

DEFINITY FINANCIAL CORPORATION

**CONDENSED INTERIM CONSOLIDATED
FINANCIAL STATEMENTS (UNAUDITED)**

FOR THE FIRST QUARTER ENDED
MARCH 31, 2023

DEFINITY FINANCIAL CORPORATION

CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

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DEFINITY FINANCIAL CORPORATION

INTERIM CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(in millions of dollars)

		As at		
	Notes	March 31, 2023	December 31, 2022 Restated	January 1, 2022 Restated
ASSETS				
Cash and cash equivalents		\$ 164.2	\$ 200.5	\$ 387.3
Restricted cash		286.7	302.1	110.8
Investments	6	4,881.5	4,897.2	5,364.9
Income taxes receivable		45.8	81.7	0.2
Reinsurance contract assets	7	315.0	305.1	238.4
Property and equipment		82.8	83.8	57.0
Deferred income tax assets		22.5	25.2	23.3
Goodwill and intangible assets		771.1	771.6	219.7
Other assets	9	169.9	152.5	136.3
		\$ 6,739.5	\$ 6,819.7	\$ 6,537.9
LIABILITIES AND EQUITY				
Insurance contract liabilities	7	\$ 3,463.6	\$ 3,577.7	\$ 3,668.9
Accounts payable and other liabilities	10	109.1	139.0	130.9
Income taxes payable		0.6	-	55.6
Deferred income tax liabilities		94.6	103.5	17.3
Demand loans		38.1	39.1	-
Demutualization amounts outstanding		286.7	302.1	110.8
		3,992.7	4,161.4	3,983.5
EQUITY				
Share capital	11	2,281.6	2,254.2	2,307.8
Contributed surplus	13	24.4	40.2	19.3
Retained earnings		362.1	287.8	220.8
Accumulated other comprehensive (loss) income		(30.9)	(32.4)	6.5
Equity attributable to common shareholders		2,637.2	2,549.8	2,554.4
Non-controlling interests		109.6	108.5	-
Total equity		2,746.8	2,658.3	2,554.4
		\$ 6,739.5	\$ 6,819.7	\$ 6,537.9

See accompanying notes.

DEFINITY FINANCIAL CORPORATION

INTERIM CONSOLIDATED STATEMENTS OF INCOME (LOSS) (UNAUDITED)

FOR THE THREE MONTHS ENDED MARCH 31

(in millions of dollars)

	Notes	2023	2022 Restated
Insurance revenue	7	\$ 907.5	\$ 814.3
Insurance service expenses	7,15	(782.3)	(664.2)
Net expenses from reinsurance contracts held	7,15	(31.3)	(34.1)
Insurance service result		93.9	116.0
Net investment income	6	41.0	25.8
Recognized gains (losses) on FVTPL investments	6	91.7	(197.8)
Investment income (loss)		132.7	(172.0)
Finance (expenses) income from insurance contracts issued	7	(64.5)	52.7
Finance income (expenses) from reinsurance contracts held	7	5.6	(3.2)
Net insurance financial result		(58.9)	49.5
Net insurance and investment result		167.7	(6.5)
Distribution revenues		25.5	-
Other (expenses) income	15	(60.0)	(41.0)
Income (loss) before income taxes		133.2	(47.5)
Income tax (expense) recovery	8	(31.1)	14.9
Net income (loss)		\$ 102.1	\$ (32.6)
Net income (loss) attributable to:			
Common shareholders		100.9	(32.6)
Non-controlling interests		1.2	-
Earnings (loss) per common share (in dollars)	12		
Basic		\$ 0.88	\$ (0.28)
Diluted		\$ 0.87	\$ (0.28)
Weighted average common shares outstanding (millions)	12		
Basic		114.7	115.9
Diluted		116.4	117.5
Dividends paid per common share (in dollars)		\$ 0.138	\$ 0.175

See accompanying notes

DEFINITY FINANCIAL CORPORATION

INTERIM CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (UNAUDITED)

FOR THE THREE MONTHS ENDED MARCH 31

(in millions of dollars)

	Notes	2023	2022 Restated
Net income (loss)		\$ 102.1	\$ (32.6)
<hr/>			
Item that may be reclassified subsequently to net income (loss):			
Foreign exchange loss on investments in associates		-	(0.4)
		-	(0.4)
<hr/>			
Items that will not be reclassified subsequently to net income (loss):			
Recognized gains (losses) on FVTOCI investments	6	2.1	(4.5)
Post-employment benefit obligation gain	14	1.6	17.5
Income tax expense		(1.0)	(3.4)
		2.7	9.6
Other comprehensive income		2.7	9.2
Comprehensive income (loss)		\$ 104.8	\$ (23.4)
<hr/>			
Comprehensive income (loss) attributable to:			
Common shareholders		103.6	(23.4)
Non-controlling interests		1.2	-

See accompanying notes

DEFINITY FINANCIAL CORPORATION

INTERIM CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY (UNAUDITED)

FOR THE THREE MONTHS ENDED MARCH 31

(in millions of dollars)

2023							
	Notes	Share capital	Contributed surplus	Retained earnings	Accumulated other comprehensive loss	Equity attributable to non-controlling interests	Total equity
Balance, December 31, 2022 (restated)	3	\$ 2,254.2	\$ 40.2	\$ 287.8	\$ (32.4)	\$ 108.5	\$ 2,658.3
Net income attributable to common shareholders		-	-	100.9	-	-	100.9
Net income attributable to non-controlling interests		-	-	-	-	1.2	1.2
Other comprehensive income		-	-	1.2 ¹	1.5	-	2.7
Total comprehensive income		-	-	102.1	1.5	1.2	104.8
Equity-settled share-based compensation	13	32.3	(15.8)	(12.0)	-	-	4.5
Shares purchased and held in trust	11	(4.9)	-	-	-	-	(4.9)
Dividends to common shareholders		-	-	(15.8)	-	-	(15.8)
Dividends to non-controlling interests		-	-	-	-	(0.1)	(0.1)
Balance, March 31, 2023		\$ 2,281.6	\$ 24.4	\$ 362.1	\$ (30.9) ²	\$ 109.6	\$ 2,746.8

2022 Restated							
	Notes	Share capital	Contributed surplus	Retained earnings	Accumulated other comprehensive income		Total equity
Balance, January 1, 2022 (restated)	3	\$ 2,307.8	\$ 19.3	\$ 220.8	\$ 6.5	\$	2,554.4
Net loss attributable to common shareholders (restated)		-	-	(32.6)	-	-	(32.6)
Other comprehensive income (loss) (restated)		-	-	12.9 ¹	(3.7)	-	9.2
Total comprehensive loss (restated)		-	-	(19.7)	(3.7)	-	(23.4)
Equity-settled share-based compensation	13	-	4.3	-	-	-	4.3
Shares purchased and held in trust	11	(8.1)	-	-	-	-	(8.1)
Dividends to common shareholders		-	-	(20.3)	-	-	(20.3)
Balance, March 31, 2022 (restated)		\$ 2,299.7	\$ 23.6	\$ 180.8	\$ 2.8 ²	\$	2,506.9

¹ Actuarial gains for the post-employment benefit obligation recognized in retained earnings (net of income tax expense of \$0.4 million (March 31, 2022: \$4.6 million)).

² Included in accumulated other comprehensive (loss) income ("AOCI") is \$5.7 million (December 31, 2022: \$5.7 million) related to the cumulative foreign exchange gain on investments in associates.

DEFINITY FINANCIAL CORPORATION

INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

FOR THE THREE MONTHS ENDED MARCH 31

(in millions of dollars)

	Notes	2023	2022
Operating activities:			
Income (loss) before income taxes		\$ 133.2	\$ (47.5)
Income taxes paid		(3.5)	(89.1)
Adjustments for non-cash items	16	(67.2)	219.9
Changes in operating assets and liabilities	16	(153.1)	(176.7)
Net cash used in operating activities		(90.6)	(93.4)
Investing activities:			
Investments purchased		(1,792.8)	(1,968.5)
Investments sold, redeemed, or matured		1,905.0	1,987.6
Commercial loans advanced		-	(5.0)
Commercial loans collected		0.4	0.9
Purchases of intangible assets and property and equipment		(28.3)	(28.0)
Business acquisitions, net of cash acquired		(8.2)	-
Net cash provided by (used in) investing activities		76.1	(13.0)
Financing activities:			
Dividends paid on common shares		(15.8)	(20.3)
Dividends paid to non-controlling interests		(0.1)	-
Common shares purchased and held in trust	11	(4.9)	(8.1)
Change in demutualization amounts outstanding		(15.4)	6.0
Repayment of demand loans		(1.0)	-
Net cash used in financing activities		(37.2)	(22.4)
Cash and cash equivalents, and restricted cash:			
Net decrease during the period		(51.7)	(128.8)
Balance, beginning of the period		502.6	498.1
Balance, end of the period		\$ 450.9	\$ 369.3
Cash		\$ 42.7	\$ 100.5
Cash equivalents		121.5	152.0
Total cash and cash equivalents		\$ 164.2	\$ 252.5
Restricted cash		286.7	116.8
Total cash and cash equivalents, and restricted cash		\$ 450.9	\$ 369.3

See accompanying notes.

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

1. NATURE OF OPERATIONS

Definity Financial Corporation (the “Company”), through its subsidiaries, offers property and casualty (“P&C”) insurance in Canada. The Company was incorporated on June 30, 2021 and is domiciled in Canada. Its registered office and principal place of business is 111 Westmount Road South, Waterloo, Ontario, Canada. The Company became the parent company of Definity Insurance Company (“Definity Insurance”), upon completion of the conversion of Definity Insurance from a mutual company to a company with share capital pursuant to the *Insurance Companies Act* (Canada) and regulations thereunder, a process known as “demutualization”.

These condensed interim consolidated financial statements (“interim financial statements”) were authorized for issuance and approved by the Company’s Board of Directors on May 11, 2023.

2. BASIS OF PREPARATION

The interim financial statements are prepared in accordance with International Accounting Standard (“IAS”) 34 – *Interim Financial Reporting* (“IAS 34”). Accordingly, certain information and disclosures normally included in annual financial statements prepared in accordance with International Financial Reporting Standards (“IFRS”), as issued by the International Accounting Standards Board (“IASB”), have been omitted or condensed. The preparation of interim financial statements in accordance with IAS 34 requires the use of certain critical accounting estimates. It also requires management to exercise judgment in applying the Company’s accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements have been set out in note 5 of the Company’s audited consolidated financial statements for the year ended December 31, 2022, excluding the changes arising from the adoption of IFRS 9 – *Financial Instruments* (“IFRS 9”) and IFRS 17 – *Insurance Contracts* (“IFRS 17”) which are discussed in note 5 of the Company’s interim financial statements. These interim financial statements should be read in conjunction with the Company’s audited consolidated financial statements for the year ended December 31, 2022.

