payable to Mutual Members. The following items are typically considered as non-current: fixed assets and intangible assets. The remaining items are comprised of both current and non-current amounts. The current and non-current portions of such balances are disclosed, where applicable, throughout the notes to the financial statements or within the risk management section.

c) Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents include cash and term deposits with maturities of three months or less from the acquisition date. As at December 31, 2015 and December 31, 2014, cash and cash equivalents consisted solely of cash.

d) Financial instruments

Financial assets and liabilities are recognized when *La Mutuelle des municipalités du Québec* becomes a party to the contractual provisions of the financial instruments. They are initially recognized at fair value and their subsequent measurement depends on their classification, as described below. Their classification depends on the nature and purpose for which the financial instruments were acquired or issued, their characteristics and the designation of such instruments by *La Mutuelle des municipalités du Québec*.

2. Significant accounting policies (cont'd)

d) Financial instruments (cont'd)

Cash	Loans and receivables
Investments – Term deposit	Loans and receivables
Investments – High-interest accounts	Loans and receivables
Investments – Capital shares	Loans and receivables
Investments – Bonds	Held to maturity
Premiums receivable	Loans and receivables
Accounts receivable	Loans and receivables
Reinsurers' share in claims and settlement expenses paid	Loans and receivables
Premiums owed to reinsurers	Other liabilities
Accounts payable and accrued liabilities	Other liabilities
Experience refund payable to Mutual Members	Other liabilities

Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market or designated into another category and that are recognized at amortized cost using the effective interest method, less any impairment.

Held to maturity
Financial assets held to maturity are non-derivative financial assets with fixed or determinable payments and fixed maturities, other than loans and receivables, that *La Mutuelle des municipalités du Québec* has the positive intent and ability to hold until maturity. These financial assets are measured at amortized cost using the effective interest method, less any impairment.

Other liabilities
Other liabilities are recorded at amortized cost using the effective interest method and include all financial liabilities.

Transaction costs
Transaction costs related to financial assets held to maturity, other liabilities, and loans and receivables are added to the carrying amount of the asset or netted against the carrying amount of the liability and are then recorded in net income over the expected life of the instrument using the effective interest method.

2. Significant accounting policies (cont'd)

d) Financial instruments (cont'd)

Effective interest method
The effective interest method is a method of calculating the amortized cost of a financial instrument and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts future cash receipts (including transaction costs, premiums and discounts earned or incurred) through the expected life of an instrument, to the net carrying amount on initial recognition.

Impairment of financial assets
Financial assets measured at amortized cost are tested for impairment at the end of each financial reporting period. The financial assets are impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial assets, the estimated future cash flows of the assets have been adversely affected.

Objective evidence of impairment includes the following situations:

- Significant financial difficulties of the issuer or counterparty;
- A breach of contract, such as a default or delinquency in interest or principal payments;
- Probability that the borrower will enter bankruptcy or any other financial reorganization;
- The disappearance of an active market for that financial asset because of financial difficulties.

For certain categories of financial assets, assets that are assessed not to be impaired individually are collectively assessed for impairment. Objective evidence of impairment for a portfolio could include *La Mutuelle des municipalités du Québec*'s past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the average credit period as well as observable changes in national or local economic conditions that correlate with default on receivables.

The amount of the impairment loss recognized is the difference between the asset's carrying amount and the present value of estimated future cash flows taking into account guarantees and sureties, discounted at the financial asset's original effective interest rate. The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets.

If, in a subsequent period, the amount of the impairment loss decreases, and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized.

Derecognition of financial assets
La Mutuelle des municipalités du Québec derecognizes a financial asset when the contractual rights to the cash flows from the asset expire or when the financial asset and substantially all risks and rewards of ownership of the financial asset are transferred to another party. If *La Mutuelle des municipalités du Québec* neither transfers nor retains substantially all risks and rewards of ownership and continues to control the transferred asset, it recognizes its retained interest in the asset and an associated liability for amounts it may have to pay.

2. Significant accounting policies (cont'd)

d) Financial instruments (cont'd)

Derecognition of financial liabilities
La Mutuelle des municipalités du Québec derecognizes financial liabilities when, and only when, *La Mutuelle des municipalités du Québec*'s obligations are discharged, cancelled or expire. The difference between the carrying amount of the financial liability derecognized and the consideration paid and payable is recognized in net income.

Regular-way purchases or sales of financial assets
Regular-way purchases or sales of held-to-maturity financial assets are recorded on the trade date, which is the date on which *La Mutuelle des municipalités du Québec* commits to buy or sell the asset.

Offsetting of financial assets and liabilities
Financial assets and liabilities are presented on a net basis when there is a legally enforceable right to set off the recognized amount and *La Mutuelle des municipalités du Québec* intends to settle on a net basis or to realize the asset and settle the liability simultaneously.

Fair value
The fair values of cash, premiums receivable, accounts receivable, the reinsurers' share in claims and settlement expenses paid, premiums owed to reinsurers, accounts payable and accrued liabilities, and experience refunds payable to Mutual Members approximate their carrying amounts due to their short-term maturities.

e) Fixed assets

Fixed assets are held for administrative purposes. They are recognized at cost less their residual value and accumulated depreciation. Depreciation is calculated based on their estimated useful lives using the straight-line method over the following terms:

Asset	Period
Leasehold improvements	Term of the lease
Furniture	10 years
Computer equipment	3 years

The estimated useful lives, residual values and depreciation method are reviewed at the end of each reporting period. The impact of any change in estimates is accounted for on a prospective basis.

2. Significant accounting policies (cont'd)

e) Fixed assets (cont'd)

Derecognition of fixed assets
A fixed asset is derecognized upon disposal when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising from the disposal or retirement of a fixed asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in profit or loss.

f) Intangible assets

Intangible assets with finite useful lives, which consist of software, and acquired separately are recognized at cost less accumulated amortization and accumulated impairment losses. Amortization is recognized on a straight-line basis over their estimated useful lives, which is a planned duration between three to seven years. The estimated useful life and amortization method are reviewed at the end of each reporting period, with the effect of any changes in estimates being accounted for on a prospective basis. Intangible assets begin to be amortized as soon as they are ready for use.

Derecognition of intangible assets
An intangible asset is derecognized on disposal or when no future economic benefits are expected from its use or disposal. Gains or losses arising from derecognition of an intangible asset (measured as the difference between the net disposal proceeds and the carrying amount of the asset) are recognized in net income when the asset is derecognized.

g) Impairment of fixed assets and intangible assets

At the end of each reporting period, *La Mutuelle des municipalités du Québec* reviews the carrying amounts of its fixed assets and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If such an indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if any. When it is not possible to estimate the recoverable amount of an individual asset, *La Mutuelle des municipalités du Québec* estimates the recoverable amount of the cash-generating unit to which the asset belongs. When a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

The recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized immediately in profit or loss.

