

## Management Discussion and Analysis Report – Q3 of 2021

### Overview

Hamilton Township Mutual Insurance Company was formed in 1898. We operate under a trade name of HTM Insurance Company. Our office is in Cobourg, Ontario and we are licensed in the proving of Ontario to write property and casualty insurance. Our license also includes drones and limited accident according to the business plans filed with FSRA. Most of our business is within a two hour radius of the company through brokers (90%) and agents. We have a staff of about 40 and a board of directors of 9 local policyholders. We will write approximately \$36 million in premium in 2021.

### Executive Summary

The third quarter has seen underwriting profits increased to 7 million. October has added a few hundred thousand more in underwriting profit. Premium growth remains poor at 4% with new policy growth just under 1%. Auto is the drag on our growth targets. A larger barn fire caused the farm business line to slip over 30% on a pure gross loss ratio basis (no IBNR, internal adjusting expenses). With input from staff and a management/board strategic planning session, we have drafted a new business plan for the next three to five years. The plan will be ratified at the December meeting.

We had a serious issue during the quarter as well, and that was a breach in our system. I will go into detail on the breach in this report.

### Breach

On the 10<sup>th</sup> of September, I received an email from our VP Finance indicating that we had suffered a breach in our system. After cutting our system off from the outside world, we called our cyber insurers immediately. They assigned a team of experts to investigate. In summary, a cyber-criminal got access to our system in August through a vulnerability in Microsoft Outlook. Our Outlook server was scheduled to be shut down and upgraded on Saturday the 11<sup>th</sup>. On September 10<sup>th</sup>, the cyber-criminals loaded a program on our server and started extracting files to a 3<sup>rd</sup> party server. Fortunately we have an appliance called “Dark Trace” that detected the download and alerted the company. However, the process of being alerted, investigated and to shut the system down takes time. About 10GB of information was extracted which represents 3% of our server files. Our cyber investigators looked at our system and determined the vulnerability that caused the issue. They removed malicious software from our system and gave us a plan to open up our system safely to get us back in business. They indicated if we had not interrupted the process, the majority of our files would have been copied and everything on our servers would have been encrypted. During their investigation, they found the software tool the cyber-criminals were using. Because we had cut them off mid-stream, they left the destination source of the extracted files along with the login credentials to the 3<sup>rd</sup> party server. Our cyber investigators used that knowledge to log in to the 3<sup>rd</sup> party server and grab a list of every file they took. After determining that a portion of the files would have private information in them, it was determined that the best approach was to delete the files off the cyber-criminals server. Further, they viewed the logs and tested whether the logs would create a record if the files were copied from that system a second time. The log showed no indications the files were copied a further time and testing the server by copying files showed a log would have been created.

In consultation with breach counsel and the cyber insurance team, we don’t believe there is any threat due to the breach. We are finishing up the review of the files, our system has been patched to the best extent possible and multi-factor authentication was implemented (it was already planned for 2021). There was no contact or ransom demand from the cyber-criminals.

## Analysis of Operating Results

The strength in our balance sheet has continued through the 3<sup>rd</sup> quarter of 2021. Total assets are up over 10% and that is a function of cash provided by profitable operations. Outstanding claims have held steady and UEPs are up due to increase in premium revenue. One notable difference is in prepaid expenses and that is just timing of when we paid items this year versus last. While our income tax expense is higher in 2021, our installments were higher because of 2020's good year. This results in our liabilities for taxes being less than 2020. Overall, surplus has improved by 16.4% over 2020.

