

# Second Quarter 2018

# 2

Interim Consolidated Financial Statements (unaudited)  
For the quarter ended June 30, 2018

Intact Financial Corporation



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**INTACT FINANCIAL CORPORATION**
**Interim Consolidated balance sheets (unaudited)**

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

As at	Note	June 30, 2018	December 31, 2017
<b>Assets</b>			
Investments	5		
Cash and cash equivalents		\$ 287	\$ 163
Debt securities		11,382	11,229
Preferred shares		1,329	1,409
Common shares		3,626	3,659
Loans		322	393
<hr/>			
Investments		16,946	16,853
Premium receivables		3,493	3,351
Reinsurance assets	10	825	822
Income taxes receivable		119	24
Deferred tax assets		92	112
Deferred acquisition costs		927	881
Other assets	11	828	782
Investments in associates and joint ventures		563	550
Property and equipment		149	150
Intangible assets		2,177	2,161
Goodwill		2,291	2,242
<hr/>			
<b>Total assets</b>		<b>\$ 28,410</b>	<b>\$ 27,928</b>
<hr/>			
<b>Liabilities</b>			
Claims liabilities	9	\$ 10,634	\$ 10,475
Unearned premiums		5,508	5,365
Financial liabilities related to investments	6	427	246
Income taxes payable		11	262
Deferred tax liabilities		238	257
Other liabilities	11	1,528	1,619
Debt outstanding	12	2,266	2,241
<hr/>			
<b>Total liabilities</b>		<b>20,612</b>	<b>20,465</b>
<hr/>			
<b>Shareholders' equity</b>			
Common shares		2,816	2,816
Preferred shares	13	1,028	783
Contributed surplus		133	128
Retained earnings		3,622	3,520
Accumulated other comprehensive income (loss)			
Available-for-sale securities		107	224
Translation of foreign operations, net of hedges		92	(2)
Other		-	(6)
<hr/>			
<b>Total liabilities and shareholders' equity</b>		<b>\$ 28,410</b>	<b>\$ 27,928</b>

See accompanying notes to the interim Consolidated financial statements.

**INTACT FINANCIAL CORPORATION**
**Interim Consolidated statements of income (unaudited)**

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

For the periods ended June 30,	Note	Three months		Six months	
		2018	2017	2018	2017
<b>Direct premiums written</b>		\$ 2,940	\$ 2,513	\$ 5,064	\$ 4,244
Premiums ceded		(83)	(42)	(184)	(91)
Net premiums written		2,857	2,471	4,880	4,153
Change in unearned premiums		(433)	(420)	(102)	(105)
<b>Net earned premiums</b>		2,424	2,051	4,778	4,048
Other underwriting revenues		27	26	54	54
Investment income	15				
Interest income		85	65	168	129
Dividend income		57	49	105	99
Other revenues		37	39	68	74
<b>Total revenues</b>		2,630	2,230	5,173	4,404
Net claims incurred	9	(1,569)	(1,314)	(3,168)	(2,713)
Underwriting expenses		(767)	(637)	(1,505)	(1,252)
Investment expenses	15	(8)	(9)	(17)	(18)
Net gains (losses)	16	(27)	59	(22)	134
Share of profit from investments in associates and joint ventures		15	11	17	13
Finance costs		(26)	(19)	(51)	(38)
Integration and restructuring costs		(14)	(8)	(39)	(12)
Other expenses		(35)	(18)	(69)	(42)
Income before income taxes		199	295	319	476
Income tax expense	17	(38)	(52)	(55)	(87)
<b>Net income attributable to shareholders</b>		\$ 161	\$ 243	\$ 264	\$ 389
Weighted-average number of common shares outstanding (in millions)	18	139.2	131.0	139.2	131.0
<b>Earnings per common share, basic and diluted (in dollars)</b>	18	\$ 1.10	\$ 1.82	\$ 1.78	\$ 2.90
Dividends paid per common share (in dollars)		\$ 0.70	\$ 0.64	\$ 1.40	\$ 1.28

See accompanying notes to the interim Consolidated financial statements.