2. Significant accounting policies (cont'd)

g) Impairment of fixed and intangible assets (cont'd)

When an impairment loss subsequently reverses, the carrying amount of the asset (or a cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset (or cash-generating unit) in prior years. A reversal of an impairment loss is recognized immediately in net income.

h) Balances related to premiums

i) Premiums and unearned premiums

Premiums are recorded when they are written and recognized on the statement of comprehensive income over the period covered by the insurance policy.

Unearned premiums represent the portion of written premiums related to the remaining coverage period up to fiscal year-end.

ii) Deferred commissions costs

Commissions associated with the earning of premiums are deferred and amortized over the duration of the related policies insofar as they are deemed recoverable, after having taken into account the claims and the related expenses as well as any expected investment income.

i) Balances related to losses

i) Provision for unpaid claims and settlement expenses

The provision for unpaid claims and settlement expenses is the estimate of the total cost to settle all claims occurring before the closing of the financial statements, regardless of whether or not they were reported to *La Mutuelle des municipalités du Québec*. The provision for unpaid claims and settlement expenses has been established in accordance with the generally accepted actuarial principles under the standards set by the Canadian Institute of Actuaries. Since this provision is necessarily based on estimates, the final value may differ from the estimates. A provision for claims and settlement expenses is included for claims incurred but not reported based on past experience. The established methods for making the estimates are periodically revised and updated, and all adjustments are reflected in the year's results. These adjustments are attributable to events related to the final settlement of claims but which have not yet occurred and which perhaps may not occur for some time. These adjustments may also be caused by additional information concerning the claims, changes in the interpretation of the contracts by the courts or major variances in relation to historical trends in terms of the seriousness or frequency of claims. Consequently, claims and settlement expenses are recognized when incurred. A provision is determined for external and internal settlement expenses.

2. Significant accounting policies (cont'd)

i) Balances related to losses (cont'd)

i) Provision for unpaid claims and settlement expenses (cont'd)

The best estimates for incurred, but not reported, claims liabilities on a gross and net basis have been determined based on various actuarial methods, mainly the Bornhuetter-Ferguson method. This method uses the historical development of incurred and reported claims, based on reserves on a case-by-case basis plus benefits paid, per year of accident in order to anticipate changes in claims and it considers the concept of earned premiums to assess future developments, making it possible to introduce a measure of risk exposure and to use an indication of the loss anticipated on the future loss experience. Different assumptions are used to estimate the unreported claims liability on a gross and net basis: the discount rate, the margin for unfavourable variances and the loss ratio.

When the undiscounted claims liability is established, it is adjusted to present value. The claims liability is discounted using a rate based on the rate of return of investments held by *La Mutuelle des municipalités du Québec*, from which a 0.25% margin is deducted. This discount rate is 1.66% as at December 31, 2015 (1.80% in 2014).

Actuarial standards require that a margin for unfavourable variances be considered to take into consideration the uncertainty level of the assumptions used. The rates used to establish the margins for unfavourable variances as at December 31, 2015 vary from 5% (5% in 2014) for short-term risks, such as for property and automobiles, and 12.5% (12.5% in 2014) for long-term risks, such as civil liability, errors and omissions.

As mentioned previously, the method used to establish the claims liability is based on a loss ratio. As at December 31, 2015, this ratio varies from 10% to 80% (10% to 80% in 2014).

ii) Reinsurers' share in the provision for unpaid claims and settlement expenses

The reinsurance amounts that are expected to be collected in relation to claims and settlement expenses are recorded as assets in accordance with the reinsurance contracts and based on principles consistent with the recognition of the provision for unpaid claims and settlement expenses. The margin for unfavorable variances applied for reinsurance is 1% as at December 31, 2015 (1% in 2014).

j) Leases

Leases in which substantially all of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any lease inducements received from the lessor) are recognized in net income on a straight-line basis over the term of the lease.

2. Significant accounting policies (cont'd)

k) Deferred lease obligation and lease inducement

La Mutuelle des municipalités du Québec leases office space with a predetermined fixed escalation clause. *La Mutuelle des municipalités du Québec* recognizes the related rent expense on a straight-line basis and, consequently, records the difference between the recognized rental expense and the amounts payable under the lease as deferred lease obligation.

Lease inducement consist of an allocation received from lessor for leasehold improvements over the lease term.

l) Investment income

Interest earned on a financial asset is recognized when it is probable that the economic benefits will flow to *La Mutuelle des municipalités du Québec* and that the amount of revenues can be reliably measured.

Interest is recognized on a time basis, based on the amount of unpaid capital and the applicable effective interest rate.

Experience refunds declared by a financial institution and calculated on interest received are recognized when the right to receive such income has been established.

m) Experience refund to Mutual Members

Experience refund is presented in the statement of comprehensive income on the date that is declared by the Board of Directors. At that time, experience refund is recorded as experience refund payable to Mutual Members on the statement of financial position. Experience refunds disbursed to Mutual Members that withdraw before the end of the eligibility period are deducted from the current period charge.

n) Use of estimates

The preparation of financial statements in accordance with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the year. Actual results could differ from management's best estimates. The most significant estimates are related to the determination of:

- the provision for unpaid claims and settlement expenses as well as the reinsurers' share;
- the estimated useful lives of fixed assets and intangible assets.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

o) Critical judgements in applying accounting policies

The following are the critical judgements, apart from those involving estimates, that the directors have made in the process of applying the accounting policies of *La Mutuelle des municipalités du Québec*.

2. Significant accounting policies (cont'd)

o) Critical judgements in applying accounting policies (cont'd)

Useful lives of fixed assets and intangible assets
La Mutuelle des municipalités du Québec reviews the estimated useful lives of fixed assets at the end of each reporting period. During the current year, management determined that no useful lives need to be modified.

Impairment of financial assets
At the end of each reporting period, *La Mutuelle des municipalités du Québec* determines if there is objective evidence of the impact of one or more events that occurred after the initial recognition of the financial assets on the estimated future cash flows of the assets. During the year considered, management determined that no such objective evidence exists.

Held-to-maturity financial assets
Management has reviewed the financial assets held to maturity of *La Mutuelle des municipalités du Québec* based on its capital and liquidity requirements and has confirmed that *La Mutuelle des municipalités du Québec* has the positive intention and ability to hold these assets to maturity. The financial assets held to maturity are the municipal bonds presented in Note 4.