### *Balance Sheet as at September 30, 2021*

	<b>2021</b>	<b>2020</b>	<b>% of Change</b>
Cash & Investments	59,887	53,523	11.9%
Accounts receivable	9,431	9,139	3.2%
Reinsurance	7,088	7,149	(0.9%)
Broker Acquisition	303	416	(27.2%)
Building & Equipment	7,184	7,514	(4.4%)
Other Assets	<u>5,041</u>	<u>3,979</u>	<u>26.7%</u>
<b>Total Assets</b>	<b><u>\$88,934</u></b>	<b><u>\$81,720</u></b>	<b>8.8%</b>
Accounts Payable	470	509	(7.7%)
Due to Brokers	1,034	923	12.0%
Outstanding Claims	24,581	24,185	1.6%
Taxes Due	982	1,364	(28.0%)
UEP & Other Liabilities	<u>18,186</u>	<u>17,217</u>	<u>5.6%</u>
<b>Total Liabilities</b>	<b><u>45,253</u></b>	<b><u>44,198</u></b>	<b>2.4%</b>
<b>Members' Surplus</b>	<b><u>43,681</u></b>	<b><u>37,522</u></b>	<b>16.4%</b>
	<b><u>\$88,934</u></b>	<b><u>\$81,720</u></b>	<b>8.8%</b>

Our budget (shown in dollars) for the balance sheet, shown below, is quite accurate, especially considering it is the first time we have done a balance sheet budget. Significant differences are in the area of claims and taxes as the underwriting profit was not anticipated. This translated into a higher surplus than anticipated. The only other notable difference is in the broker acquisition. This will take place in 2022, not 2021 as anticipated in the budget.

### *Balance Sheet as at September 30, 2021*

	2021	2021 B	% Off Budget
Cash & Investments	59,887,158	57,974,726	3.3%
Accounts receivable	9,431,126	9,296,296	1.5%
Reinsurance	7,088,742	7,605,915	(6.8%)
Broker Acquisition	302,533	1,391,033	(78.3%)
Building & Equipment	7,184,108	7,220,952	(0.5%)
Other Assets	<u>5,040,324</u>	<u>4,422,726</u>	<u>14.0%</u>
<b>Total Assets</b>	<b><u>88,933,991</u></b>	<b><u>87,911,649</u></b>	<b>1.2%</b>
Accounts Payable	470,118	514,836	(8.7%)
Due to Brokers	1,033,936	951,977	8.6%
Outstanding Claims	24,580,878	28,878,626	(14.9%)
Taxes Due	981,629	(257,606)	(481.1%)
UEP & Other Liabilities	<u>18,186,256</u>	<u>19,005,408</u>	<u>(4.3%)</u>
<b>Total Liabilities</b>	<b><u>45,252,818</u></b>	<b><u>49,093,240</u></b>	<b>(7.8%)</b>
<b>Members' Surplus</b>	<b><u>43,681,173</u></b>	<b><u>38,818,408</u></b>	<b>12.5%</b>
	<b><u>\$88,933,991</u></b>	<b><u>\$87,911,649</u></b>	<b>1.2%</b>

The change in UEP is due to the low premium growth in 2021 @ 3.8% compared to 2020 which was over 8% by this point. Investment income rose and fell during the quarter leaving YTD income in the same position as it was in June. Almost income shown below is earned income from interest and dividends.

## *Income Statement to September 30, 2021*

	2021	2020	<u>% of Change</u>	
Premiums	26,709	25,724	3.8%	
Reinsurance Premiums	3,169	3,219	(1.6%)	
Increase (Decrease) in UEP	<u>793</u>	<u>1,056</u>	<span style="color: red;">(24.9%)</span>	
<b>Net Premiums Earned</b>	22,747	21,449	6.1%	
Policy Interest / Charges	<u>371</u>	<u>350</u>	6.0%	% of EP
	<b><u>\$23,118</u></b>	<b><u>\$21,799</u></b>	6.1%	<b><u>2021</u></b>
Gross Claims & Adjusting Incurred	7,899	10,978	<span style="color: red;">(28.0%)</span>	34.7%
Reinsurance Recoveries	<u>731</u>	<u>1,478</u>	<span style="color: red;">(50.5%)</span>	3.2%
<b>Net Claims Incurred</b>	7,168	9,500	<span style="color: red;">(24.5%)</span>	<b>31.5%</b>
Policy Acquisition Expenses	5,282	4,922	7.3%	23.2%
All other Expenses	<u>3,583</u>	<u>3,831</u>	(6.5%)	15.8%
<b>General Expenses</b>	8,865	8,753	1.3%	<b>39.0%</b>
<b>Underwriting Profit / (Loss)</b>	<b>\$7,085</b>	<b>\$3,546</b>	<span style="color: red;">99.8%</span>	<b>70.5%</b>
Investment Income	969	2,416	<span style="color: red;">(59.9%)</span>	
Income Tax Expense	<u>2,014</u>	<u>1,601</u>	25.8%	
<b>Net Profit / (Loss)</b>	<b><u>\$6,040</u></b>	<b><u>\$4,361</u></b>	<span style="color: red;">38.5%</span>	