These interim financial statements have been prepared on a historical cost basis, except for those financial instruments, including those held in the defined benefit pension plan, that have been measured at fair value, and liabilities for incurred claims, assets for incurred claims, and benefit plan obligations which are valued on a discounted basis in accordance with accepted actuarial practice.

The financial statements of the subsidiaries and material associates are prepared for the same reporting period as the Company. Where necessary, the accounting policies of subsidiaries and associates are adjusted to align with those of the Company. The interim financial statements include the accounts of Definity Financial Corporation and its subsidiaries, Definity Insurance, Waterloo Insurance Company, Perth Insurance Company, The Missisquoi Insurance Company, Sonnet Insurance Company, Petline Insurance Company (“Petline”), Westmount Financial Inc., McDougall Insurance Brokers Limited, McConville Omni Insurance Brokers Ltd., T.G Colley & Sons Limited, Integrisure Group Insurance Inc., Family Insurance Solutions Inc., and TEIG Investment Partnership (which holds the investment portfolio for all insurance companies in the group, except for the Company and Petline). Each of these subsidiaries operate and are incorporated or established in Canada. The Company has appointed a trust company as its administrative agent and record keeper of its share-based compensation plans.

The Company’s non-controlling interest investments in companies subject to significant influence are accounted for using the equity method and are included in “Other assets”. Under the equity method, the original cost of the investments is increased by the comprehensive income of the non-controlling interest since acquisition and reduced by any dividends received. All intercompany transactions and balances have been eliminated on consolidation to the extent of the interest in the associate.

All amounts in the notes are shown in millions of Canadian dollars, unless otherwise stated.

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

3. ADOPTION OF NEW ACCOUNTING STANDARDS

The Company has applied IFRS 17 and IFRS 9 for the first time in these interim financial statements. IFRS 17 replaces IFRS 4 – *Insurance Contracts* (“IFRS 4”) and IFRS 9 replaces IAS 39 – *Financial Instruments: Recognition and Measurement* (“IAS 39”) for annual periods beginning on or after January 1, 2023.

These standards have brought significant changes to the accounting for insurance and reinsurance contracts, and financial instruments. The Company has restated comparative information for 2022 and presented a third consolidated balance sheet as at January 1, 2022. The nature of the changes in accounting policies resulting from the adoption of IFRS 17 and IFRS 9 is summarized below.

IFRS 17

In May 2017, the IASB issued IFRS 17. IFRS 17 establishes principles for the recognition, measurement, presentation, and disclosure of insurance contracts issued and reinsurance contracts held. There are two measurement methodologies under IFRS 17 that may be applicable to the Company, the general measurement model (“GMM”) and the premium allocation approach (“PAA”). The PAA is a simplified measurement model that can be applied to insurance contracts with coverage periods of one year or less (which is the coverage period of most P&C insurance contracts), or where the PAA approximates the GMM. Under IFRS 17, the Company’s insurance contracts issued and reinsurance contracts held are all eligible to be measured by applying the PAA.

(a) Changes to classification and measurement (IFRS 17)

The measurement principles of the PAA differ from the measurement under IFRS 4 in the following key areas:

Insurance contract liabilities	The sum of the liabilities for remaining coverage (“LRC”) and the liabilities for incurred claims (“LIC”).
Liabilities for remaining coverage	<p>The LRC consists of unearned premiums received less unamortized acquisition cash flows paid, plus a loss component for onerous contracts.</p> <p>Insurance acquisition cash flows: IFRS 17 broadened the costs eligible for deferral, which has resulted in an increase in the amount deferred, as compared to the deferred policy acquisition expenses recorded under IFRS 4.</p> <p>Onerous contracts: Where facts and circumstances indicate that a group of insurance contracts will be non-profitable at initial recognition, the Company performs analyses to determine if a group of contracts is onerous. For groups of contracts that are onerous, the Company recognizes a loss in net income (loss) for the expected net outflow, resulting in earlier recognition compared to IFRS 4. These losses are reversed to net income (loss) over the term of the contracts.</p>

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

3. ADOPTION OF NEW ACCOUNTING STANDARDS (continued)

(a) Changes to classification and measurement (IFRS 17) (continued)

Liabilities for incurred claims	<p>The LIC includes estimates of the Company’s obligation to pay claim liabilities and other incurred insurance expenses. Measurement of the LIC is determined on a discounted probability-weighted expected value basis and includes an explicit risk adjustment for non-financial risk.</p> <p>Risk adjustment: The measurement of claim liabilities includes an explicit risk adjustment for non-financial risk. The risk adjustment for non-financial risk is applied to the present value of the estimated future cash flows and reflects the uncertainty around the amount and timing of the cash flows as the Company fulfils insurance contracts. The risk adjustment replaces the provision for adverse deviation (“PfAD”) under IFRS 4. Changes in the risk adjustment impacts insurance service expenses.</p> <p>Discounting: Under IFRS 17, cash flows are discounted using risk-free yield curves adjusted to reasonably reflect the characteristics of the cash flows and the liquidity of the insurance contracts. The risk-free yield curves are adjusted by an illiquidity premium using a reference portfolio to reflect the liquidity characteristics of the insurance contracts. The selection of reference portfolios is based on market instruments that reflect the nature of the insurance contracts in terms of amount, timing, currency, and liquidity. In contrast to using a liquidity-adjusted risk-free rate, the impact of discounting under IFRS 4 was calculated using a rate derived from investment returns of the Company’s investment portfolio backing the claim liabilities. Under IFRS 17, the impact of discounting continues to be recorded by the Company entirely in net income (loss). The impact of discounting is included in “Insurance service expenses” and in “Finance (expenses) income from insurance contracts issued.”</p>
Reinsurance contract assets	The sum of the assets for remaining coverage (“ARC”) and the assets for incurred claims (“AIC”).
Assets for remaining coverage	Measurement of the ARC reflects unearned reinsurance premiums paid for reinsurance contracts held. The ARC is adjusted to include a loss-recovery component to reflect the expected recovery of onerous contract losses where such contracts reinsure onerous direct contracts.
Assets for incurred claims	Measurement of the AIC reflects estimates of claims recoverable from reinsurance contracts held and is determined on a discounted probability-weighted expected value basis and includes an explicit risk adjustment for non-financial risk. The risk adjustment is included in the interim consolidated statements of income (loss) in “Net expenses from reinsurance contracts held”. The impact of discounting is included in “Net expenses from reinsurance contracts held” and in “Finance income (expenses) from reinsurance contracts held.”

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

3. ADOPTION OF NEW ACCOUNTING STANDARDS (continued)

(a) Changes to classification and measurement (IFRS 17) (continued)

The Company's policies for classification and measurement of insurance and reinsurance contracts are explained in note 4.

(b) Changes to presentation and disclosure (IFRS 17)

The presentation of line items in the interim financial statements has changed significantly compared with the presentation under IFRS 4.

Insurance contract liabilities presented in the interim consolidated balance sheets consist of unearned premiums received, unamortized acquisition cash flows paid, loss component for onerous contracts, claim liabilities (including the impact of discounting and risk adjustment), and other related liabilities. Reinsurance contract assets are separately presented in the interim consolidated balance sheets and include amounts expected to be recovered from reinsurers and reinsurance premiums paid for future reinsurance coverage. The reclassification of amounts in the interim consolidated balance sheets has resulted in a reduction in the consolidated assets and liabilities of the Company.

IFRS 17 requires separate presentation of insurance revenue, insurance service expenses, income or expenses from reinsurance contracts held, and insurance finance income or expenses, which are further described below. Results from insurance contracts issued and reinsurance contracts held are presented separately in the interim consolidated statements of income (loss). Written premiums are no longer disclosed in the interim consolidated statements of income.

Insurance revenue	The Company allocates the expected premiums to each period based on the passage of time similar to IFRS 4. Other underwriting revenues, which consist of various customer service fees, are included in "Insurance revenue" in the interim consolidated statements of income (loss) under IFRS 17.
Insurance service expenses	Insurance service expenses include incurred claims and other incurred directly attributable expenses, amortization of insurance acquisition cash flows, changes that relate to past service (changes in fulfilment cash flows relating to the liabilities for incurred claims), and changes that relate to future service (losses on onerous groups of contracts and reversals of such losses). Costs that do not relate directly to the fulfilment of an insurance contract are included in "Other (expenses) income" in the interim consolidated statements of income (loss), whereas under IFRS 4 these costs were included within underwriting income.
Net expenses from reinsurance contracts held	Income and expenses from reinsurance contracts, other than insurance finance income or expenses, are presented on a net basis as "Net expenses from reinsurance contracts held" in the insurance service result in the interim consolidated statements of income (loss). Net expenses from reinsurance contracts held include revenue and expenses related to ceded business.
Insurance finance income or expenses	Insurance finance income or expenses comprise the change in the carrying amounts of the group of insurance and reinsurance contracts arising from the discounting impacts of the time value of money and the effect of financial risk.

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

3. ADOPTION OF NEW ACCOUNTING STANDARDS (continued)

(c) Transition (IFRS 17)

Changes in accounting policies resulting from the adoption of IFRS 17 have been applied using a full retrospective approach. Under the full retrospective approach, at January 1, 2022, the Company identified, recognized, and measured each group of insurance and reinsurance contracts as if IFRS 17 had always applied, derecognized any previously reported balances that would not have existed if IFRS 17 had always been applied, and recognized any resulting net difference in equity in the January 1, 2022 opening balance sheet, net of income taxes.

IFRS 9

In July 2014, the IASB issued the final version of IFRS 9, which reflects all phases of the financial instruments project. IFRS 9 sets out the requirements for recognizing and measuring financial assets, financial liabilities, and some contracts to buy or sell non-financial items. IFRS 9 was effective for annual periods beginning on or after January 1, 2018. An entity whose activities are predominantly connected with insurance was eligible to apply a temporary exemption to adopt IFRS 9 in conjunction with its adoption of IFRS 17. The Company chose to apply the temporary exemption from IFRS 9 to defer the application of IFRS 9 until the effective date of IFRS 17.

(a) Changes to classification and measurement (IFRS 9)

In December 2021, the IASB amended IFRS 17 to add a transition option for a “classification overlay” to address possible accounting mismatches between financial assets measured under IFRS 9 and insurance contract liabilities in the comparative information presented on initial application of IFRS 17. Applying the classification overlay, an entity is permitted to present comparative information for a financial asset as if the classification and measurement requirements in IFRS 9 had been applied to that financial asset. The Company has applied the classification overlay to all financial assets derecognized in the comparative period.