**INTACT FINANCIAL CORPORATION**

**Interim Consolidated statements of comprehensive income (unaudited)**

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

For the periods ended June 30,	Note	Three months		Six months	
		2018	2017	2018	2017
<b>Net income attributable to shareholders</b>		\$ 161	\$ 243	\$ 264	\$ 389
<b>Other comprehensive income (loss)</b>					
<b>Available-for-sale securities:</b>					
net changes in unrealized gains (losses)		68	(43)	(73)	100
income tax benefit (expense)		(17)	12	18	(27)
reclassification of net losses (gains)		(28)	(54)	(81)	(152)
income tax benefit (expense)		9	14	19	38
		32	(71)	(117)	(41)
<b>Cash flow hedges:</b>					
net changes in unrealized gains (losses)		-	(121)	-	(121)
		-	(121)	-	(121)
<b>Foreign exchange gains (losses) on:</b>					
translation of foreign operations		72	-	198	-
net investment hedges		(34)	-	(104)	-
		38	-	94	-
<b>Other</b>		5	(4)	6	(4)
<b>Items that may be reclassified subsequently to net income</b>		75	(196)	(17)	(166)
Net actuarial gains (losses) on employee future benefits	20	72	(97)	72	(118)
income tax benefit (expense)		(19)	26	(19)	31
<b>Items that will not be reclassified subsequently to net income</b>		53	(71)	53	(87)
<b>Other comprehensive income (loss)</b>		128	(267)	36	(253)
<b>Total comprehensive income attributable to shareholders</b>		\$ 289	\$ (24)	\$ 300	\$ 136

See accompanying notes to the interim Consolidated financial statements.

**INTACT FINANCIAL CORPORATION**
**Interim Consolidated statements of changes in shareholders' equity (unaudited)**

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

	Note	Common shares	Preferred shares	Contributed surplus	Retained earnings	Accumulated other comprehensive income (loss)	Total
<b>Balance as at January 1, 2018</b>		\$ 2,816	\$ 783	\$ 128	\$ 3,520	\$ 216	\$ 7,463
Net income attributable to shareholders		-	-	-	264	-	264
Other comprehensive income (loss)		-	-	-	53	(17)	36
<b>Total comprehensive income (loss)</b>		-	-	-	317	(17)	300
Preferred shares issued	13	-	245	-	-	-	245
Dividends declared on:							
common shares		-	-	-	(195)	-	(195)
preferred shares		-	-	-	(16)	-	(16)
Share-based payments	19	-	-	5	(4)	-	1
<b>Balance as at June 30, 2018</b>		\$ 2,816	\$ 1,028	\$ 133	\$ 3,622	\$ 199	\$ 7,798
<b>Balance as at January 1, 2017</b>		\$ 2,082	\$ 489	\$ 129	\$ 3,197	\$ 191	\$ 6,088
Net income attributable to shareholders		-	-	-	389	-	389
Other comprehensive income (loss)		-	-	-	(87)	(166)	(253)
Total comprehensive income (loss)		-	-	-	302	(166)	136
Preferred shares issued		-	147	-	-	-	147
Common shares repurchased for cancellation		(1)	-	-	(6)	-	(7)
Dividends declared on:							
common shares		-	-	-	(173)	-	(173)
preferred shares		-	-	-	(9)	-	(9)
Share-based payments		-	-	(11)	(5)	-	(16)
Acquisition of non-controlling interests		-	-	-	(8)	-	(8)
<b>Balance as at June 30, 2017</b>		\$ 2,081	\$ 636	\$ 118	\$ 3,298	\$ 25	\$ 6,158

See accompanying notes to the interim Consolidated financial statements.