Below compares the 2021 figures to our budget (in dollars). Reinsurance costs were overstated due to the projected premiums being off. Claims, as previously noted, are not at all typical for this period. Our budget anticipated a more normal year. This translates into a much higher underwriting profit and affects taxes.

## *Income Statement to September 30, 2021*

	2021	2021 B	<u>% Off Budget</u>		
Premiums	26,709,483	27,709,130	(3.6%)		
Reinsurance Premiums	3,169,463	3,856,177	(17.8%)		
Increase (Decrease) in UEP	<u>792,642</u>	<u>1,434,151</u>	(44.7%)		
<b>Net Premiums Earned</b>	22,747,378	22,418,802	1.5%		
Policy Interest / Charges	<u>371,163</u>	<u>373,531</u>	(0.6%)	<u>% of EP</u>	<u>% of EP</u>
	<b><u>\$23,118,542</u></b>	<b><u>\$22,792,333</u></b>	1.4%	<b><u>2021</u></b>	<b><u>2021 B</u></b>
Gross Claims & Adjusting Incurred	7,899,445	15,105,276	(47.7%)	34.7%	67.4%
Reinsurance Recoveries	<u>731,477</u>	<u>2,025,000</u>	(63.9%)	3.2%	9.0%
<b>Net Claims Incurred</b>	7,167,968	13,080,276	(45.2%)	<b>31.5%</b>	<b>58.3%</b>
Policy Acquisition Expenses	5,282,081	5,607,241	(5.8%)	23.2%	25.0%
All other Expenses	<u>3,583,901</u>	<u>3,534,516</u>	1.4%	15.8%	15.8%
<b>General Expenses</b>	8,865,982	9,141,757	(3.0%)	<b>39.0%</b>	<b>40.8%</b>
<b>Underwriting Profit / (Loss)</b>	<b>\$7,084,592</b>	<b>\$570,301</b>	<b>1142.3%</b>	<b>70.5%</b>	<b>99.1%</b>
Investment Income	969,922	1,000,424	(3.0%)		
Income Tax Expense	<u>2,013,700</u>	<u>392,681</u>	412.8%		
<b>Net Profit / (Loss)</b>	<b><u>\$6,040,813</u></b>	<b><u>\$1,178,043</u></b>	<b>412.8%</b>		

## Claims

Claims counts for the year are down across the board with the exception of residential. We have had two large fire losses (just under \$600,000 and a \$1.2M horse barn). Typically, we would have 5 or 6 large losses in a nine month period. You can see from our budget that anticipated claims are much higher. Even 2020 was a significant improvement over the “normal” year.

### **Gross Claims (Year-to-Date)**

Claims Count by Policy Class

Policy Class	Current	Prior	Change #	Change %	Budget	Off Budget #	Off Budget %
Auto	236	271	(35)	(12.9%)	361	(125)	(34.6%)
Commercial	27	27	0	0.0%	32	(5)	(15.6%)
Farm	66	89	(23)	(25.8%)	113	(47)	(41.6%)
Residential	177	167	10	6.0%	286	(109)	(38.1%)
<b>Total</b>	<b>506</b>	<b>554</b>	<b>(48)</b>	<b>(8.7%)</b>	<b>792</b>	<b>(286)</b>	<b>(36.1%)</b>

You can see from the chart below, significant improvements over 2020, which were better than previous years' results.