Under IFRS 9, financial instruments are classified as amortized cost, fair value through other comprehensive income (“FVTOCI”), or fair value through profit or loss (“FVTPL”). The determination of the appropriate classification is based upon the entity’s business model, contractual cash flow characteristics of the instrument, and the entity’s election, if any, on classification. Equity instruments are classified as FVTPL unless the entity qualifies and elects them as FVTOCI.

The Company assessed its short-term investments and bonds previously classified as available for sale (“AFS”) and FVTPL. These instruments met the solely payments of principal and interest (“SPPI”) criterion. Based on the Company’s assessment under IFRS 9, these assets have been measured at FVTPL. The majority of the Company’s preferred stocks, common stocks, and pooled funds that were previously measured as AFS under IAS 39 must be measured as FVTPL under IFRS 9. The preferred stocks classified as FVTPL are hybrid securities. The Company utilized the optional election to designate certain non-hybrid preferred stocks previously measured as AFS under IAS 39 as FVTOCI with realized and unrealized gains and losses presented directly and permanently in other comprehensive income (“OCI”). The Company assessed its commercial loans previously classified as loans and receivables (“L&R”) under IAS 39. These instruments did not meet the SPPI criterion, and as such are mandatorily measured at FVTPL under IFRS 9.

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

3. ADOPTION OF NEW ACCOUNTING STANDARDS (continued)

(a) Changes to classification and measurement (IFRS 9) (continued)

The following table sets out the Company's cash and cash equivalents and investments classifications under IFRS 9, the previous classification under IAS 39, and the impact on cash and cash equivalents and investments. A reconciliation between the carrying amounts under IAS 39 as at December 31, 2021 to the balances reported under IFRS 9 as at January 1, 2022 is as follows:

(in millions of dollars)

	IAS 39		IFRS 9		
	Classification	Amortized cost	Carrying amount	Re-classifications	Carrying amount
Cash and cash equivalents	L&R		\$ 387.3	\$ -	\$ 387.3
Short-term investments	AFS		41.3	(41.3)	-
	FVTPL	FVTPL	47.5	41.3	88.8
Bonds	AFS		2,141.8	(2,141.8)	-
	FVTPL	FVTPL	2,092.0	2,141.8	4,233.8
Preferred stocks	AFS		405.7	(405.7)	-
		FVTOCI		232.7	232.7
		FVTPL		173.0	173.0
Common stocks	AFS		570.5	(570.5)	-
		FVTPL		570.5	570.5
Pooled funds	AFS		42.7	(42.7)	-
		FVTPL		42.7	42.7
Commercial loans ¹	L&R		24.3	(24.3)	-
		FVTPL		23.4	23.4
Total cash and cash equivalents, and investments			\$ 5,753.1	\$ (0.9)	\$ 5,752.2

¹ Included in this amount is a fair value adjustment with respect to commercial loans of \$0.9 million.

The Company's classification and measurement of financial instruments is explained in note 4.

(b) Changes to presentation and disclosure (IFRS 9)

The transition to IFRS 9 has resulted in changes to the composition of gains and losses on investments between net income (loss) and OCI in the interim consolidated statements of income (loss). As more of the Company's investments are designated as FVTPL, unrealized gains and losses on these investments that previously were recorded in OCI will now be recorded in net income (loss). As a result, the Company expects there may be additional volatility in net income (loss). Unrealized losses on investments of \$94.7 million have been recognized in net income (loss) in the three months ended March 31, 2022 that were previously recognized in OCI. Realized gains on FVTOCI preferred stocks of \$0.7 million have been recognized in OCI in the three months ended March 31, 2022 that were previously recognized in net income (loss). Under IFRS 9, gains or losses on equity instruments classified as FVTOCI are not reclassified to profit and loss and are therefore no longer required to be reviewed for impairment.

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

3. ADOPTION OF NEW ACCOUNTING STANDARDS (continued)

(c) Transition (IFRS 9)

Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively. The Company has applied the classification overlay to all financial assets derecognized in the comparative period, and has restated the comparative period for the impacts of IFRS 9.

Impact of IFRS 17 and IFRS 9 transition adjustments on equity

The estimated effects of adopting IFRS 17 and IFRS 9 on retained (deficit) earnings and AOCI in the interim consolidated statements of changes in equity as at January 1, 2022 are as follows:

<i>(in millions of dollars)</i>	As at January 1, 2022	
	Retained (deficit) earnings	AOCI
Balance as at December 31, 2021, as previously reported	\$ (28.8)	\$ 98.0
IFRS 17 adjustments:		
Change from PfAD to risk adjustment	140.0	-
Difference in discounting under IFRS 17	28.0	-
Increased deferral of insurance acquisition cash flows	73.6	-
Establishment of onerous loss provision	(26.3)	-
Income tax impact on transition adjustments	(56.5)	-
Total IFRS 17 adjustments	158.8	-
IFRS 9 adjustments:		
Reclass AFS unrealized gains, excluding FVTOCI preferred stocks, from AOCI to retained (deficit) earnings	122.9	(122.9)
Fair value adjustment to commercial loans	(0.9)	-
Income tax impact on transition adjustments	(31.2)	31.4
Total IFRS 9 adjustments	90.8	(91.5)
Restated balance as at January 1, 2022	\$ 220.8	\$ 6.5

The estimated effects of adopting IFRS 17 and IFRS 9 on the interim consolidated balance sheet as at January 1, 2022 are as follows:

<i>(in millions of dollars)</i>	As at January 1, 2022		
	As previously reported	Impact of IFRS 17 and IFRS 9 adjustments	Restated
Total assets	\$ 7,891.4	\$ (1,353.5)	\$ 6,537.9
Total liabilities	5,495.1	(1,511.6)	3,983.5
Total equity	2,396.3	158.1	2,554.4

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NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

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3. ADOPTION OF NEW ACCOUNTING STANDARDS (continued)

The estimated effects of adopting IFRS 17 and IFRS 9 on the interim consolidated statements of changes in equity as at December 31, 2022 are as follows:

		2022 Restated					
	Notes	Share capital	Contributed surplus	Retained (deficit) earnings	Accumulated other comprehensive income (loss)	Equity attributable to non-controlling interests	Total equity
Balance, December 31, 2021, as previously reported		\$ 2,307.8	\$ 19.3	\$ (28.8)	\$ 98.0	\$ -	\$ 2,396.3
Impact of initial application of IFRS 17	3	-	-	158.8	-	-	158.8
Impact of initial application of IFRS 9	3	-	-	90.8	(91.5)	-	(0.7)
Restated balance at January 1, 2022		2,307.8	19.3	220.8	6.5	-	2,554.4
Net income attributable to common shareholders (restated)		-	-	110.9	-	-	110.9
Net income attributable to non-controlling interests		-	-	-	-	0.6	0.6
Other comprehensive income (loss) (restated)		-	-	19.4	(38.9)	-	(19.5)
Total comprehensive income (loss) (restated)		-	-	130.3	(38.9)	0.6	92.0
Equity-settled share-based compensation	13	-	20.9	-	-	-	20.9
Shares purchased and held in trust	11	(53.6)	-	-	-	-	(53.6)
Dividends to common shareholders		-	-	(63.3)	-	-	(63.3)
Non-controlling interests		-	-	-	-	107.9	107.9
Balance, December 31, 2022 (restated)		\$ 2,254.2	\$ 40.2	\$ 287.8	\$ (32.4)	\$ 108.5	\$ 2,658.3

4. ACCOUNTING POLICIES

The interim financial statements were prepared using the same accounting policies as disclosed in note 3 of the Company's audited consolidated financial statements for the year ended December 31, 2022, except for the accounting for insurance contracts and reinsurance contracts, and financial instruments due to the adoption of IFRS 17 and IFRS 9 as discussed in note 3. The accounting policies for insurance contracts and reinsurance contracts, and financial instruments are set out below.

(a) Insurance and reinsurance contracts

Insurance and reinsurance contracts classification

The Company issues insurance contracts in the normal course of business, under which it accepts significant insurance risk from its policyholders by agreeing to compensate the policyholder if a specified event (the insured event) with uncertain timing or amount occurs. Similarly, by purchasing reinsurance, the Company transfers significant insurance risk to the reinsurers. As a general guideline, the Company determines whether significant insurance risk has been transferred for insurance and reinsurance contracts by comparing whether significantly more would be paid or received if the insured event occurs, versus if the insured event did not occur.

The Company assesses its insurance products to determine whether they contain distinct components that must be segregated and accounted for separately from IFRS 17. Currently, the Company's products do not include any distinct components that require separation.

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

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4. ACCOUNTING POLICIES (continued)

(a) Insurance and reinsurance contracts (continued)

Level of aggregation

IFRS 17 requires entities to determine the level of aggregation for applying its requirements. The Company has identified a contract as the smallest 'unit'. However, the Company makes an evaluation of whether a series of contracts need to be treated together as one unit based on reasonable and supportable information, or whether a single contract contains components that need to be separated and treated as stand-alone contracts. The level of aggregation is determined firstly by dividing the business written into portfolios. Portfolios comprise groups of contracts with similar risks that are managed together.

IFRS 17 also requires that no group for level of aggregation purposes may contain contracts issued more than one year apart. Within each year of issue, portfolios of contracts are divided into three groups, as follows: (i) a group of contracts that are onerous at initial recognition (if any), (ii) a group of contracts that, at initial recognition, have no significant possibility of becoming onerous subsequently (if any), and (iii) a group of the remaining contracts in the portfolio (if any).

The Company considers facts and circumstances to identify whether a group of contracts is onerous at initial recognition based on estimated fulfilment cash flows, pricing information, results of similar contracts it has recognized, and the operating and regulatory environment. The profitability of groups of contracts is assessed by actuarial valuation models that take into consideration existing and new business. For contracts that are not onerous, an assessment is made at initial recognition whether there is significant possibility of becoming onerous subsequently by assessing the likelihood of changes in applicable facts and circumstances.

The Company divides portfolios of reinsurance contracts held applying the same principles set out above, except that the references to onerous contracts refer to contracts on which there is a net gain on initial recognition. For reinsurance contracts held, a group can comprise a single contract.

Contract boundary

The Company includes in the measurement of a group of insurance contracts all the future cash flows within the boundary of each contract in the group. Cash flows are within the boundary of an insurance contract if they arise from substantive rights and obligations that exist during the reporting period in which the Company can compel the policyholder to pay the premiums, or in which the Company has a substantive obligation to provide the policyholder with insurance contract services.

For groups of reinsurance contracts held, cash flows are within the contract boundary if they arise from substantive rights and obligations that exist during the reporting period in which:

- The Company is compelled to pay amounts to the reinsurer or the reinsurer has the right to compel premiums from the Company; or
- The Company has a substantive right to receive insurance contract services from the reinsurer or the reinsurer has the obligation to provide services to the Company.