**INTACT FINANCIAL CORPORATION**
**Interim Consolidated statements of cash flows (unaudited)**

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

For the periods ended June 30,	Note	Three months		Six months	
		2018	2017	2018	2017
<b>Operating activities</b>					
Income before income taxes		\$ 199	\$ 295	\$ 319	\$ 476
Income tax received (paid), net		(90)	(4)	(381)	-
Contributions to the defined benefit pension plans		(13)	(16)	(27)	(31)
Share-based payments		(3)	(1)	(4)	(2)
Net losses (gains)	16	27	(59)	22	(134)
Adjustments for non-cash items	22	68	46	143	94
Changes in other operating assets and liabilities	22	106	77	(98)	(153)
Changes in net claims liabilities	9	23	15	96	86
<b>Net cash flows provided by operating activities</b>		<b>317</b>	<b>353</b>	<b>70</b>	<b>336</b>
<b>Investing activities</b>					
Proceeds from sale of investments		3,662	2,304	9,344	5,105
Purchases of investments		(4,034)	(2,982)	(9,255)	(5,683)
Purchases of brokerages and other equity investments, net		(2)	(42)	(5)	(76)
Purchases of intangibles and property and equipment, net		(29)	(25)	(51)	(50)
<b>Net cash flows (used in) provided by investing activities</b>		<b>(403)</b>	<b>(745)</b>	<b>33</b>	<b>(704)</b>
<b>Financing activities</b>					
Proceeds from issuance of debt, net of issuance costs		-	422	-	422
Proceeds from issuance of preferred shares, net of issuance costs	13	243	147	243	147
Amount borrowed (repaid) on the credit facility	12	12	-	10	-
Common shares repurchased for cancellation		-	(2)	-	(7)
Common shares repurchased for share-based payments	19	(21)	(20)	(29)	(30)
Dividends paid on common shares		(97)	(84)	(195)	(168)
Dividends paid on preferred shares		(8)	(4)	(16)	(9)
<b>Net cash flows provided by financing activities</b>		<b>129</b>	<b>459</b>	<b>13</b>	<b>355</b>
Net increase (decrease) in cash and cash equivalents		43	67	116	(13)
Cash and cash equivalents, beginning of period		240	88	163	168
Exchange rate differences on cash and cash equivalents		4	-	8	-
<b>Cash and cash equivalents, end of period</b>		<b>\$ 287</b>	<b>\$ 155</b>	<b>\$ 287</b>	<b>\$ 155</b>
<b>Composition of cash and cash equivalents</b>					
Cash		110	154	110	154
Cash equivalents		177	1	177	1
<b>Cash and cash equivalents, end of period</b>		<b>\$ 287</b>	<b>\$ 155</b>	<b>\$ 287</b>	<b>\$ 155</b>
<b>Other relevant cash flow disclosures – operating activities</b>					
Interest paid		30	15	52	37
Interest received		100	87	166	132
Dividends received		60	53	112	106

See accompanying notes to the interim Consolidated financial statements.

## INTACT FINANCIAL CORPORATION

### Notes to the interim Consolidated financial statements (unaudited)

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

#### Glossary of abbreviations

<b>AFS</b>	Available for sale	<b>LTIP</b>	Long-term incentive plan
<b>AMF</b>	Autorité des marchés financiers	<b>MBS</b>	Mortgage-backed securities
<b>CAD</b>	Canadian Dollar	<b>MCT</b>	Minimum capital test
<b>CALs</b>	Company action levels	<b>MD&amp;A</b>	Management's Discussion and Analysis
<b>DSU</b>	Deferred share unit	<b>MYA</b>	Market yield adjustment
<b>EPS</b>	Earnings per share to common shareholders	<b>NEP</b>	Net earned premiums
<b>ESPP</b>	Employee share purchase plan	<b>OCI</b>	Other comprehensive income
<b>FVTPL</b>	Fair value through profit and loss	<b>OSFI</b>	Office of the Superintendent of Financial Institutions
<b>IASB</b>	International Accounting Standards Board	<b>P&amp;C</b>	Property and casualty
<b>IBNR</b>	Insurance claims incurred but not yet reported by policyholders	<b>RBC</b>	Risk-based capital
<b>IFRS</b>	International Financial Reporting Standards	<b>U.S.</b>	United States
<b>JV</b>	Joint ventures	<b>USD</b>	U.S. Dollar

#### Note 1 – Status of the Company

Intact Financial Corporation (the “Company”), incorporated under the *Canada Business Corporations Act*, is domiciled in Canada and its shares are publicly traded on the Toronto Stock Exchange (TSX: IFC). The Company has investments in wholly-owned subsidiaries which operate principally in the Canadian P&C insurance market and offers specialty insurance products to small and midsize businesses in the United States. The Company, through its operating subsidiaries, principally underwrites automobile, home, as well as commercial P&C contracts to individuals and businesses. On September 28, 2017, the Company acquired all of the issued and outstanding shares of OneBeacon Insurance Group, Ltd. (“OneBeacon”), a leading U.S. specialty insurer. Further details of the acquisition are provided in *Note 4 – Business combination*.

These interim Consolidated financial statements include the accounts of the Company and its subsidiaries.