### **Gross Claims (Year-to-Date)**

Claims Incurred by Policy Class

Policy Class	Current	Prior	Change #	Change %	Budget	Off Budget \$	Off Budget %
Auto	1,505,071	3,203,307	(1,698,236)	(53.0%)	3,802,319	(2,297,248)	(60.4%)
Commercial	682,947	742,887	(59,940)	(8.1%)	1,076,739	(393,792)	(36.6%)
Farm	2,106,883	1,593,448	513,435	32.2%	3,323,833	(1,216,950)	(36.6%)
Residential	3,232,988	7,098,420	(3,865,432)	(54.5%)	8,368,826	(5,135,838)	(61.4%)
<b>Total</b>	<b>7,527,889</b>	<b>12,638,062</b>	<b>(5,110,173)</b>	<b>(40.4%)</b>	<b>16,571,717</b>	<b>(9,043,828)</b>	<b>(54.6%)</b>

We monitor our claims reserves closely and analyze the impact of prior year reserves on current year claims. In addition, from an accounting standpoint, an actuary provides us with IBNR calculations and during the year, we add \$30,000 per month in net IBNR to cover potential year end changes. The chart below shows the impact of claims that occurred in 2020 and prior on the current year results. While the impact is not insignificant, the underwriting profit of HTM to September is still well above normal, even if this improvement in reserve did not occur.

## Gross Claims Incurred (Year-to-Date)

By Class showing the effect of Claims Activity for prior years

Policy Class	2021 Claims Incurred	Prior Year Claims Incurred	Total Incurred	% Impact of Prior Year Claims
Auto	2,085,006	(579,935)	1,505,071	27.8%
Commercial	658,787	24,160	682,947	3.7%
Farm	2,716,535	(609,652)	2,106,883	22.4%
Residential	3,151,845	81,143	3,232,988	2.6%
<b>Totals</b>	<b>8,612,173</b>	<b>(1,084,284)</b>	<b>7,527,889</b>	<b>12.6%</b>

### Expense Ratio

The expense ratio dropped below 40%. This is the result of some net overall growth in excess of expense spending on the general expense side. Part of this reduced expense is due to the current pandemic environment. Travel and convention have all been significantly reduced. There are no areas of our expense that have any change worth noting. Most are common inflation or in some cases timing between one year and the next.

## Investments

As mention above investment income was down from the prior year in all areas except dividend income. Other than the market value, these are not significant changes and are not due to any changes in investment philosophy or policy change. Our investments are handled by a single firm and they report directly to the board twice per year. The board reviews the investment policy annually and did not make any changes during the last review in 2020. Investment performance is looked at over several periods and compared to industry benchmarks by major category. We also consider the comparison to the mutual system provided to us by the FRC. Our next investment review is November.

The table below are our targets and benchmarks for each class. Our investment advisor provides us with a report showing any violations to the policy. Getting outside our policy is usually caused by timing of sales and purchases affecting temporary cash position or a drop in the credit rate of a bond, falling below our threshold and the timing of the sale of that bond.