3. Changes in accounting policies

Application of new accounting standards

Every year, the *International Accounting Standards Board* ("IASB") publishes IFRS improvements that consist of limited scope amendments to clarify or adjust certain aspects of existing IFRS standards. The provisions set out in some of these annual improvements are effective for annual reporting periods beginning on or after July 1, 2014. These annual improvements had no material impact on the financial statements of *La Mutuelle des municipalités du Québec*.

Future changes in accounting policies

IFRS 9 *Financial Instruments* ("IFRS 9")
In July 2014, the IASB published an amended version of IFRS 9 *Financial Instruments*, which replaces IAS 39 *Financial Instruments: Recognition and Measurement*, and IFRIC 9 *Reassessment of Embedded Derivatives.*

IFRS 9 includes guidance on the classification and measurement of financial instruments, impairment of financial assets, and a new general hedge accounting model. The IASB has now concluded the replacement initiative of IAS 39. The IFRS 9 version published in 2014 supersedes all preceding versions of the standard. However, early adoption of preceding versions is allowable, as long as the initial adoption date is anterior to February 1, 2015. IFRS 9 does not replace requirements in relation with portfolio fair value hedge accounting with regards to interest rate risk. This initiative was separated from the IFRS 9 project, due to the long term nature of work currently underway related to macro coverage. As a result, the exception presented under IAS 39 related to portfolio fair value hedge accounting with regards to interest rate risk of a financial assets or liabilities portfolio continues to apply.

3. Changes in accounting policies (cont'd)

Future changes in accounting policies (cont'd)

IFRS 9 *Financial Instruments* ("IFRS 9") (cont'd)

While the new standard is generally effective for years beginning on after January 1, 2018, in December 2015 the IASB published an Exposure Draft *Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts*, which proposes to allow some insurers optional transitional relief until the forthcoming insurance accounting standard is available for implementation. The proposed options would allow (a) entities whose predominant activity is issuing insurance contracts within the scope of IFRS 4 to defer the implementation of IFRS 9 to as late as January 1, 2021, which may allow alignment of the implementation of IFRS 9 with the forthcoming insurance accounting standard, or alternatively (b) give entities issuing insurance contracts the option to remove from profit or loss the incremental volatility caused by changes in the measurement of specified financial assets upon application of IFRS 9.

IFRS 4 *Insurance Contracts* ("IFRS 4")

In June 2013, the IASB issued a revised exposure draft proposing a comprehensive measurement approach for all types of insurance contracts, which would replace the existing IFRS 4 *Insurance Contracts*. Deliberations of the exposure draft continue and a final standard is expected to be issued in late 2016. The effective date of the final standard is not expected to be before 2020.

IFRS 15 *Revenue from Contracts with Customers* ("IFRS 15")

In May 2014, the IASB issued a new standard that revises previous guidance on revenue recognition, from sources other than insurance premiums and investment income, which are unaffected. The new standard is effective for years beginning on or after January 1, 2018. *La Mutuelle des municipalités du Québec* does not expect the application of this standard to have an impact on its financial statements.

IFRS 16 *Leases* ("IFRS 16")

IFRS 16 was issued on January 13, 2016. The new standard will replace existing lease guidance in IFRS and related interpretations, and requires companies to bring most leases on-balance sheet. The financial reporting impact of adopting IFRS 16 is being assessed. The new standard is effective for years beginning on or after January 1, 2019.

4. Investments

	2015		
	$	$	$
	Nominal value	**Fair value**	**Carrying amount**
HELD TO MATURITY			
Municipal bonds, stipulated interest rates from 1.25% to 5.45%, effective interest rates from 1.13% to 4.90%, maturing from February 2016 to March 2024	20,895,000	21,700,913	21,311,022
LOANS AND RECEIVABLES			
High-interest cash accounts variable rates currently bearing interest from 0.85% to 1.05% with no fixed maturity	27,267,652	27,267,652	27,267,652
Variable rate capital shares bearing interest from 0% to 4.25% with no fixed maturity	2,000,000	2,000,000	2,000,000
Term deposit redeemable at any time, currently bearing interest at 1.8%, maturing in September 2017	4,054,000	4,054,000	4,054,000
	54,216,652	**55,022,565**	**54,632,674**

	2014		
	$	$	$
	Nominal value	Fair value	Carrying amount
HELD TO MATURITY			
Municipal bonds, stipulated interest rates from 1.40% to 5.45%, effective interest rates from 1.32% to 4.90% maturing from January 2015 to March 2024	23,093,000	23,917,245	23,565,806
LOANS AND RECEIVABLES			
Term deposits, $5,000,000 redeemable at any time, bearing interest from 1.31% to 2.8%, maturing from February 2015 to September 2017	14,600,000	14,600,000	14,600,000
Term savings bearing interest at the rate of 1.15% for all amounts exceeding $1,000,000 and maturing on June 30, 2015	12,759,491	12,759,491	12,759,491
	50,452,491	51,276,736	50,925,297

4. Investments (cont'd)

Hierarchy of recurring fair value measurements

Disclosures regarding financial instruments must be presented as a hierarchy that categorizes the inputs to valuation models used to value financial assets and liabilities. The hierarchy gives the highest priority to readily available unadjusted quoted prices in active markets for identical assets or liabilities and lowest priority to unobserved inputs. The three levels of the hierarchy are described below:

Level 1 - Fair value measurement based on unadjusted quoted prices in active market for identical assets of liabilites.

Level 2 – Fair value measurement based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 – Fair value measurement based on significant unobservable inputs that are supported by little or no market activity and incorporate management's best estimates.

The fair value of municipal bonds for which the market is not active is determined by independent valuation services that take into consideration the return or market price of financial instruments that have comparable conditions, such as quality, maturity and type of investment. Municipal bonds are classified at Level 2.

The fair value of high-interest accounts cannot be determined by using quoted prices from active markets for similar assets or in a similar way, directly or indirectly, and is based mostly on non- market observable input and management's best estimates. Capital shares are classified at Level 3.

The fair value of term deposit approximates its carrying amount due to the weak interest rate fluctuations and its relatively short maturity.

There were no transfers between levels in 2015 and 2014.