Recognition

The Company recognizes groups of insurance contracts it issues from the earliest of the following:

- The beginning of the coverage period of the group of contracts (i.e., the period during which the Company provides services in respect of any premiums within the boundary of the contracts);
- The date when the first payment from a policyholder in the group becomes due; and
- For a group of onerous contracts, when the group becomes onerous.

Groups of contracts are established on initial recognition and their composition is not revised once all contracts have been added to the group.

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

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4. ACCOUNTING POLICIES (continued)

(a) Insurance and reinsurance contracts (continued)

The Company recognizes a group of reinsurance contracts held from the earlier of the following:

- The beginning of the coverage period of the group of reinsurance contracts held. However, the Company delays the recognition of a group of reinsurance contracts held that provide proportionate coverage until the date any underlying insurance contract is initially recognized, if that date is later than the beginning of the coverage period of the group of reinsurance contracts held; and
- The date the Company recognizes a group of insurance contracts as onerous if the Company entered into the related reinsurance contract held at or before that date.

Insurance contracts acquired in a business combination within the scope of IFRS 3 – *Business Combinations* or a portfolio transfer are accounted for as if they were entered into at the date of acquisition or transfer.

Insurance contracts – initial measurement

The Company applies the PAA to all the insurance contracts that it issues and reinsurance contracts that it holds. For contracts with coverage periods greater than one year, the Company reasonably expects that the measurement of the LRC (or the ARC with respect to reinsurance) for the group containing those contracts under the PAA does not differ materially from the measurement that would be produced applying the GMM. The Company does not have any significant contracts with coverage periods greater than one year.

The Company measures the carrying amount of the LRC as the premiums, if any, received at initial recognition minus any insurance acquisition cash flows paid at that date, and adjusted for any amount arising from the derecognition at that date of the asset recognized for insurance acquisition cash flows. The Company has elected to defer insurance acquisition cash flows over the contract period. The LRC is not adjusted for the time value of money as the premiums are due within one year of the coverage period.

Where facts and circumstances indicate that contracts are onerous, the Company will perform additional analyses to determine if a net outflow is expected from the contracts. Such onerous contracts are separately grouped from other contracts and the Company recognizes a loss in the interim consolidated statements of income (loss) in “Insurance service expenses” for the expected net outflow. A loss component is established by the Company within the LRC for such onerous group depicting the losses recognized.

Insurance contracts – subsequent measurement

The Company measures the carrying amount of the LRC at the end of each reporting period as the LRC at the beginning of the period plus any premiums received in the period and any amounts relating to the amortization of the insurance acquisition cash flows recognized as an expense in the reporting period, minus insurance acquisition cash flows paid and the amount recognized as insurance revenue for the services provided in the period. Where, during the coverage period, facts and circumstances indicate that a group of contracts is onerous, the Company recognizes a loss in the interim consolidated statements of income (loss) in “Insurance service expenses” for the expected net outflow.

The Company estimates the LIC (or the AIC with respect to reinsurance) as the fulfilment cash flows related to incurred claims and other incurred insurance expenses. The fulfilment cash flows incorporate, in an unbiased way, all reasonable and supportable information available without undue cost or effort about the amount, timing and uncertainty of those future cash flows, reflect current estimates from the perspective of the Company, and include an explicit adjustment for non-financial risk (the “risk adjustment”). The Company adjusts the LIC (or the AIC) for discounting.

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

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4. ACCOUNTING POLICIES (continued)**(a) Insurance and reinsurance contracts (continued)**

The claim liabilities included in the LIC consist of reserves for reported claims as determined on a case-by-case basis by claims adjusters and an actuarially determined provision for incurred but not reported claims. Measurement uncertainty exists due to internal and external factors that can substantially impact the ultimate settlement costs. Consequently, the Company reviews and re-evaluates claims and reserves on a regular basis and any resulting adjustments are included in "Insurance service expenses" in the interim consolidated statements of income (loss) in the period the adjustment is made. The claim liabilities are extinguished when the obligation to pay a claim expires, is discharged, or is cancelled.

Reinsurance contracts held – initial measurement

The Company measures its reinsurance assets for a group of reinsurance contracts that it holds on the same basis as insurance contracts that it issues. However, the measurement reflects the features of reinsurance contracts held that differ from insurance contracts issued, for example the generation of expenses or reduction in expenses rather than revenue.

Where the Company recognizes a loss on initial recognition of an onerous group of underlying insurance contracts or when further onerous underlying insurance contracts are added to a group, the Company establishes a loss-recovery component of the ARC for a group of reinsurance contracts held, if applicable, for the expected recovery of the losses.

The Company calculates the loss-recovery component by multiplying the loss component recognized on the underlying insurance contracts by the percentage of claims on the underlying insurance contracts the Company expects to recover from the group of reinsurance contracts held. In order to be included in the loss-recovery calculation, the group of reinsurance contracts covering the onerous underlying contracts must be entered into before or at the same time as the loss is recognized on the underlying insurance contracts. The Company uses a systematic and rational method to determine the portion of the loss component of the group of insurance contracts that relates to insurance contracts covered by the group of reinsurance contracts held.

Reinsurance contracts held – subsequent measurement

The subsequent measurement of reinsurance contracts held follows the same principles as those for insurance contracts issued and has been adapted to reflect the specific features of reinsurance contracts held.

Insurance acquisition cash flows

Insurance acquisition cash flows arise from the costs of selling, underwriting, and starting a group of insurance contracts (issued or expected to be issued) that are directly attributable to the portfolio of insurance contracts to which the group belongs. Insurance acquisition cash flows are capitalized and then expensed in the period over which the related premiums are recognized as income.

Insurance acquisition cash flows are allocated to groups of insurance contracts using a systematic and rational method and considering, in an unbiased way, all reasonable and supportable information that is available without undue cost or effort. If insurance acquisition cash flows are directly attributable to a group of insurance contracts, then they are allocated to that group. If insurance acquisition cash flows are directly attributable to a portfolio but not to a group of insurance contracts, then they are allocated to groups in the portfolio using a systematic and rational method.

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

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4. ACCOUNTING POLICIES (continued)

(a) Insurance and reinsurance contracts (continued)

Insurance contracts – modification and derecognition

The Company derecognizes insurance contracts when the rights and obligations relating to the contract are extinguished (that is, when the specified obligations in the contract expire or are discharged or cancelled). The Company also derecognizes a contract if its terms are modified in a way such that the modification results in a change in the measurement model or the applicable standard for measuring a component of the contract, substantially changes the contract boundary, or requires the modified contract to be included in a different group. In such cases, the Company derecognizes the initial contract and recognizes the modified contract as a new contract. When a modification is not treated as a derecognition, the Company recognizes amounts paid or received for the modification with the contract as an adjustment to the relevant LRC.

Presentation

The Company disaggregates the total amount recognized in the interim consolidated statements of income (loss) into an insurance service result (comprising insurance revenue, insurance service expenses, and net expenses from reinsurance contracts held) and insurance finance income or expenses.

Insurance revenue

The insurance revenue for the period is the amount of expected premiums allocated to the period. The Company allocates the expected premiums to each period based on the passage of time of the coverage period.

Insurance service expenses

Insurance service expenses arising from insurance contracts are recognized in the interim consolidated statements of income (loss) generally as they are incurred. Insurance service expenses include incurred claims and other incurred directly attributable expenses, amortization of insurance acquisition cash flows, changes that relate to past service (changes in fulfilment cash flows relating to the LIC), and changes that relate to future service (losses on onerous groups of contracts and reversals of such losses).

Net expenses from reinsurance contracts held

Included in net expenses from reinsurance contracts held on the interim consolidated statements of income (loss) are amounts expected to be recovered from reinsurers, and an allocation of the reinsurance premiums paid. The Company treats reinsurance cash flows that are contingent on claims on the underlying contracts as part of the claims that are expected to be reimbursed under the reinsurance contract held. Where reinsurance cash flows are not contingent on claims on the underlying contracts, they are included as part of the allocation of reinsurance premiums.

Insurance finance income or expenses

Insurance finance income or expenses comprise the change in the carrying amounts of the group of insurance and reinsurance contracts arising from the effects of the time value of money and changes in the time value of money, and the effect of financial risk and changes in financial risk. The Company includes all insurance and reinsurance finance income or expenses for the period in net income (loss).

Insurance contract liabilities and reinsurance contract assets

Insurance contract liabilities at the end of each reporting period is the sum of the LRC and the LIC. Reinsurance contract assets at the end of each reporting period is the sum of the ARC and the AIC.

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NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

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4. ACCOUNTING POLICIES (continued)

(b) Financial instruments including investments

The Company classifies all of its financial instruments based on the business model for managing the instruments and their contractual terms. The categories include the following:

- Amortized cost
- FVTPL
- FVTOCI

The Company determines its business model at the level that best reflects how it manages groups of financial assets to achieve its business objectives. The Company holds financial assets to generate returns and provide a capital base to provide for settlement of claims as they arise. The Company considers the timing, amount, and volatility of cash flow requirements to support insurance liabilities in determining the business model for the assets as well as the potential to maximize return for shareholders and future business development.

The Company's business model is not assessed on an instrument-by-instrument basis, but at a higher level of aggregated portfolios that is based on observable factors such as:

- How the performance of the business model and the financial assets held within that business model are evaluated and reported to the Company's key management personnel
- The risks that affect the performance of the business model (and the financial assets held within that business model) and, in particular, the way those risks are managed
- How managers of the business are compensated (for example, whether the compensation is based on the fair value of the assets managed or on the contractual cash flows collected)

The expected frequency, value, and timing of asset sales are also important aspects of the Company's assessment. The business model assessment is based on reasonably expected scenarios without taking 'worst case' or 'stress case' scenarios into account. If cash flows after initial recognition are realized in a way that is different from the Company's original expectations, the Company does not change the classification of the remaining financial assets held in that business model, but incorporates such information when assessing newly originated or newly purchased financial assets going forward.

As a second step of its classification process the Company assesses the contractual terms to identify whether they meet the SPPI test. The SPPI test involves assessing the contractual features of an instrument to determine if they give rise to cash flows that are consistent with a basic lending arrangement. Contractual cash flows are consistent with a basic lending arrangement if they represent cash flows that are SPPI on the principal amount outstanding. 'Principal' for the purpose of this test is defined as the fair value of the financial asset at initial recognition and may change over the life of the financial asset due to repayments of principal or amortization of the premium/discount. The most significant elements of interest within a debt arrangement are typically the consideration for the time value of money and credit risk. To make the SPPI assessment, the Company applies judgment and considers relevant factors.

The classification of financial instruments at initial recognition depends on their contractual terms and the Company's business model for managing the instruments. Financial assets purchased and sold, where the contract requires the asset to be delivered within an established timeframe, are recognized on a settlement-date basis. Transaction costs are expensed as incurred for FVTPL financial instruments. For equity instruments designated as FVTOCI, transaction costs are included in the instrument's carrying value.