<b>Asset Class</b>	<b>Min</b>	<b>Target</b>	<b>Max</b>	<b>Benchmark</b>
Cash & Short Term Securities	0%	5%	10%	FTSE TMX Canada 60 Day T-Bill Index
Fixed Income	55%	65%	85%	FTSE TMX Canada Short-Mid Blend Index
Total Equities	10%	25%	30%	
Canadian Equities	10%	20%	30%	S&P/TSX Composite Index
U.S. Equities	0%	5%	10%	S&P 500 Index (CS)
International Equities	0%	0%	0%	MSCI EAFE Index (C\$)
Alternative Investments	0%	5%	10%	FTSE TMX 91-Day T-Bill Index + 5%

	<b>2020</b>	<b>2021</b>	<b>% off Prior</b>	<b>2021 B</b>	<b>% off Budget</b>
Investment Interest Earned	531,707	517,445	-2.7%	497,418	4.0%
Dividend Income Earned	56,472	465,290	723.9%	13,417	3367.9%
Gain or Loss on Sale of Investments	372,487	172,794	-53.6%	452,089	-61.8%
Change in Market Value Investments	1,566,579	(47,604)	-103.0%	150,000	-131.7%
Loss/Gain on Disposal of Assets	0	0	0.0%	0	0.0%
Portfolio Management Fees	<u>111,372</u>	<u>138,004</u>	23.9%	<u>112,500</u>	22.7%
	<b>2,415,873</b>	<b>969,922</b>	<b>-59.9%</b>	<b>1,000,424</b>	<b>-3.0%</b>

## Significant Changes

There have not been any significant changes to the organization in the last quarter other than a very unusual profitable 1<sup>st</sup> half of the year.

## Significant Risks

### **Insurance**

There has been no significant changes to our risk profile or risk appetite.

### **Cyber**

This issue has been outlined in the report above. Our system has been improved due to the breach, however it should be noted that our cyber experts gave our system a passing grade even before the changes we made after the breach.



## Staff

No senior staff changes have been made in the last quarter.

## Technology

The company has migrated to Cognition+ for all lines of business in the underwriting department. The last few months in underwriting has seen improved productivity as our knowledge of the system grows. The migration to claims starts with a kick-off meeting on the 22<sup>nd</sup> of November.

## Compliance

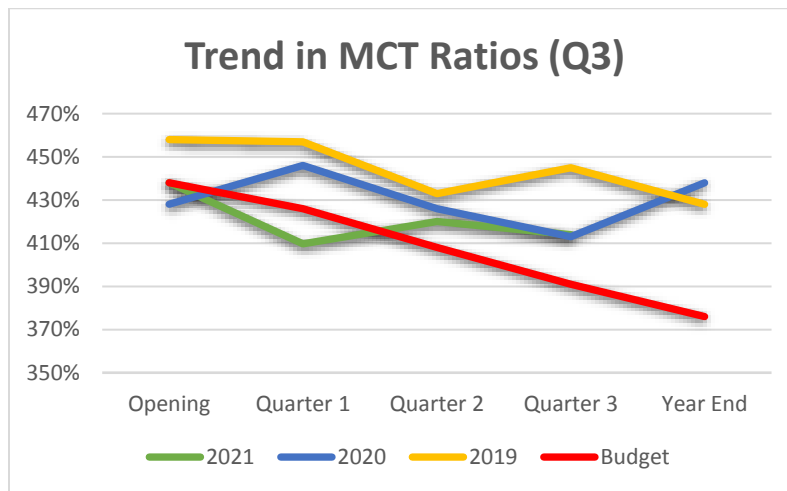
There are no known compliance issues at this time.

## Succession

We have no succession issues at this time. Two directors have retired and were replaced. The new directors are Trish Baird and Susan Treverton. These two appointments add further diversity to the board as well as a closer balance when it comes to gender equality.

## MCT

The ratio dipped slightly to 414% which is on par with 2020. The MCT chart is shown below with Budget in red. The reason for the budget MCT to look this way was in anticipation of continued premium growth in the 8% range and a small underwriting profit. The positive financial results to September 2021, with slow premium growth substantial underwriting profit has helped maintain the ratio.



## Other

We were deeply saddened by the loss of our AB adjuster, Brandon Watt, who passed away at the young age of 34, leaving a wife and two young children. He will be sorely missed by everyone here.

Respectfully submitted,

**Alec Harmer, CIP**  
President/CEO