The registered office of the Company is 700 University Avenue, Toronto, Canada.

#### Note 2 – Basis of presentation

##### 2.1 Statement of compliance

These interim Consolidated financial statements are prepared in accordance with International Accounting Standards 34 – *Interim Financial Reporting*. These interim Consolidated financial statements and the accompanying notes were authorized for issue in accordance with a resolution of the Board of Directors on July 31, 2018.

##### 2.2 Preparation and presentation of financial statements

These interim Consolidated financial statements are condensed financial statements and should be read in conjunction with the Company's annual Consolidated financial statements for the year ended December 31, 2017.

The Company presents its interim Consolidated balance sheets broadly in order of liquidity. Certain comparative figures have been reclassified to conform to the presentation adopted in the current year.

##### 2.3 Seasonality

The P&C insurance business is seasonal in nature. While net premiums earned are generally stable from quarter to quarter, underwriting results are driven mainly by weather conditions which may vary significantly between quarters.

## INTACT FINANCIAL CORPORATION

### Notes to the interim Consolidated financial statements (unaudited)

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

#### 2.4 Foreign currency translation

Table 2.1 – Exchange rates used in the preparation of the interim consolidated financial statements

	As at		Average rate for the three-month periods ended		Average rate for the six-month periods ended	
	June 30, 2018	December 31, 2017	June 30, 2018	June 30, 2017	June 30, 2018	June 30, 2017
USD vs CAD	1.31450	1.25730	1.29094	1.34453	1.27790	1.33422

#### Note 3 – Summary of significant accounting policies

The accounting policies applied during the six-month period ended June 30, 2018 are the same as those described and disclosed in Note 2 – *Summary of significant accounting policies* of the annual Consolidated financial statements for the year ended December 31, 2017. In addition, on January 1, 2018, the Company adopted the following new standards and amendments to existing standards:

##### Amendments to IFRS 4 – *Insurance Contracts* for the application of IFRS 9 – *Financial Instruments*

The Company has adopted the amendments to IFRS 4 – *Insurance Contracts* (“IFRS 4”) that address concerns of insurers about the different effective dates for IFRS 9 – *Financial Instruments* (“IFRS 9”) and IFRS 17, the new insurance contracts standard. The amendments allow insurance entities to elect one of the two following options:

- the deferral approach provides entities whose predominant activities are to issue contracts within the scope of IFRS 4, a temporary exemption to continue using IAS 39, instead of IFRS 9 until January 1, 2021 (the “deferral approach”).
- the overlay approach can be applied to eligible financial assets and provides an option for all issuers of insurance contracts to reclassify from profit or loss to OCI any additional accounting volatility that may arise from applying IFRS 9 before the new insurance contracts standard.

The Company has opted for the deferral approach and performed an assessment as at September 30, 2017, considering OneBeacon’s acquisition (*see Note 4 – Business combination*). The Company concluded that its activities are predominantly connected with insurance, since the percentage of liabilities connected with insurance contracts over total liabilities is above the 80% threshold.

Therefore, the Company applies the temporary exemption and will continue to apply IAS 39 to its financial assets until January 1, 2021.

##### IFRS 15 – *Revenue from contracts with customers*

The Company has adopted the new IFRS 15 – *Revenue from Contracts with Customers* (“IFRS 15”). The standard supersedes IAS 18 – *Revenue*, IAS 11 – *Construction Contracts*, and a number of revenue-related interpretations. This new standard specifies how and when to recognize revenue and additional relevant disclosure requirements. IFRS 15 applies to nearly all contracts with customers, except for insurance contracts, financial instruments and leases.

IFRS 15 only applies to the Company’s Other revenues and its adoption had no impact on the interim Consolidated financial statements.

## INTACT FINANCIAL CORPORATION

### Notes to the interim Consolidated financial statements (unaudited)

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

#### Note 4 – Business combination

##### 4.1 OneBeacon

On September 28, 2017, the Company completed the acquisition of OneBeacon, a leading U.S. specialty insurer, for a cash consideration of US\$1.7 billion (\$2.3 billion). OneBeacon became a wholly-owned subsidiary of the Company and the results of operations are included in the Consolidated financial statements from that date.

The following table summarizes the consideration paid for OneBeacon, and the amounts recognized for the assets acquired and liabilities assumed (determined in accordance with IFRS) as at the acquisition date.