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

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4. ACCOUNTING POLICIES (continued)**(b) Financial instruments including investments (continued)**

The fair value of a financial instrument on initial recognition is normally the transaction price, i.e., the fair value of the consideration given. Subsequent to initial recognition, the fair values are determined based on available information. The fair values of investments, excluding commercial loans, are based on quoted bid market prices where available or observable market inputs. The fair values of commercial loans and other financial instruments are obtained using discounted cash flow analysis at the current market interest rate for comparable financial instruments with similar terms and risks.

Financial instruments are no longer recognized when the rights to receive cash flows from the investments have expired or have been transferred and the Company has transferred substantially all the risks and rewards of ownership.

Financial assets measured at fair value through profit or loss

Financial assets in this category are those that are managed in a fair value business model, or that have been designated by management upon initial recognition, or are required to be measured at fair value under IFRS 9. This category includes equity investments whose cash flow characteristics fail the SPPI criterion and debt (including short-term) investments that are not held within a business model whose objective is either to collect contractual cash flows, or to both collect contractual cash flows and sell. This includes short-term investments, bonds, certain preferred stocks, common stocks, pooled funds, and commercial loans. Short-term investments consist of term deposits having original maturities of greater than ninety days and less than one year.

Changes in fair values as well as gains and losses on disposal of FVTPL financial instruments are recorded in "Recognized gains (losses) on FVTPL investments" in the interim consolidated statements of income (loss) with the related tax impact included in "Income tax (expense) recovery". Gains and losses on the sale of FVTPL financial instruments are calculated on an average cost basis. As changes in the fair value of FVTPL financial instruments are reflected directly within net income (loss) in the interim consolidated statements of income (loss), it is not necessary to record an impairment loss when there has been a decline in the fair value of FVTPL financial instruments.

Derivative financial instruments

Derivatives are financial instruments that have value derived from underlying interest rates or other financial instrument prices or indices. Derivatives are mandatorily measured at FVTPL because they do not give rise to cash flows that are SPPI. There are currently no derivatives designated as a hedge for accounting purposes. Derivatives are initially measured at fair value at the settlement date and subsequently remeasured at fair value at the end of each reporting date. The gains and losses arising from remeasuring the derivatives at fair value are recognized in "Recognized gains (losses) on FVTPL investments" in the interim consolidated statements of income (loss) with the related tax impact included in "Income tax (expense) recovery".

Equity instruments measured at fair value through other comprehensive income

The Company has opted to designate certain preferred stocks as FVTOCI without recycling of fair value changes to profit and loss as they are not held with the intent of short-term profit taking.

Other receivables/Other financial liabilities

Other receivables and other financial liabilities are initially recognized at fair value and subsequently measured at amortized cost using the effective interest rate method. When there is evidence of impairment, the value of these financial instruments is written down to the estimated net realizable value in the interim consolidated statements of income (loss).

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4. ACCOUNTING POLICIES (continued)

(b) Financial instruments including investments (continued)

Investment income recognition

Interest income is recognized on bonds and commercial loans on the accrual basis and includes the amortization of premiums and discounts over the life of the investment using the effective interest rate method. The treatment of recognized gains and losses on disposal of FVTPL and FVTOCI investments is discussed in “Financial assets measured at fair value through profit or loss” and “Equity instruments measured at fair value through other comprehensive income” above.

Dividend income is recognized on the ex-dividend date.

(c) Comparative figures

Certain comparative figures have been reclassified from statements previously presented to conform to the presentation of the current period’s interim financial statements.

5. SIGNIFICANT ACCOUNTING JUDGMENTS, ESTIMATES AND ASSUMPTIONS

The preparation of the Company’s interim financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities, and the disclosure of contingent assets and liabilities as at the reporting date, and the reported amounts of revenues and expenses during the period. Actual results could differ from these estimates. Although some variability is inherent in these estimates, management believes that the amounts provided are reasonable. The most complex and significant judgments, estimates and assumptions used in preparing the Company’s interim financial statements are discussed in note 5 of the Company’s audited consolidated financial statements for the year ended December 31, 2022, excluding the changes arising from the adoption of IFRS 9 and IFRS 17 discussed below.

Under IFRS 9, as changes in the fair value of FVTPL financial instruments are reflected directly within net income (loss), and changes in the fair value of FVTOCI financial instruments remain within OCI in the interim consolidated statements of comprehensive income (loss), it is no longer necessary to record an impairment loss when there has been a decline in the fair value of these financial instruments. As a result, impairment on investments is no longer a significant estimate.

Under IFRS 17, the Company has applied judgment in its determination of groups of contracts that are onerous on initial recognition and those that have no significant possibility of becoming onerous subsequently, and in the determination of cash flows that relate directly to the fulfilment of insurance contracts.

The Company has used estimates in the determination of the carrying amount of LIC. The Company is required by applicable insurance laws, regulations, and IFRS to establish liabilities for payment of claims and claims adjustment expenses that arise from the Company’s insurance products. These liabilities, which are included in the LIC, represent the expected ultimate cost to settle claims occurring prior to, but still outstanding as of, the reporting date. The estimates used in the valuation of claim liabilities are consistent with those under IFRS 4, except for discounting and risk adjustment, which are described below.

Discount rates

All cash flows are discounted using risk-free yield curves adjusted to reflect the characteristics of the cash flows and the liquidity of the associated insurance contracts. The Company generally determines the risk-free rates based on government of Canada zero-coupon bonds. The risk-free yield curves are adjusted by an illiquidity premium using a reference portfolio to reflect the liquidity characteristics of the associated insurance contracts. The selection of reference portfolios is based on market instruments that reasonably reflect the nature of the associated insurance contracts in terms of amount, timing, currency, and liquidity.

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5. SIGNIFICANT ACCOUNTING JUDGMENTS, ESTIMATES AND ASSUMPTIONS (continued)

Discount rates applied for discounting of future cash flows are listed below:

Discount rate	Insurance contracts issued / Reinsurance contracts held							
	Current Year +1	Current Year +2	Current Year +3	Current Year +4	Current Year +5	Current Year +6	Current Year +7	Current >7 years*
As at March 31, 2023	5.24%	4.77%	4.44%	4.23%	4.11%	4.07%	4.07%	4.28%
As at December 31, 2022	5.47%	5.29%	5.02%	4.81%	4.69%	4.64%	4.64%	4.77%

*Weighted average discount rate of the future discount rates for year 8 and beyond.

Risk adjustment for non-financial risk

The risk adjustment for non-financial risk is applied to the present value of the estimated future cash flows and reflects the uncertainty around the amount and timing of the cash flows as the Company fulfils insurance contracts. For reinsurance contracts held, the risk adjustment for non-financial risk represents the amount of risk being transferred by the Company to the reinsurer.

The Company has estimated the risk adjustment using a value-at-risk confidence level method to generally be in the range of the 75th to 80th percentile of the stochastically simulated results. This analysis has also been adjusted for correlation between different reserving segments, and the diversification between them.

The Company does not disaggregate changes in the risk adjustment for non-financial risk between the insurance service result and insurance finance income or expenses. All changes in the risk adjustment for non-financial risk are included in the insurance service result.

6. INVESTMENTS

(a) Investment income (loss) and balances

Total investment income (loss) recognized in profit or loss and OCI by financial instrument classification is as follows:

<i>(in millions of dollars)</i>	Three months ended March 31, 2023		
	FVTPL	FVTOCI	Total
Interest	\$ 34.3	\$ -	\$ 34.3
Dividends	5.2	3.2	8.4
Investment expenses	-	-	(1.7)
Net investment income	39.5	3.2	41.0
Realized losses on sale of FVTPL investments	(24.6)	-	(24.6)
Unrealized gains on FVTPL investments	116.3	-	116.3
Recognized gains on investments in net income (loss)	91.7	-	91.7
Realized losses on FVTOCI preferred stocks	-	(2.2)	(2.2)
Unrealized gains on FVTOCI preferred stocks	-	4.3	4.3
Recognized gains on investments in OCI	-	2.1	2.1
	\$ 131.2	\$ 5.3	\$ 134.8

DEFINITY FINANCIAL CORPORATION

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6. INVESTMENTS (continued)

(a) Investment income (loss) and balances (continued)

<i>(in millions of dollars)</i>	Three months ended March 31, 2022		
	FVTPL	FVTOCI	Total
Interest	\$ 19.7	\$ -	\$ 19.7
Dividends	5.0	2.7	7.7
Investment expenses	-	-	(1.6)
Net investment income	24.7	2.7	25.8
Realized losses on sale of FVTPL investments	(15.0)	-	(15.0)
Unrealized losses on FVTPL investments	(182.8)	-	(182.8)
Recognized losses on investments in net income (loss)	(197.8)	-	(197.8)
Realized gains on FVTOCI preferred stocks	-	0.7	0.7
Unrealized losses on FVTOCI preferred stocks	-	(5.2)	(5.2)
Recognized losses on investments in OCI	-	(4.5)	(4.5)
	\$ (173.1)	\$ (1.8)	\$ (176.5)

Dividends related to FVTOCI investments disposed of during the three months ended March 31, 2023 amounted to \$0.1 million (March 31, 2022: \$0.2 million).

Investment carrying values by financial instrument classification are as follows:

<i>(in millions of dollars)</i>	As at March 31, 2023		
	FVTPL	FVTOCI	Total
Short-term investments	\$ 58.6	\$ -	\$ 58.6
Bonds:			
Government	2,323.0	-	2,323.0
Corporate	1,583.3	-	1,583.3
Preferred stocks	134.0	171.2	305.2
Common stocks	544.2	-	544.2
Pooled funds	56.3	-	56.3
Commercial loans	10.9	-	10.9
	\$ 4,710.3	\$ 171.2	\$ 4,881.5

<i>(in millions of dollars)</i>	As at December 31, 2022		
	FVTPL	FVTOCI	Total
Short-term investments	\$ 89.3	\$ -	\$ 89.3
Bonds:			
Government	2,315.8	-	2,315.8
Corporate	1,607.9	-	1,607.9
Preferred stocks	119.8	178.2	298.0
Common stocks	517.7	-	517.7
Pooled funds	57.2	-	57.2
Commercial loans	11.3	-	11.3
	\$ 4,719.0	\$ 178.2	\$ 4,897.2

The fair value of the FVTOCI preferred stocks disposed of during the three months ended March 31, 2023 was \$14.3 million (March 31, 2022: \$20.7 million).

The fair value yield as at March 31, 2023 for the bond portfolio was 4.06% (December 31, 2022: 4.39%).

Of the bonds held as at March 31, 2023, 84.5% (December 31, 2022: 83.8%) were rated "A-" or better and 82.3% (December 31, 2022: 81.0%) of the preferred stocks were rated "P2L" or better.