5. Premiums receivable

In accordance with the provisions of an enforceable netting agreement, *La Mutuelle des municipalités du Québec* accounts for premiums receivable and commissions payable on a net basis. The gross amounts are as follows:

	2015	2014
	$	$
GROSS FINANCIAL ASSETS		
Premiums receivable	14,693,824	13,792,411
OFFSET FINANCIAL LIABILITIES		
Commissions payable	(2,209,293)	(2,072,633)
Net amount presented in the statement of financial position	**12,484,531**	11,719,778

6. Claims and settlement expenses

The change in the provision for claims and settlement expenses as well as reinsurers' share in the claims and settlement expenses included in the statement of financial position, together with its impact on the claims and settlement expenses shown in the statement of comprehensive income for the years are as follows:

			2015
	$	**$**	**$**
	Gross	**Transferred**	**Net**
Provision for unpaid claims and settlement expenses at beginning	33,432,505	11,063,482	22,369,023
Increase (decrease) in estimated losses and expenses			
During the current year	18,039,555	2,397,003	15,642,552
During previous years	(557,409)	(357,042)	(200,367)
	17,482,146	2,039,961	15,442,185
Amounts paid for claims incurred			
During the current year	5,707,702	–	5,707,702
During previous years	11,805,799	4,290,529	7,515,270
	17,513,501	4,290,529	13,222,972
Provision for unpaid claims and settlement expenses at end	**33,401,150**	**8,812,914**	**24,588,236**

6. Claims and settlement expenses (cont'd)

			2014
	$	$	$
	Gross	Transferred	Net
Provision for unpaid claims and settlement expenses at beginning	31,560,502	10,017,680	21,542,822
Increase (decrease) in estimated losses and expenses			
During the current year	17,502,294	2,651,826	14,850,468
During previous years	(258,538)	66,945	(325,483)
	17,243,756	2,718,771	14,524,985
Amounts paid for claims incurred			
During the current year	5,868,771	68,580	5,800,191
During previous years	9,502,982	1,604,389	7,898,593
	15,371,753	1,672,969	13,698,784
Provision for unpaid claims and settlement expenses at end	33,432,505	11,063,482	22,369,023

Loss ratio sensitivity analysis

Given that a loss ratio is used to establish the provision for unpaid claims and settlement expenses, as mentionned in second paragraph of Note 2 i) i), a 5% increase or decrease in the loss ratio would result in an increase or decrease in the net provision of reinsurers' share for unpaid claims and settlement expenses, of approximately $436,000 as at December 31, 2015 ($368,000 as at December 31, 2014).

6. Claims and settlement expenses (cont'd)

Estimated ultimate claims (in thousands of dollars)

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	TOTAL
	$	$	$	$	$	$	$	$	$	$	$
At the end of year of occurrence	5,665	7,382	8,992	9,689	12,680	11,034	12,993	16,254	14,850	15,643	
One year later	5,446	7,883	9,642	11,920	11,998	10,656	11,131	15,596	14,807		
Two years later	5,367	8,170	11,626	11,624	11,855	10,128	11,149	16,010			
Three years later	5,902	9,424	11,879	11,590	11,644	10,245	10,892				
Four years later	6,278	9,200	11,651	11,560	11,685	10,493					
Five years later	6,318	9,168	11,481	11,652	11,640						
Six years later	7,587	9,174	11,447	11,285							
Seven years later	7,506	9,216	11,286								
Eight years later	7,543	9,183									
Nine years later	7,568										
Current estimate of cumulative claims	7,568	9,183	11,286	11,285	11,640	10,493	10,892	16,010	14,807	15,643	118,807
Less cumulative payments	7,491	8,862	11,123	10,997	10,769	8,792	9,085	11,837	9,569	5,708	94,233
Provision for unpaid claims and settlement expenses - net	77	321	163	288	871	1,701	1,807	4,173	5,238	9,935	24,574
Years before 2006											14
Reinsurers' share in the provision for unpaid claims and settlement expenses											8,813
Provision for unpaid claims and settlement expenses – gross											**33,401**

7. Deferred commissions costs

	2015	2014
	$	$
Balance at beginning	2,776,712	2,513,559
Deferred commissions costs during the year	5,720,569	5,427,753
Amortization of deferred commissions costs during the year	(5,542,931)	(5,164,600)
	177,638	263,153
Balance at end	**2,954,350**	2,776,712

8. Fixed assets

	Leasehold improvements	Furniture	Computer equipment	Total
	$	$	$	$
COST				
Balance as at January 1, 2014	140,232	63,765	109,389	313,386
Acquisitions	274,560	51,782	53,179	379,521
Balance as at December 31, 2014	414,792	115,547	162,568	692,907
Disposals	(140,232)	-	(20,320)	(160,552)
Acquisitions	20,410	11,426	64,609	96,445
Balance as at December 31, 2015	294,970	126,973	206,857	628,800
ACCUMULATED DEPRECIATION				
Balance as at January 1, 2014	130,014	18,584	54,994	203,592
Depreciation expense	30,287	10,011	41,905	82,203
Balance as at December 31, 2014	160,301	28,595	96,899	285,795
Disposals	(140,232)	-	(20,320)	(160,552)
Depreciation expense	27,825	12,026	46,834	86,685
Balance as at December 31, 2015	47,894	40,621	123,413	211,928
CARRYING AMOUNT				
As at December 31, 2014	254,491	86,952	65,669	407,112
As at December 31, 2015	**247,076**	**86,352**	**83,444**	**416,872**

9. Intangible assets

	Software
	$
COST	
Balance as at January 1, 2014	1,143,141
Acquisitions	78,666
Balance as at December 31, 2014	1,221,807
Acquisitions	142,855
Balance as at December 31, 2015	1,364,662
ACCUMULATED AMORTIZATION	
Balance as at January 1, 2014	79,545
Amortization expense	165,774
Balance as at December 31, 2014	245,319
Amortization expense	190,158
Balance as at December 31, 2015	435,477
CARRYING AMOUNT	
As at December 31, 2014	976,488
As at December 31, 2015	**929,185**

10. Unearned premiums

	2015	2014
	$	$
Balance at beginning	18,511,408	16,758,807
Net written premiums during the year	31,853,238	30,372,816
Net earned premiums during the year	(30,669,000)	(28,620,215)
	1,184,238	1,752,601
Balance at end	**19,695,646**	18,511,408

11. Personnel related costs

	2015	2014
	$	$
Salaries	2,914,918	2,719,434
Fringe benefits	519,455	451,716
	3,434,373	3,171,150

12. Investment income

	2015	2014
	$	$
LOANS AND RECEIVABLES		
Interest	448,991	396,382
Experience refunds on cashed interest	41,091	23,305
	490,082	419,687
HELD TO MATURITY		
Interest	555,769	627,870
	1,045,851	1,047,557

13. Experience refund to Mutual Members

The payment of experience refund must be approved by the Board of Directors. The amount of the experience refund is based on the historic performance of *La Mutuelle des municipalités du Québec* and on the conclusions of the dynamic capital adequacy test prepared annually by the appointed actuary. Among other things, this test determines whether *La Mutuelle des municipalités du Québec* has the financial capacity to meet adverse situations while remaining financially viable.