Table 4.1 – Business combination – OneBeacon

<b>As at June 30, 2018</b>	<b>USD</b>	<b>CAD</b>
<b>Purchase price</b>		
Cash consideration paid	1,702	2,128
Purchase price hedge	-	200
<b>Total purchase price</b>	<b>1,702</b>	<b>2,328</b>
<b>Provisional fair value of assets acquired and liabilities assumed</b>		
Investments <sup>1</sup>	2,706	3,383
Premium receivables	275	343
Reinsurance assets	287	358
Distribution networks and other intangibles	626	782
Other assets	379	474
Claims liabilities	(1,628)	(2,036)
Unearned premiums	(650)	(813)
Deferred tax liabilities	(36)	(43)
Debt outstanding	(292)	(364)
Other liabilities	(431)	(538)
<b>Total identifiable net assets</b>	<b>1,236</b>	<b>1,546</b>
<b>Goodwill</b>	<b>466</b>	<b>782</b>
Exchange rate (CAD/USD) as at the acquisition date		1.25030

<sup>1</sup> Included net cash acquired of US\$151 million.

The fair value of the acquired distribution networks, trade names and other intangible assets are based on a discounted cash flow analysis. The distribution networks are amortized over a 20 year period. The fair value of the claims liabilities reflected the impact of discounting and risk margin. Goodwill reflects the quality of the acquired business and the synergies expected following the integration of OneBeacon. The goodwill is not deductible for tax purposes. The final determination of the fair value of identifiable assets and liabilities acquired will be completed within the prescribed period of one year following the acquisition.

The integration costs in connection with the acquisition of OneBeacon are reported in Integration and restructuring costs in the interim Consolidated Statements of income.

The Company hedged the purchase price and book value exposure associated with CAD/USD exchange rate fluctuations.

**INTACT FINANCIAL CORPORATION**
**Notes to the interim Consolidated financial statements (unaudited)**

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

**Note 5 – Investments**
**5.1 Classification of investments**

Table 5.1 – Classification of investments

As at	Fair value			Amortized cost	Total carrying amount
	AFS	Classified as FVTPL	Designated as FVTPL	Cash and cash equivalents, and loans	
<b>June 30, 2018</b>					
<b>Cash and cash equivalents</b>	-	-	-	287	287
Short-term notes	64	-	-	-	64
Fixed income					
Investment grade					
Government	2,044	-	2,991	-	5,035
Corporate	2,034	-	2,183	-	4,217
Asset backed <sup>1</sup>	444	-	266	-	710
Mortgage backed					
Agency <sup>2</sup>	216	-	379	-	595
Non agency	289	-	318	-	607
Below investment grade					
Corporate	-	-	7	-	7
Non rated <sup>3</sup>	147	-	-	-	147
<b>Debt securities</b>	<b>5,238</b>	<b>-</b>	<b>6,144</b>	<b>-</b>	<b>11,382</b>
Investment grade					
Retractable	24	-	-	-	24
Fixed-rate perpetual	275	-	-	-	275
Other perpetual	1,030	-	-	-	1,030
<b>Preferred shares</b>	<b>1,329</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>1,329</b>
<b>Common shares</b>	<b>2,486</b>	<b>151</b>	<b>989</b>	<b>-</b>	<b>3,626</b>
<b>Loans</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>322</b>	<b>322</b>
	<b>9,053</b>	<b>151</b>	<b>7,133</b>	<b>609</b>	<b>16,946</b>
<b>December 31, 2017</b>					
<b>Cash and cash equivalents</b>	-	-	-	163	163
Short-term notes	120	97	-	-	217
Fixed income					
Investment grade					
Government	1,775	-	3,432	-	5,207
Corporate	1,505	-	2,368	-	3,873
Asset backed <sup>1</sup>	500	-	487	-	987
Mortgage backed					
Agency <sup>2</sup>	90	-	250	-	340
Non agency	109	-	218	-	327
Below investment grade					
Corporate	-	99	18	-	117
Mortgage backed – non agency	-	-	7	-	7
Non rated <sup>3</sup>	122	-	32	-	154
<b>Debt securities</b>	<b>4,221</b>	<b>196</b>	<b>6,812</b>	<b>-</b>	<b>11,229</b>
Investment grade					
Retractable	24	-	-	-	24
Fixed-rate perpetual	285	-	-	-	285
Other perpetual	1,100	-	-	-	1,100
<b>Preferred shares</b>	<b>1,409</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>1,409</b>
<b>Common shares</b>	<b>2,272</b>	<b>357</b>	<b>1,030</b>	<b>-</b>	<b>3,659</b>
<b>Loans</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>393</b>	<b>393</b>
	<b>7,902</b>	<b>553</b>	<b>7,842</b>	<b>556</b>	<b>16,853</b>

<sup>1</sup> Consist of credit card receivables and auto loans.