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6. INVESTMENTS (continued)

(a) Investment income (loss) and balances (continued)

Of the preferred stocks and corporate bonds held, the industry of issuer is as follows:

	As at March 31, 2023	As at December 31, 2022
Financial services	52.9%	50.4%
Communication services	10.9%	10.8%
Energy	10.7%	13.5%
Utilities	8.7%	9.1%
Industrials	6.3%	5.3%
Consumer discretionary	4.4%	4.8%
Other	6.1%	6.1%
	100.0%	100.0%

Of the preferred stocks and bonds held, the country of issuer is as follows:

	As at March 31, 2023	As at December 31, 2022
Canada	99.5%	99.5%
United States	0.5%	0.5%
	100.0%	100.0%

(b) Financial instruments measured at fair value

The Company categorizes its fair value measurements according to a three-level hierarchy, which prioritizes the inputs used by the Company's valuation techniques. A level is assigned to each fair value measurement based on the lowest level input significant to the fair value measurement in its entirety. The three levels of the fair value hierarchy are defined as follows:

- (i) Level 1 fair value measurements reflect unadjusted, quoted prices in active markets for identical assets, and liabilities that the Company has the ability to access at the measurement date.
- (ii) Level 2 fair value measurements use inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets and liabilities in inactive markets, inputs that are observable but are not prices such as interest rates and credit risks and inputs that are derived from or corroborated by observable market data.
- (iii) Level 3 fair value measurements use significant non-market observable inputs, including assumptions about risk or liquidity.

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

6. INVESTMENTS (continued)

(b) Financial instruments measured at fair value (continued)

Distribution of financial instruments measured at fair value in the three-level hierarchy is as follows:

<i>(in millions of dollars)</i>	As at March 31, 2023			
	Level 1	Level 2	Level 3	Total
Short-term investments	\$ -	\$ 58.6	\$ -	\$ 58.6
Bonds	-	3,906.3	-	3,906.3
Preferred stocks	305.2	-	-	305.2
Common stocks	544.2	-	-	544.2
Pooled funds	-	56.3	-	56.3
Commercial loans	-	-	10.9	10.9
	\$ 849.4	\$ 4,021.2	\$ 10.9	\$ 4,881.5

<i>(in millions of dollars)</i>	As at December 31, 2022			
	Level 1	Level 2	Level 3	Total
Short-term investments	\$ -	\$ 89.3	\$ -	\$ 89.3
Bonds	-	3,923.7	-	3,923.7
Preferred stocks	298.0	-	-	298.0
Common stocks	517.7	-	-	517.7
Pooled funds	-	57.2	-	57.2
Commercial loans	-	-	11.3	11.3
	\$ 815.7	\$ 4,070.2	\$ 11.3	\$ 4,897.2

There were no transfers of financial instruments between the levels during the three months ended March 31, 2023 (year ended December 31, 2022: nil).

Investments in equity and debt instruments are not subject to an impairment assessment, as they are measured at FVTPL or FVTOCI without recycling of fair value changes to profit or loss.

(c) Derivative financial instruments

The Company holds an interest rate futures contract, which is a contractual obligation to buy or sell financial instruments on a future date at a specified price established in an organized market. The futures contract is exchange traded and collateralized by cash. As at March 31, 2023, the Company had derivative financial assets with a notional amount of \$62.3 million (December 31, 2022: \$74.2 million). These derivatives have an expected maturity date within the next year. The fair value of the derivative financial instruments is not significant.

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

7. INSURANCE AND REINSURANCE CONTRACTS

(a) Insurance contract liabilities

The roll-forward of the liabilities for insurance contracts issued, showing the LRC and the LIC, is presented in the following tables:

<i>(in millions of dollars)</i>	Three months ended March 31, 2023				
	Liabilities for remaining coverage		Liabilities for incurred claims		Total
	Excluding loss component	Loss component	Estimates of the present value of future cash flows	Risk adjustment for non-financial risk	
Insurance contract liabilities, beginning of period	\$ 303.3	\$ 27.7	\$ 3,068.7	\$ 178.0	\$ 3,577.7
Insurance revenue	(907.5)	-	-	-	(907.5)
Insurance service expenses:					
Incurred claims and other directly attributable expenses	-	(11.1)	581.7	15.0	585.6
Amortization of insurance acquisition cash flows	197.6	-	-	-	197.6
Changes in fulfilment cash flows relating to the LIC	-	-	5.8	(16.6)	(10.8)
Losses on onerous contracts and reversals of such losses	-	9.9	-	-	9.9
Insurance service result	(709.9)	(1.2)	587.5	(1.6)	(125.2)
Finance expenses from insurance contracts issued	-	-	64.5	-	64.5
Total changes in the interim consolidated statements of income (loss)	(709.9)	(1.2)	652.0	(1.6)	(60.7)
Cash flows:					
Premiums received	923.7	-	-	-	923.7
Claims and other directly attributable expenses paid	-	-	(746.0)	-	(746.0)
Insurance acquisition cash flows	(212.0)	-	-	-	(212.0)
Total cash flows	711.7	-	(746.0)	-	(34.3)
Other movements	-	-	(19.1)	-	(19.1)
Insurance contract liabilities, end of period	\$ 305.1	\$ 26.5	\$ 2,955.6	\$ 176.4	\$ 3,463.6

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

7. INSURANCE AND REINSURANCE CONTRACTS (continued)

(a) Insurance contract liabilities (continued)

<i>(in millions of dollars)</i>	Three months ended March 31, 2022				
	Liabilities for remaining coverage		Liabilities for incurred claims		Total
	Excluding loss component	Loss component	Estimates of the present value of future cash flows	Risk adjustment for non-financial risk	
Insurance contract liabilities, beginning of period	\$ 282.3	\$ 26.3	\$ 3,192.2	\$ 168.1	\$ 3,668.9
Insurance revenue	(814.3)	-	-	-	(814.3)
Insurance service expenses:					
Incurred claims and other directly attributable expenses	-	(10.3)	517.4	15.7	522.8
Amortization of insurance acquisition cash flows	182.6	-	-	-	182.6
Changes in fulfilment cash flows relating to the LIC	-	-	(30.3)	(20.5)	(50.8)
Losses on onerous contracts and reversals of such losses	-	9.6	-	-	9.6
Insurance service result	(631.7)	(0.7)	487.1	(4.8)	(150.1)
Finance income from insurance contracts issued	-	-	(52.7)	-	(52.7)
Total changes in the interim consolidated statements of income (loss)	(631.7)	(0.7)	434.4	(4.8)	(202.8)
Cash flows:					
Premiums received	811.1	-	-	-	811.1
Claims and other directly attributable expenses paid	-	-	(555.7)	-	(555.7)
Insurance acquisition cash flows	(193.0)	-	-	-	(193.0)
Total cash flows	618.1	-	(555.7)	-	62.4
Other movements	-	-	(15.9)	-	(15.9)
Insurance contract liabilities, end of period	\$ 268.7	\$ 25.6	\$ 3,055.0	\$ 163.3	\$ 3,512.6

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

7. INSURANCE AND REINSURANCE CONTRACTS (continued)

(a) Insurance contract liabilities (continued)

The composition of the insurance contract liabilities is as follows:

	As at March 31, 2023	As at March 31, 2022
Premiums receivable	\$ (1,112.8)	\$ (1,019.1)
Unearned premiums	1,720.8	1,555.9
Unearned premiums received	608.0	536.8
Unamortized insurance acquisition cash flows	(302.9)	(268.2)
Onerous loss provision	26.5	25.6
Provision for unpaid claims and other directly attributable payables	3,132.0	3,218.4
	<u>\$ 3,463.6</u>	<u>\$ 3,512.6</u>

(b) Reinsurance contract assets

The roll-forward of the reinsurance contract assets showing the ARC and the AIC is presented in the following tables:

(in millions of dollars)

Three months ended March 31, 2023

	Assets for remaining coverage		Assets for incurred claims		Total
	Excluding loss- recovery component	Loss- recovery component	Estimates of the present value of future cash flows	Risk adjustment for non- financial risk	
Reinsurance contract assets, beginning of period	\$ 18.7	\$ -	\$ 272.0	\$ 14.4	\$ 305.1
Allocation of reinsurance premiums paid	(57.5)	-	-	-	(57.5)
Amounts recoverable from reinsurers for incurred claims:					
Amounts recoverable for incurred claims and other directly attributable expenses	-	-	28.0	1.3	29.3
Changes to amounts recoverable for incurred claims	-	-	(2.5)	(0.6)	(3.1)
Net expenses from reinsurance contracts held	(57.5)	-	25.5	0.7	(31.3)
Finance income from reinsurance contracts held	-	-	5.6	-	5.6
Total changes in the interim consolidated statements of income (loss)	(57.5)	-	31.1	0.7	(25.7)
Cash flows:					
Premiums paid	59.1	-	-	-	59.1
Amounts received	-	-	(23.5)	-	(23.5)
Total cash flows	59.1	-	(23.5)	-	35.6
Reinsurance contract assets, end of period	\$ 20.3	\$ -	\$ 279.6	\$ 15.1	\$ 315.0

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

7. INSURANCE AND REINSURANCE CONTRACTS (continued)

(b) Reinsurance contract assets (continued)

<i>(in millions of dollars)</i>	Three months ended March 31, 2022				
	Assets for remaining coverage		Assets for incurred claims		
	Excluding loss-recovery component	Loss-recovery component	Estimates of the present value of future cash flows	Risk adjustment for non-financial risk	Total
Reinsurance contract assets, beginning of period	\$ 26.2	\$ -	\$ 201.0	\$ 11.2	\$ 238.4
Allocation of reinsurance premiums paid	(40.6)	-	-	-	(40.6)
Amounts recoverable from reinsurers for incurred claims:					
Amounts recoverable for incurred claims and other directly attributable expenses	-	-	16.3	0.7	17.0
Changes to amounts recoverable for incurred claims	-	-	(9.1)	(1.4)	(10.5)
Net expenses from reinsurance contracts held	(40.6)	-	7.2	(0.7)	(34.1)
Finance expenses from reinsurance contracts held	-	-	(3.2)	-	(3.2)
Total changes in the interim consolidated statements of income (loss)	(40.6)	-	4.0	(0.7)	(37.3)
Cash flows:					
Premiums paid	38.8	-	-	-	38.8
Amounts received	-	-	(22.8)	-	(22.8)
Total cash flows	38.8	-	(22.8)	-	16.0
Reinsurance contract assets, end of period	\$ 24.4	\$ -	\$ 182.2	\$ 10.5	\$ 217.1

The composition of the reinsurance contract assets is as follows:

	As at March 31, 2023	As at March 31, 2022
Premiums ceded payable	\$ (25.1)	\$ (12.0)
Unearned premiums ceded	48.9	40.5
Unearned reinsurance premiums paid	23.8	28.5
Claims recoverable from reinsurance contracts held	296.2	191.5
Unearned reinsurance commissions received	(5.0)	(2.9)
	\$ 315.0	\$ 217.1

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

7. INSURANCE AND REINSURANCE CONTRACTS (continued)

(b) Reinsurance contract assets (continued)

The Company follows the policy of underwriting and reinsuring contracts of insurance, which limits the liability of the Company for individual large losses and in the event of a series of claims arising out of a single occurrence and for an aggregation of several such occurrences in the same year. These limits were as follows:

<i>(in millions of dollars)</i>	As at March 31, 2023	As at December 31, 2022
Individual loss		
Property		
Net company retention ¹	\$ 5.0	\$ 5.0
Maximum limit ²	100.0	100.0
Auto and general liability		
Net company retention ¹	4.0	4.0
Maximum limit	40.0	40.0
Catastrophe – primary		
Net company retention ¹	40.0	30.0
Maximum limit ²	1,950.0	1,800.0
Catastrophe – aggregate		
Annual aggregate deductible ³	65.0	65.0
Annual aggregate limit ³	25.0	25.0

¹ Excludes reinstatement premiums, co-participations between the retention level and maximum limit, and tax impacts.