On November 30, 2015, the Board of Directors approved experience refund of $4,000,000 for the year ended December 31, 2015 ($4,000,000 for the year ended December 31, 2014).

13. Experience refund to Mutual Members (cont'd)

To be eligible for experience refund for the year ended December 31, 2015, a Mutual Member must:

- Be a Mutual Member of *La Mutuelle des municipalités du Québec* since January 1st 2012;
- Keep its insurance policy in force between December 31, 2015 and December 30, 2016.

The formula used for calculating each eligible Mutual Member's share is a two-step process:

- The first portion of $2,000,000 in experience refund is distributed to eligible Mutual Members in proportion to the total amount of premiums paid during a defined period;
- The second portion of $2,000,000 in experience refund is based on the Mutual Member's contribution to the profitability of *La Mutuelle des municipalités du Québec*. The latter is established as a function of the insurance records' quality based upon the loss experience of the corresponding period, which must be below a maximum threshold.

Experience refund for Members that withdraw before the end of the eligibility period is presented separately in the statement of comprehensive income.

14. Mutual Members' shares

Membership and initial contribution and rights

To become a Mutual Member of *La Mutuelle des municipalités du Québec*, a municipality, as defined in Note 1, must adopt a resolution in which it adheres to the Agreement under section 465.1 and thereafter of the *Cities and Towns Act* and section 711.2 and thereafter of the *Municipal Code of Québec* signed on April 3, 2003, which is deemed to form an integral part of said resolution, take out insurance with *La Mutuelle des municipalités du Québec* and pay an initial contribution of $100.

The initial contribution is non-refundable.

Every member has the right to be invited to any Mutual Members' annual assembly of *La Mutuelle des municipalités du Québec*, to attend such meetings, and to cast a vote on the basis of one vote per Mutual Member. The head of a Mutual Member's Board may perform any duty within the Board of Directors of *La Mutuelle des municipalités du Québec* or one of its committees on the conditions set out in By-law 1.1, subject to legislative provisions in force.

Annual contribution

The Board of Directors can set the amount of the annual contribution, as necessary. If no annual contribution is determined, the amount is considered to be zero.

Special contribution

The Board of Directors may order that a special contribution be paid, as necessary. This contribution is divided among the Mutual Members in proportion to the amount of the premium written by the Mutual Member and its agencies.

14. Mutual Members' shares (cont'd)

Suspension or expulsion

The Board of Directors may order the suspension or expulsion of a Mutual Member pursuant to the terms and conditions set out in By-law 1.1 of *La Mutuelle des municipalités du Québec*.

Withdrawal

According to the *Municipal Code of Québec* and the *Cities and Towns Act*, a Mutual Member may not withdraw from *La Mutuelle des municipalités du Québec* within five years of joining *La Mutuelle des municipalités du Québec*.

In addition, a Mutual Member may not withdraw from *La Mutuelle des municipalités du Québec* without providing twelve months' prior notice to general management.

A Mutual Member who withdraws from *La Mutuelle des municipalités du Québec* remains subject to any special contribution as determined by the Board of Directors within a period of two years following its withdrawal. If applicable, the contribution is based on the premium paid by this Mutual Member and its agencies prior to the withdrawal.

In all cases, the departure of a Mutual Member must be approved by the *Autorité des marchés financiers* in accordance with the *Municipal Code of Québec* and the *Cities and Towns Act*.

	2015	2014
Number of Mutual Members	**1,050**	1,021
Contributions from Mutual Members	**$105,000**	$102,100

During the year ended December 31, 2015, 29 Mutual Members (27 Mutual Members in 2014) joined *La Mutuelle des municipalités de Québec* and no Mutual Members withdrew (2 Mutual Members in 2014).

15. Additional cash flow information

Change in non-cash operating working capital items:

	2015	2014
	$	$
Premiums receivable	(764,753)	(1,309,788)
Accounts receivable	(9,637)	(1,122)
Reinsurers' share in claims and settlement expenses paid	395,285	375,381
Prepaid expenses	57,925	(48,539)
Prepaid reinsurance premiums	(213,814)	73,288
Accounts payable and accrued liabilities	(51,260)	286,240
Experience refund payable to Mutual Members	-	1,000,000
	(586,254)	375,460

16. Commitments

La Mutuelle des municipalités du Québec leases automotive equipment and premises under operating leases that expire on various dates until June 2024. Future rental payments will total $1,755,722 and include the following payments over the next financial periods:

	$
2016	224,582
2017	216,063
2018	197,458
2019	191,869
2020	199,882
2021 to 2024	725,868

The costs relating to these operating leases recognized totalled $204,742 in 2015 ($206,552 in 2014). These costs are presented as administrative expenses and as policyholder benefits and settlement expenses.

As of December 31, 2015, *La Mutuelle des municipalités du Québec* had a total of $75,000 ($150,000 in 2014) of letters of guarantee in circulation, for an authorized amount of $75,000 ($150,000 in 2014) which will expire June 30, 2016. This letter of guarantee has been issued in favor of the lessor of the premises so as to secure the obligations of *La Mutuelle des municipalités du Québec* as lessee.

17. Contingencies

In the normal course of business, various claims are pending against *La Mutuelle des municipalités du Québec*. Such claims are often subject to much uncertainty and their outcome cannot be predicted. According to management, adequate provision has been made for these claims and their settlement should not have a significant adverse effect on *La Mutuelle des municipalités du Québec*'s future operating results or financial position.

18. Capital management

La Mutuelle des municipalités du Québec manages its capital funds in such manner as to comply with capital adequacy as required under *An Act respecting insurance* (R.S.Q. c. A-32) and its financial commitments to stakeholders in the settlement of claims. The regulatory capital differs from the Mutual Members' equity as stated in the statement of financial position owing to the fact that it is weighted as a function of the risk associated with the financial situation and insurance activities.

Under *An Act respecting insurance*, *La Mutuelle des municipalités du Québec* is required to maintain adequate capital funds to ensure sound and prudent management practices. The *Autorité des marchés financiers* has issued a guideline that limits the minimum capital funds standard according to the minimum capital test (MCT), represented by the ratio of available capital over the minimum required capital (the solvency ratio).