<sup>2</sup> Consist of publicly traded MBS, which carry the full faith and credit guarantee of the U.S. Government or are guaranteed by a Government sponsored entity.

<sup>3</sup> Included \$40 million of MBS as at December 31, 2017 and nil as at June 30, 2018.

## INTACT FINANCIAL CORPORATION

### Notes to the interim Consolidated financial statements (unaudited)

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

#### 5.2 Carrying value of investments

Table 5.2 – Carrying value of investments

As at	FVTPL	Amortized	Unrealized	Unrealized	Other	Total
	investments				investments	investments
	Carrying	cost	gains	losses	Carrying	Carrying
	value				value	value
<b>June 30, 2018</b>						
Cash and cash equivalents	-	287	-	-	287	287
Debt securities	6,144	5,249	27	(38)	5,238	11,382
Preferred shares	-	1,276	72	(19)	1,329	1,329
Common shares	1,140	2,369	192	(75)	2,486	3,626
Loans	-	322	-	-	322	322
	<b>7,284</b>	<b>9,503</b>	<b>291</b>	<b>(132)</b>	<b>9,662</b>	<b>16,946</b>
<b>December 31, 2017</b>						
Cash and cash equivalents	-	163	-	-	163	163
Debt securities	7,008	4,199	43	(21)	4,221	11,229
Preferred shares	-	1,330	95	(16)	1,409	1,409
Common shares	1,387	2,060	263	(51)	2,272	3,659
Loans	-	393	-	-	393	393
	<b>8,395</b>	<b>8,145</b>	<b>401</b>	<b>(88)</b>	<b>8,458</b>	<b>16,853</b>

As at June 30, 2018, approximately 92% of the fixed-income securities were rated 'A-' or better and 80% of the preferred shares were highly-rated with at least a 'P2L' credit rating (December 31, 2017 – 90% and 79% respectively).

#### 5.3 Market neutral equity investment strategy

Table 5.3 – Market neutral equity investment strategy

As at	June 30, 2018		December 31, 2017	
	Fair value	Collateral	Fair value	Collateral
Long positions – common shares	128	-	121	-
Short positions (Table 6.1)	(130)	132	(122)	126

#### Note 6 – Financial liabilities related to investments

Table 6.1 – Financial liabilities related to investments

As at	June 30, 2018	December 31, 2017
Accounts payable to investment brokers on unsettled trades	135	24
Equities sold short positions (Table 5.3)	130	122
Derivative financial liabilities (Table 7.1)	91	21
Embedded derivatives	71	79
	<b>427</b>	<b>246</b>

**INTACT FINANCIAL CORPORATION**

**Notes to the interim Consolidated financial statements (unaudited)**

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

**Note 7 – Derivative financial instruments**

**7.1 Fair value and notional amount of derivatives**

The Company uses derivatives for economic hedging purposes and for the purpose of improving the risk profile of its investment portfolio, as long as the resulting exposures remain within the guidelines of its investment policy. In certain circumstances, these hedges also meet the requirements for hedge accounting. Risk management strategies eligible for hedge accounting have been designated as net investment hedges in foreign operations.