² Excludes co-participation.

³ Contributing event to the annual aggregate deductible and limit is a maximum of \$27 million on events above \$3 million as at March 31, 2023 (December 31, 2022: maximum \$27 million on events above \$3 million).

For catastrophe events, the Company participated an average of 8.6% on layers between the net Company retention and the maximum limit as at March 31, 2023 (December 31, 2022: 3.4%), including an average of 42.5% between the net Company retention and up to a \$100 million loss (December 31, 2022: 0%).

For catastrophe aggregate events, the annual aggregate limit was 100% placed in the three months ended March 31, 2023 (2022: 100.0%). The Company also retains small participations on other reinsurance treaties based on market conditions and risk appetite.

The Company also purchases other types of reinsurance tailored to individual risks or specific exposures as required by its underwriting guidelines and risk management practices.

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

8. INCOME TAXES

The reconciliation of income tax calculated at the Canadian statutory tax rate to the income tax expense (recovery) at the effective tax rate recorded in net income (loss) in the interim consolidated statements of income (loss) is provided in the table below:

<i>(in millions of dollars)</i>	Three months ended March 31			
		2023		2022
Income tax expense (recovery) calculated based on statutory tax rates	26.3%	\$ 35.0	26.3%	\$ (12.5)
Canadian dividend income not subject to tax	(1.5%)	(2.0)	3.9%	(1.9)
Non-deductible expenses	0.0%	0.1	(0.3%)	0.2
Other	(1.3%)	(2.0)	1.5%	(0.7)
Income tax expense (recovery) recorded in net income (loss)	23.5%	\$ 31.1	31.4%	\$ (14.9)

<i>(in millions of dollars)</i>	Three months ended March 31			
		2023		2022
Current income taxes		\$ 37.6		\$ (12.1)
Deferred income taxes		(6.5)		(2.8)
Income tax expense (recovery)		\$ 31.1		\$ (14.9)

9. OTHER ASSETS

Other assets, as presented in the interim consolidated balance sheets, are composed of the following:

<i>(in millions of dollars)</i>	Notes	As at	
		March 31, 2023	December 31, 2022
Pension asset	14	\$ 43.1	\$ 40.3
Investments in associates		45.6	36.7
Prepaid expenses and other		29.2	29.7
Accrued investment income		28.4	26.6
Other receivables		23.6	19.2
		\$ 169.9	\$ 152.5

10. ACCOUNTS PAYABLE AND OTHER LIABILITIES

Accounts payable and other liabilities, as presented in the interim consolidated balance sheets, are composed of the following:

<i>(in millions of dollars)</i>	Notes	As at	
		March 31, 2023	December 31, 2022
Accounts payable and other		\$ 47.3	\$ 77.9
Lease liabilities		30.5	31.7
Pension and non-pension benefit obligations	14	27.1	26.3
Cash-settled share-based compensation plans	13	4.2	3.1
		\$ 109.1	\$ 139.0

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

11. SHARE CAPITAL

The Company is authorized to issue an unlimited number of common shares without nominal or par value and an unlimited number of preferred shares issuable in series. The Company's issued and outstanding common shares were as follows:

<i>(in millions of dollars, except as otherwise noted)</i>	Three months ended March 31, 2023	
	Number of shares (in millions)	Amount
Issued and outstanding, beginning and end of period	115.9	\$ 2,307.8
Shares held in trust, beginning of period	(1.5)	(53.6)
Purchased for future settlement of the Long-Term Incentive Plan ("LTIP") and Medium-Term Incentive Plan ("MTIP")	(0.2)	(4.9)
Released for settlement of the LTIP and MTIP	0.9	32.3
Shares held in trust, end of period	(0.8)	(26.2)
Issued and outstanding, net of shares held in trust, end of period	115.1	\$ 2,281.6

<i>(in millions of dollars, except as otherwise noted)</i>	Year ended December 31, 2022	
	Number of shares (in millions)	Amount
Issued and outstanding, beginning and end of year	115.9	\$ 2,307.8
Shares held in trust, beginning of year	-	-
Purchased for future settlement of the LTIP and MTIP	(1.5)	(53.6)
Shares held in trust, end of year	(1.5)	(53.6)
Issued and outstanding, net of shares held in trust, end of year	114.4	\$ 2,254.2

On May 11, 2023, the Board of Directors declared a \$0.1375 per share dividend, payable on June 28, 2023 to shareholders of record at the close of business on June 15, 2023.

No preferred shares were issued and outstanding.

12. EARNINGS (LOSS) PER COMMON SHARE

Basic earnings (loss) per common share ("EPS") is calculated by dividing net income (loss) attributable to common shareholders by the weighted average number of common shares outstanding during the period. Diluted EPS is calculated by adjusting the net earnings available to common shareholders, if applicable, and the weighted average number of common shares outstanding for the effects of dilutive instruments pertaining to the Company's share-based compensation plans.

<i>(in millions of dollars, except as otherwise noted)</i>	Three months ended March 31	
	2023	2022
Net income (loss) attributable to common shareholders	\$ 100.9	\$ (32.6)
Weighted average common shares outstanding (in millions)	114.7	115.9
Dilutive effect of share-based compensation plans (in millions)	1.7	1.6
Weighted average of diluted common shares outstanding (in millions)	116.4	117.5
EPS (in dollars)		
Basic	\$ 0.88	\$ (0.28)
Diluted	\$ 0.87	\$ (0.28)

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

13. SHARE-BASED COMPENSATION PLANS

(a) Medium-term and long-term incentive plans

Restricted units (“RUs”) and restricted share units (“RSUs”)

The following table shows the movements in the RUs and RSUs under the MTIP and LTIP during the period:

	Three months ended March 31	
	2023	2022
	Number of units	Number of units
Outstanding, beginning of period	998,685	1,102,254
Awarded	229,058	269,307
Forfeited	(17,334)	(6,826)
Settled	(351,953)	(328,474)
Outstanding, end of period	858,456	1,036,261

The recorded compensation expense during the three months ended March 31, 2023 for the RUs and RSUs was \$1.9 million (March 31, 2022: \$2.1 million), and the aggregate contributed surplus balance attributable to the RUs and RSUs at March 31, 2023 was \$10.0 million (December 31, 2022: \$15.9 million).

Performance units (“PUs”) and performance share units (“PSUs”)

The following table shows the movements in the PUs and PSUs under the MTIP and LTIP during the period:

	Three months ended March 31	
	2023	2022
	Number of units	Number of units
Outstanding, beginning of period	915,452	972,752
Awarded	185,512	252,885
Forfeited	(15,010)	(6,636)
Settled	(342,413)	(284,744)
Outstanding, end of period	743,541	934,257

The recorded compensation expense during the three months ended March 31, 2023 for the PUs and PSUs was \$2.6 million (March 31, 2022: \$2.2 million), and the aggregate contributed surplus balance attributable to the PUs and PSUs as at March 31, 2023 was \$14.4 million (December 31, 2022: \$24.3 million).

(b) Deferred share unit plans

As at March 31, 2023, there were 121,922 deferred share units (“DSUs”) outstanding. The DSU liability as at March 31, 2023 was \$4.2 million (December 31, 2022: \$3.1 million).

(c) Stock option plan

The Company has a stock option plan in place for certain employees, which became effective as of November 23, 2021. Grants under this plan were made in the three months ended March 31, 2023, amounting to 177,891 shares.

DEFINITY FINANCIAL CORPORATION

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MARCH 31, 2023

13. SHARE-BASED COMPENSATION PLANS (continued)

(c) Stock option plan (continued)

The fair value of stock options granted was measured using the Black-Scholes option pricing model. The fair value of stock options granted in the three months ended March 31, 2023 was \$1.3 million (March 31, 2022: nil). The key assumptions used to measure the fair value of options granted under the Black-Scholes option pricing model at the date of grant were as follows:

Share price at the date of grant	\$36.48
Exercise price	\$36.48
Expected share price volatility	18.0%
Expected life of options	6.25 Years
Expected dividend yield	1.6%
Risk-free interest rate	3.4%

The exercise price was determined using the volume weighted average trading price of the Company's common shares during the five trading days immediately preceding the date of the grants.

Given the Company's IPO was in November 2021, the Company does not yet have sufficient history to use the volatility of its own share price to determine the Company's expected share price volatility. As a result, the Company also considered the volatility of share prices of comparable companies.

14. POST-EMPLOYMENT BENEFITS

The Company provides certain pension and other post-employment benefits through defined benefit, defined contribution, and other post-employment benefit plans to eligible participants upon retirement.

The contribution to be paid by the Company to the defined benefit pension plans is determined each year by the Company's pension actuaries based on the latest actuarial valuations of all its plans. The total contributions to the defined benefit pension plans made by the Company during the three months ended March 31, 2023 were \$0.6 million (March 31, 2022: \$0.4 million).

Under the defined contribution component of the pension plan, the Company contributes a fixed percentage of an employee's pensionable earnings to the plan. Contributions under the defined contribution component of the pension plan during the three months ended March 31, 2023 were \$6.8 million (March 31, 2022: \$5.2 million).

The following table presents the actuarial gains (losses) for the post-employment benefit obligation recognized in OCI during the period:

<i>(in millions of dollars)</i>	Three months ended March 31	
	2023	2022
Re-measurements related to:		
Changes in discount rate used to determine the benefit obligation	\$ (4.4)	\$ 31.9
Return on plan assets excluding interest income	6.0	(14.4)
	\$ 1.6	\$ 17.5

The discount rate as at March 31, 2023 used to determine the defined benefit obligations for the Company's pension plans was 5.0% (December 31, 2022: 5.2%) and other benefit plans was 5.0% (December 31, 2022: 5.2%).