January 1, 2015, the *Autorité des marchés financiers* has modified its guideline. Thus, for year 2014, the measure of MCT is calculated under previous requirements whereas 2015 is calculated under current requirements.

The available capital corresponds to Mutual Members' equity. The minimum required capital comes from the assessment of the risk of financial assets and liabilities related to policies by the application of various capital factors. The *Autorité des marchés financiers* has established the minimal MCT at 100%. Furthermore, the target MCT is set at 150% for Canadian property & casualty insurance companies. In order to reach its own objectives, *La Mutuelle des municipalités du Québec* has set its minimal target ratio at 175%.

As at December 31, 2015, the MCT is detailed as follows:

(in thousands of dollars)	**2015 (New)**	2014 (Old)
	$	$
Total capital available	25,877	23,783
Total capital required	7,743	6,772
Excess capital	18,134	17,011
Result of MCT Measure	334%	351%

19. Risk management related to financial instruments and insurance risk

Risk management policies and objectives

In its normal course of business, *La Mutuelle des municipalités du Québec* is exposed to a variety of financial risks, namely credit, liquidity, interest rate, market and insurance and reinsurance risks.

The Board of Directors is in charge of understanding and approving the financial risk management strategies, and management is in charge of implementing these strategies. *La Mutuelle des municipalités du Québec*'s goal with regard to financial risks is to optimize the risk-return ratio within defined limits throughout all its activities. Risk control is carried out through the application of policies, strategies as well as sound and cautious management procedures that are blended into all of *La Mutuelle des municipalités du Québec*'s operations. The Board has created the following committees to identify, understand, communicate and manage *La Mutuelle des municipalités du Québec*'s risk exposure: the statutory committee of ethics and governance and the statutory committee of audit and investment, as well as the advisory committee of insurance and the advisory committee for Mutual Members' risk management. *La Mutuelle des municipalités du Québec* adopted an integrated risk management policy, which structures and integrates upstream actions to be taken for all types of risk to which it is exposed, including financial risks. This policy has been reviewed during a fourth exercise of integrated risk management which took place in 2014.

La Mutuelle des municipalités du Québec has an investment policy whose objectives are prioritized as follows: the safeguarding of capital from risks of losses, neutralizing poor matching of capital with needs for liquidity, optimizing return on investment within the set investment boundaries for each eligible investments. The investment policy, which was entirely reviewed in 2015, is revised annually and updated if required by changing circumstances.

The risk exposure, objectives, procedures and risk management processes have not changed significantly during the year, with the exception of the above-mentioned item.

Financial risks

a) Credit risk

Credit risk arises from potential losses involving a borrower's or a counterparty's failure to fulfill its contractual duties when impending and outstanding. A counterparty can be any person or entity whose cash resources or other valuable considerations are considered forthcoming in order to extinguish a liability or obligation owed to *La Mutuelle des municipalités du Québec*.

Credit risk also includes concentration risk. Concentration risk arises when there is a concentration of investments in entities with similar characteristics, or when a substantial investment is made with a single entity.

Based on the valuation performed by *La Mutuelle des municipalités du Québec*, cash, investments, accounts receivable, amounts receivable from reinsurers and premiums receivable are the main items that may represent a credit risk.

19. Risk management related to financial instruments and insurance risk (cont'd)

Financial risks (cont'd)

a) Credit risk (cont'd)

Cash
All cash is held in a financial institution with good standings in Québec and with an excellent credit rating. *La Mutuelle des municipalités du Québec* considers that the credit risk related to this financial institution is low. *La Mutuelle des municipalités du Québec* does not actively manage the concentration risk related to cash.

Investments
All term deposits, high-interest accounts and capital shares are held in financial institutions with a credit rating of A- or better. *La Mutuelle des municipalités du Québec* considers that the credit risk relating to these financial institutions is low.

To satisfy the objectives of its investment policy and comply with the applicable regulatory provisions, *La Mutuelle des municipalités du Québec* favours investing in instruments whose credit risk rating is low. The investment policy makes it possible to acquire bonds issued or guaranteed by the federal, provincial or municipal government, with preference being given to Quebec municipalities. Municipal bond issuers have generally no credit rating on the market, making it impossible to measure the credit risk of most issuers. The policy also allows for investment in term deposits, mutual of exchange traded funds, deposit notes and capital shares.

As at December 31, 2015, its entire bond portfolio was made up of bonds from Quebec municipalities. As at December 31, 2015, four municipalities account for 49% of the bond portfolio (four municipalities accounted for 48% in 2014).

Accounts receivable
In 2015, accounts receivable are comprised of interests receivable. The credit risk associated with interest receivable is the same as for term deposits and municipal bonds.

Due from reinsurers
Failure on the part of reinsurers to fulfill their obligations could result in losses for *La Mutuelle des municipalités du Québec*. *La Mutuelle des municipalités du Québec* does business with more than one reinsurer, thereby reducing its concentration risk In addition, all reinsurers with which it does business are certified with a credit rating of A- or better, which serves to reduce the credit risk.

Premiums receivable
All premiums are receivable from the only broker mandated by *La Mutuelle des municipalités du Québec*. *La Mutuelle des municipalités du Québec* has no knowledge of information leading it to believe that this broker may be faced with insolvency problems. As at December 31, 2015 and December 31, 2014, no premiums receivable were outstanding.

19. Risk management related to financial instruments and insurance risk (cont'd)

Financial risks (cont'd)

a) Credit risk (cont'd)

Maximum credit risk
The maximum credit risk exposure associated with financial instruments is equivalent to the carrying amount of the financial assets presented in the statement of financial position.

b) Liquidity risk

Liquidity risk represents the possibility that *La Mutuelle des municipalités du Québec* may not be able to gather sufficient cash resources, when required and under reasonable conditions, to meet its financial obligations. The investment policy uses the timeframe established to settle claims in the dynamic capital adequacy testing to establish acceptable investment terms.

The liquidity risk for current financial items is low. Cash, premiums receivable, accounts receivable and the reinsurers' share in claims and settlement expenses paid are sufficient to allow *La Mutuelle des municipalités du Québec* to meet its financial obligations to settle accounts payable and accrued liabilities, experience refund payable to Mutual Members and premiums owed to reinsurers.

Liquidity risk mainly relates to the provision for unpaid claims and settlement expenses, net of the reinsurers' share. The following tables present an estimate of amounts established for each settlement period and the matching of investment maturities, at nominal value. Investments with no maturity are presented under the column "less than 12 months."

(in thousands of dollars)				**2015**
	$	**$**	**$**	**$**
	Less than 12 months	**1 to 2 years**	**2 to 4 years**	**More than 4 years**
Provision for unpaid claims and settlement expenses, net of the reinsurers' share (undiscounted amount)	**10,870**	**5,696**	**6,187**	**2,485**
Bonds	4,571	4,419	10,311	1,594
High interest accounts	27,268	-	-	-
Capital shares	2,000	-	-	-
Term deposit	-	4,054	-	-
Total	**33,839**	**8,473**	**10,311**	**1,594**

19. Risk management related to financial instruments and insurance risk (cont'd)

Financial risks (cont'd)

b) Liquidity risk (cont'd)

(in thousands of dollars)				2014
	$	$	$	$
	Less than 12 months	1 to 2 years	2 to 4 years	More than 4 years
Provision for unpaid claims and settlement expenses, net of the reinsurers' share (undiscounted amount)	10,030	5,120	5,607	2,247
Bonds	4,597	4,571	8,652	5,273
Term deposits	23,359	-	4,000	-
Total	27,956	4,571	12,652	5,273

c) Market risk

Market risk occurs when the value of an investment fluctuates because of changes in market prices, whether those changes are caused by factors specific to the investment or its issuer, or by factors affecting all instruments traded in the market. *La Mutuelle des municipalités du Québec* seeks to minimize this risk by making investments whose market risks are low. The policy of *La Mutuelle des municipalités du Québec* is to hold on to its bond investments to maturity, thereby limiting market risk.

d) Interest rate risk

Interest rate risk occurs when interest rates fluctuate and negatively affect the financial position of *La Mutuelle des municipalités du Québec*, which occurs when market interest rates increase.

Interest rate risk is also attributable to bond investments. The policy of *La Mutuelle des municipalités du Québec* is to hold on to its bond investments to maturity, thereby limiting market risk since a fluctuation in interest rates would not change the nominal value received upon maturity of the bond.

Interest rate risk is also due to term deposit investments. The policy of *La Mutuelle des municipalités du Québec* is to invest in term deposits that are redeemable at all times or maturing in less than two years.

Information on the maturity of interest-bearing investments is presented in the Liquidity risk section in this note.

19. Risk management related to financial instruments and insurance risk (cont'd)

Financial risks (cont'd)

e) Interest rate sensitivity

When the time value of money is taken into consideration to establish provisions for unpaid claims and settlement expenses, an increase or decrease in the capitalization rate may result in a decrease or increase in the burden of losses and the settlement expenses. A 1% change in the discount rate would have a $411,000 impact on the provision for unpaid claims and settlement expenses as at December 31, 2015 ($370,000 as at December 31, 2014).

Management estimates that an immediate hypothetical 1% parallel rise or decline in interest rates would respectively decrease or increase the fair value of bonds by approximately $530,000 as at December 31, 2015 ($655,000 as at December 31, 2014).

Insurance risk

La Mutuelle des municipalités du Québec was created for general insurance purposes and in order to manage risk for its Mutual Members as well as their agencies.

The risk in any insurance contract is the possibility that an insured event will occur, together with the uncertainty as to the value of the resulting claim. Due to the very nature of an insurance contract, this risk is random and therefore unpredictable. However, overall, these risks follow probability trends making it possible to manage insurance risk.

There are three possible types of insurance risk in the normal course of business: product design and pricing risk, underwriting risk and claims settlement risk.

Product design and pricing risk

Product design and pricing risk is the financial risk of losses related to insurance operations, namely, when commitments exceed those that were anticipated or when such commitments exceed the price that was set for such products.

La Mutuelle des municipalités du Québec is a niche market insurer specializing in the municipal sector. It has acquired insurance expertise in this sector for both insurance products and their application. Since its creation, the insurance committee has validated changes to underwriting parameters or the pricing schedule and submitted this to the Board, as well as any additions, extensions or deletions of guarantees, therefore monitoring profitability.

La Mutuelle des municipalités du Québec's exposure to insurance risk concentration is mitigated by portfolio diversification in various geographical areas and lines of business. *La Mutuelle des municipalités du Québec* has exposure to catastrophic losses and has sought protection by signing reinsurance treaties limiting the losses that could result from each event.

19. Risk management related to financial instruments and insurance risk (cont'd)

Insurance risk (cont'd)

Underwriting risk
Underwriting risk is the risk resulting from the selection and acceptance of risks to be insured.

Under its statutes, *La Mutuelle des municipalités du Québec*'s sole purpose is to insure municipal risks in Quebec. This specialization provides greater stability and predictability, thereby reducing the anti-selection risk. Moreover, to minimize risks, insurance policies are underwritten in accordance with *La Mutuelle des municipalités du Québec's* management practices taking its risk tolerance and underwriting standards into account.

The insurance program is available to local municipalities, regional county municipalities, inter-municipal boards and other municipal agencies allowed under its statutes.

La Mutuelle des municipalités du Québec offers property insurance, loss of income, civil liability insurance, umbrella (Follow-form) liability, errors and omissions, automobile, crime, and boiler and machinery insurance.

The insurance portfolio is stable, with a retention rate of more than 99% since its creation. Notwithstanding the fact that a Mutual Member becomes a member for an initial five-year period, *La Mutuelle des municipalités du Québec* issues twelve months insurance contracts that are reviewed annually upon their renewal. Following the initial five-year period, if a Mutual Member wishes to withdraw, a twelve months advance notice must be provided to *La Mutuelle des municipalités du Québec*. These rules allow *La Mutuelle des municipalités du Québec* to invest substantially in risk management while also enabling it to acquire in-depth knowledge of each municipality being insured. Given its very high rate of market penetration, *La Mutuelle des municipalités du Québec* underwrites a limited number of new business annually in accordance with the standards of *La Mutuelle des municipalités du Québec* as well as prices in effect.

Moreover, *La Mutuelle des municipalités du Québec* has created two committees to oversee underwriting activities. The insurance technical committee reviews, on a weekly basis, the more complex applications submitted by brokers representing Mutual Members. This committee consists of management team as well as the president and chief executive officer. The committee reaches a decision regarding applications following their analysis. On another level, the Board of Directors' insurance committee, chaired by a Board member and composed of management team as well as external members, makes proposals to the Board of Directors on such matters as changes to the underwriting guide.

As mentioned previously, underwriting risk is also mitigated by a comprehensive risk management program. All Mutual Members undergo periodic inspections and new risks are inspected upon request to enable underwriters to make informed decisions.