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

15. EXPENSES

(a) Insurance service expenses and other (expenses) income

Insurance service expenses and other (expenses) income incurred by the Company, as presented in the interim consolidated statements of income (loss), are composed of the following:

<i>(in millions of dollars)</i>	Three months ended March 31, 2023			
	Expenses attributed to insurance acquisition cash flows	Other directly attributable expenses	Other expenses (income)	Total
Claims and adjustment expenses	\$ -	\$ 542.9	\$ 14.6	\$ 557.5
Discounting in insurance service expenses	-	(22.9)	-	(22.9)
Risk adjustment	-	(1.6)	-	(1.6)
Commissions	120.5	16.0	-	136.5
Operating expenses	47.0	50.3	21.1	118.4
Premium taxes	31.3	-	-	31.3
(Gains) losses on onerous insurance contracts	-	(1.2)	-	(1.2)
Public company expenses	-	-	6.8	6.8
Distribution:				
Distribution business expenses	-	-	16.6	16.6
Amortization of intangible assets recognized in business combinations on distribution business	-	-	3.8	3.8
Interest on restricted cash, and demutualization and IPO-related expenses	-	-	(2.5)	(2.5)
Share of profit from investments in other associates	-	-	(1.0)	(1.0)
Other	-	-	0.6	0.6
	\$ 198.8	\$ 583.5	\$ 60.0	\$ 842.3
Insurance service expenses				782.3
Other expenses (income)				60.0
				\$ 842.3

DEFINITY FINANCIAL CORPORATION

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MARCH 31, 2023

15. EXPENSES (continued)

(a) Insurance service expenses and other (expenses) income (continued)

<i>(in millions of dollars)</i>	Three months ended March 31, 2022			
	Expenses attributed to insurance acquisition cash flows	Other directly attributable expenses	Other expenses (income)	Total
Claims and adjustment expenses	\$ -	\$ 444.9	\$ 15.8	\$ 460.7
Discounting in insurance service expenses	-	(18.1)	-	(18.1)
Risk adjustment	-	(4.8)	-	(4.8)
Commissions	111.1	20.5	-	131.6
Operating expenses	44.3	38.6	21.2	104.1
Premium taxes	28.4	-	-	28.4
(Gains) losses on onerous insurance contracts	-	(0.7)	-	(0.7)
Public company expenses	-	-	6.5	6.5
Distribution:				
Share of distribution profit from investments in associates	-	-	(3.4)	(3.4)
Amortization of intangible assets recognized in business combinations on distribution business	-	-	0.3	0.3
Interest on restricted cash, and demutualization and IPO-related expenses	-	-	1.9	1.9
Share of profit from investments in other associates	-	-	(1.1)	(1.1)
Other	-	-	(0.2)	(0.2)
	\$ 183.8	\$ 480.4	\$ 41.0	\$ 705.2
Insurance service expenses				664.2
Other expenses (income)				41.0
				\$ 705.2

(b) Net expenses from reinsurance contracts held

Net expenses from reinsurance contracts held incurred by the Company, as presented in the interim consolidated statements of income (loss), are composed of the following:

<i>(in millions of dollars)</i>	Three months ended March 31	
	2023	2022
Earned reinsurance premiums	\$ 68.4	\$ 49.0
Claims recoverable from reinsurers for incurred claims	(31.2)	(8.0)
Commissions earned on ceded reinsurance	(11.7)	(8.7)
Discounting in net expenses from reinsurance contracts held	6.5	1.1
Risk adjustment	(0.7)	0.7
	\$ 31.3	\$ 34.1

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16. CASH FLOWS FROM OPERATING ACTIVITIES

The following table shows the changes in operating assets and liabilities included in the interim consolidated statements of cash flows during the period:

<i>(in millions of dollars)</i>	Three months ended March 31	
	2023	2022
Adjustments for non-cash items:		
Amortization and depreciation		
Bond premium/discount	\$ (3.1)	\$ 5.7
Property and equipment	3.3	2.5
Intangible assets	20.8	13.8
Net investment (gains) losses	(91.7)	197.8
Share-based compensation	4.5	4.3
Share of profit from investments in associates	(1.0)	(4.2)
	<u>\$ (67.2)</u>	<u>\$ 219.9</u>
Changes in operating assets and liabilities:		
Reinsurance contract assets	(9.9)	21.3
Other operating assets	(4.9)	(18.1)
Insurance contract liabilities	(114.1)	(156.3)
Accounts payable and other liabilities	(24.2)	(23.6)
	<u>\$ 153.1</u>	<u>\$ (176.7)</u>

17. RISKS RELATED TO ECONOMIC UNCERTAINTY AND RELATED FINANCIAL IMPACTS

Geopolitical events and the COVID-19 pandemic have resulted in heightened economic uncertainty. The conflict between Russia and Ukraine continues to evolve and foreign governments continue to respond accordingly. This, along with the ongoing COVID-19 pandemic, has resulted in volatile global financial markets and presented further economic challenges, including rising inflation and global supply chain disruption. Persistent and rising inflation has prompted central banks to significantly raise interest rates. The Company does not have direct investments nor underwriting exposures of significance in Russia or Ukraine, and is continuing to monitor the evolving economic impact of the above on its operations and capital position. The Company's strong capital position and its proactive capital and risk management practices developed in recent years have enabled the Company to react rapidly to the changing environment.

Along with many other P&C insurers in Canada, Definity Insurance has been named as a defendant in litigation for certain business interruption losses related to the COVID-19 pandemic, seeking to establish coverage under insurance policies, including national and regional class proceedings. An Ontario action on behalf of a national class (businesses in Canada, excluding Québec) was certified as a class proceeding in 2021 and a trial was completed in the first quarter of 2023, with a decision now pending. Definity Insurance denies liability and intends to vigorously defend its positions in this proceeding. There is also a potential class proceeding in Québec outstanding and at a preliminary stage. The parties have agreed to discontinue the Québec action against Definity Insurance and certain other defendants, subject to court approval.

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18. INSURANCE RISK MANAGEMENT

By the very nature of an insurance contract, there is uncertainty as to whether an insured event will occur and the amount of loss that would arise in such an event. In the course of these insurance activities, there are several risks the Company must address by applying appropriate underwriting and claims policies and processes. Note 10 of the Company's audited consolidated financial statements for the year ended December 31, 2022 outlines the most significant insurance risks and the practices employed to mitigate these risks. The below has been updated as at December 31, 2022, as applicable, to reflect the adoption of IFRS 17.

The following table presents the interest rate sensitivity analysis for a one percentage point change in interest rates on the LIC after risk mitigation by reinsurance as at December 31, 2022 on income before income taxes:

(in millions of dollars)

		+1 pt		-1 pt
LIC after risk mitigation by reinsurance	\$	(59.0)	\$	63.2

The analysis below demonstrates the impact of changing assumptions for all lines of business and regions in such a way that the average claim severity and frequency is altered significantly. The analysis below also isolates the impact within the average claims severity of a change in internal claims expenses on the LIC. The impacts below are on the LIC after risk mitigation by reinsurance as at December 31, 2022 on income before income taxes.

(in millions of dollars)

		+5%		-5%
Change in average claims severity	\$	143.7	\$	(143.7)
Change in frequency on unreported claims	\$	13.2	\$	(13.2)
Change in internal claims expenses	\$	8.5	\$	(8.5)

The following table presents the sensitivity of risk adjustment for a five percentage point change in the confidence level on the LIC after risk mitigation by reinsurance as at December 31, 2022 on income before income taxes.

(in millions of dollars)

		+5 pts		-5 pts
Change in risk adjustment	\$	45.3	\$	(37.0)

19. FINANCIAL RISK MANAGEMENT

The Company's financial instruments, including investments, are exposed to interest rate risk (including the impact of credit spreads), equity market price risk and preferred stock price risk, credit risk, foreign exchange risk, and liquidity risk as disclosed in note 8 of the Company's audited consolidated financial statements for the year ended December 31, 2022. The below has been updated as at December 31, 2022 to reflect the adoption of IFRS 9.

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19. FINANCIAL RISK MANAGEMENT (continued)

(a) Interest rate risk

The impact of an immediate hypothetical one percentage point change in interest rates (assuming a parallel shift across the yield curve), on the Company's bond portfolios, with all other variables held constant is as follows:

<i>(in millions of dollars)</i>	December 31, 2022	
	Change in assumption	Impact on income (loss) before income taxes
Fair value of bonds	+ 1 pt	\$ (143.7)
Fair value of bonds	- 1 pt	\$ 161.5

(b) Common equity market price risk and preferred stock price risk

The estimated impact of a 10% movement in the indices (S&P/Toronto Stock Exchange 60 Index - Canadian common stocks, MSCI World Index - foreign stocks and pooled funds, Solactive Canadian Rate Reset Preferred Share Index - preferred stocks) with all other variables held constant, to the extent the Company does not dispose of any of these equities during the year, is as follows:

<i>(in millions of dollars)</i>	December 31, 2022	
	Change in assumption	Impact on income (loss) before income taxes
Fair value of Canadian stocks	+ 10%	\$ 38.3
Fair value of foreign stocks and pooled funds	+ 10%	\$ 19.7
Fair value of FVTPL preferred stocks	+ 10%	\$ 12.9
Fair value of Canadian stocks	- 10%	\$ (38.3)
Fair value of foreign stocks and pooled funds	- 10%	\$ (19.7)
Fair value of FVTPL preferred stocks	- 10%	\$ (12.9)

<i>(in millions of dollars)</i>	December 31, 2022	
	Change in assumption	Impact on OCI before income taxes
Fair value of FVTOCI preferred stocks	+ 10%	\$ 19.2
Fair value of FVTOCI preferred stocks	- 10%	\$ (19.2)

20. SUBSEQUENT EVENT

On May 8, 2023, the Company through its subsidiary McDougall Insurance Brokers Limited ("McDougall") acquired 100% of the shares of McFarlan Rowlands Insurance Brokers Inc. and affiliated entities ("McFarlan Rowlands") for cash and share consideration of approximately \$232 million (subject to post-closing adjustments). The initial purchase price was funded with cash including approximately \$75 million in debt and \$45 million in equity subscriptions from McFarlan Rowlands shareholders. McFarlan Rowlands is a leading Ontario-based insurance brokerage, with over 200 employees in 18 office locations across southwestern Ontario, and over \$200 million in annual premiums. In addition to its property and casualty brokerage operations, McFarlan Rowlands also has expertise in claims adjusting, life and group benefits brokering, and investment counselling and portfolio management services.