19. Risk management related to financial instruments and insurance risk (cont'd)

Insurance risk (cont'd)

Claims settlement risk
The claims settlement risk is influenced by the frequency and seriousness of claims as well as by the uncertainty in estimating future claims payments.

Property – The largest claims relating to property insurance involve fires, water damage and natural risks such as storms, floods and earthquakes.

As most fires in municipal buildings are electrical in origin, *La Mutuelle des municipalités du Québec* has implemented a thermographic analysis program of electrical panels as well as a building inspection program. Furthermore, Mutual Members benefit from training in fire and premises safety.

Loss of income – Given the nature of Mutual Members' activities, loss of income is not a major concern for *La Mutuelle des municipalités du Québec*.

Civil liability and umbrella (Follow-form) liability – Civil liability claims often involve a bodily injury suffered on city property, in particular after falling on a sidewalk or having an accident while taking part in a recreational activity. Firefighting activities also result in a large number of claims. Due to climate change, environmental risks such as sewer backups and ditch overflows are likely to increase.

The general civil liability-related risks are mitigated by the risk management program. A prevention program for recreational and sport accidents is made available to Mutual Members to plan activities or the use of specialized equipment and to put in place risk mitigation measures. *La Mutuelle des municipalités du Québec* provides to its Mutual Members experts in risk management who go on site to assess the location, establish relevant standards and best practices or to provide training regarding matters involving high or particular risks. Where firefighting activities are concerned, municipalities that have a fire risk coverage diagram and that have put in place the measures in their implementation plan in accordance with the established timetable will be granted immunity under the *Fire Safety Act*. In addition, *La Mutuelle des municipalités du Québec* travels around the regions to support Mutual Members in implementing their diagram. *La Mutuelle des municipalités du Québec* also has put in place another program to inform municipalities on the application of the many legislative parameters relating to environmental matters.

Errors and omissions – Most claims relating to errors and omissions result from alleged errors relating to the issuance of permits or the awarding of a contract being contested by certain bidders. *La Mutuelle des municipalités du Québec* has developed a range of training activities given by internal experts or in collaboration with municipal associations.

Automobile – This risk is rather low since, in Quebec, automobile risk is limited to property. Bodily injuries are covered by government insurance.

19. Risk management related to financial instruments and insurance risk (cont'd)

Insurance risk (cont'd)

Claims settlement risk (cont'd)

Crime – Given the nature of Mutual Members' activities, theft is not a major concern for *La Mutuelle des municipalités du Québec*.

Boiler and machinery – Generally, the frequency of equipment breakdown claims is low. Furthermore, the risk is offset by the inspection program implemented pursuant to *An Act respecting pressure vessels* and by the regular inspections carried out on other insured property.

La Mutuelle des municipalités du Québec prepares many publications on risk management, which are emailed to Mutual Members, posted on its website, or included in specialized magazines for the municipal sector. Training activities are held annually in meeting rooms in most regions and via web conference so as to reach as many Mutual Members as possible.

Causes of uncertainty in estimating future claims payments

In addition to managing the underwriting risk resulting from the selection and acceptance of risk to be insured, the reserve valuation risk is monitored specifically. Provisions for claims payable must be established as soon as the claim is reported. *La Mutuelle des municipalités du Québec* has set guidelines for reserves to which analysts refer daily. These reserves are valued individually for each case by the indemnification department. In addition to a regular follow-up, each file is reviewed annually by the department manager. Although the department analysts spare no effort in preparing reliable financial data, this is not an exact science and surpluses or deficiencies in provisions may occasionally occur in spite of the control methods put in place to limit them. Moreover, insurers will always have to face changes in legal decisions, which can sometimes complicate the outcome of disputes anticipated. Any loss of more than $100,000 is examined by the insurance technical committee and the executive committee.

Additional provisions for claims incurred but that have not yet been reported and provisions for claims that have arisen and been reported but for which inadequate provisions exist are also recognized.

Reinsurance

The severity of claims is limited by reinsurance treaties in which, as a result, *La Mutuelle des municipalités du Québec* will bear up to $497,500 on a net basis per event. Moreover, *La Mutuelle des municipalités du Québec* optimizes its reinsurance strategies to limit certain exposure.

Beyond this retention, excess, catastrophic and facultative loss treaties bring together the reinsurance capacity required for the operations of *La Mutuelle des municipalités du Québec*.

Reinsurance operations do not relieve *La Mutuelle des municipalités du Québec* of its obligations toward policyholders.

La Mutuelle des municipalités du Québec has treaties in all lines of business, which, beyond its retention, provide a limit of $15 million. It also has a catastrophe treaty for property and automobile insurance with a limit of $25 million in excess of $15 million.

19. Risk management related to financial instruments and insurance risk (cont'd)

Reinsurance (cont'd)

To select its reinsurers, *La Mutuelle des municipalités du Québec* applies certain criteria as defined by its risk management policy for reinsurance. This policy provides selection criteria for both the reinsurers and the reinsurance broker chosen to represent it.

Moreover, *La Mutuelle des municipalités du Québec* does not use non-traditional transferred reinsurance treaties such as obligations in the event of a disaster.

20. Compensation of key management personnel

Compensation of key management personnel, i.e., the directors and executive committee members, are detailed in the table below:

	2015	2014
	$	$
SHORT-TERM BENEFITS		
Executive committee	**1,106,743**	1,030,444
Director's attendance fees	**57,141**	62,941

21. Additional information to the statement of comprehensive income

Risk management expenses for Mutual Members are comprised of the following:

	2015	2014
	$	$
Risk management advisors	546,079	471,146
Risk management events	201,456	183,083
Professional fees	153,608	143,811
Travel expenses	112,968	93,275
Relations with Mutual Members	38,207	50,380
	1,052,318	941,695

21. Additional information to the statement of comprehensive income (cont'd)

Operating expenses are comprised of the following:

	2015	2014
	$	$
Salaries and corporate fringe benefits	1,870,131	1,764,834
Rent and administrative expenses	253,357	277,847
IT service expenses	374,631	242,231
Communication & public relations activities	219,063	231,273
Professional fees	187,187	178,952
Business partnerships	104,463	84,064
Committee expenses	68,516	71,266
Travel expenses	101,503	70,450
Dues and subscriptions	52,812	45,942
Representation expenses	45,354	40,808
Depreciation of fixed assets (Note 8)	86,685	82,203
Amortization of intangible assets (Note 9)	190,158	165,774
	3,553,860	3,255,644

22. Comparative information

Certain comparative information has been reclassified to conform with the current year's presentation.