Table 7.1 – Fair value and notional amount of derivatives by nature of risk

As at	June 30, 2018			December 31, 2017		
	Notional amount	Fair value		Notional amount	Fair value	
		Asset	Liability		Asset	Liability
<b>Foreign currency contracts<sup>1</sup></b>						
Forwards	1,751	1	74	1,852	8	13
<b>Interest rate contracts</b>						
Futures and forwards	1,073	-	-	1,317	-	-
<b>Equity contracts</b>						
Swap agreements	981	2	17	1,022	-	8
Futures	180	-	-	247	-	-
<b>Inflation options</b>						
Options	54	-	-	63	-	-
	<b>4,039</b>	<b>3</b>	<b>91</b>	<b>4,501</b>	<b>8</b>	<b>21</b>
Held for risk management purposes	3,980	3	91	4,337	8	21
Held for trading purposes	59	-	-	164	-	-
	<b>4,039</b>	<b>3</b>	<b>91</b>	<b>4,501</b>	<b>8</b>	<b>21</b>
<b>Term to maturity:</b>						
less than one year	4,039			4,279		
from one to five years	-			222		
	<b>4,039</b>			<b>4,501</b>		

<sup>1</sup> Includes net investment hedges of foreign subsidiaries.

INTACT FINANCIAL CORPORATION

Notes to the interim Consolidated financial statements (unaudited)

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

Note 8 – Fair value measurement

8.1 Categorization of fair values

Table 8.1 – Fair value hierarchy of financial assets and financial liabilities measured at fair value

As at	Level 1 Valued using quoted (unadjusted) market prices	Level 2 Valued using models (with observable inputs)	Level 3 Valued using models (without observable inputs)	Total
<b>June 30, 2018</b>				
Short-term notes	64	-	-	64
Fixed income				
Investment grade				
Government	2,700	2,335	-	5,035
Corporate	-	4,217	-	4,217
Asset backed	-	710	-	710
Mortgage backed				
Agency	-	595	-	595
Non agency	-	607	-	607
Below investment grade				
Corporate	-	7	-	7
Non rated	-	-	147	147
<b>Debt securities</b>	<b>2,764</b>	<b>8,471</b>	<b>147</b>	<b>11,382</b>
<b>Preferred shares</b>	<b>1,258</b>	<b>-</b>	<b>71</b>	<b>1,329</b>
<b>Common shares</b>	<b>3,600</b>	<b>-</b>	<b>26</b>	<b>3,626</b>
<b>Derivative financial assets (Table 7.1)</b>	<b>-</b>	<b>3</b>	<b>-</b>	<b>3</b>
<b>Total financial assets measured at fair value</b>	<b>7,622</b>	<b>8,474</b>	<b>244</b>	<b>16,340</b>
<b>Total financial liabilities measured at fair value</b>	<b>130</b>	<b>91</b>	<b>71</b>	<b>292</b>
<b>December 31, 2017</b>				
Short-term notes	217	-	-	217
Fixed income				
Investment grade				
Government	2,902	2,305	-	5,207
Corporate	-	3,873	-	3,873
Asset backed	-	987	-	987
Mortgage backed				
Agency	-	340	-	340
Non agency	-	327	-	327
Below investment grade				
Corporate	-	117	-	117
Mortgage backed – non agency	-	7	-	7
Non rated	-	43	111	154
<b>Debt securities</b>	<b>3,119</b>	<b>7,999</b>	<b>111</b>	<b>11,229</b>
<b>Preferred shares</b>	<b>1,330</b>	<b>-</b>	<b>79</b>	<b>1,409</b>
<b>Common shares</b>	<b>3,595</b>	<b>35</b>	<b>29</b>	<b>3,659</b>
<b>Derivative financial assets (Table 7.1)</b>	<b>-</b>	<b>8</b>	<b>-</b>	<b>8</b>
<b>Total financial assets measured at fair value</b>	<b>8,044</b>	<b>8,042</b>	<b>219</b>	<b>16,305</b>
<b>Total financial liabilities measured at fair value</b>	<b>122</b>	<b>21</b>	<b>79</b>	<b>222</b>

The fair value of loans presented at amortized cost was \$313 million as at June 30, 2018 (December 31, 2017 – \$384 million).

## INTACT FINANCIAL CORPORATION

### Notes to the interim Consolidated financial statements (unaudited)

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

#### Note 9 – Claims liabilities

Claims liabilities are established to reflect the estimate of the full amount of all liabilities associated with the insurance contracts earned at the balance sheet date, including IBNR, that have occurred on or before the balance sheet date. The ultimate amount of these liabilities will vary from the best estimate made for a variety of reasons, including additional information with respect to the facts and circumstances of the insurance claims incurred. To recognize the uncertainty in establishing this best estimate, to allow for possible deterioration in experience and to provide greater comfort that the actuarial liabilities are sufficient to pay future benefits, actuaries are required to include margins in some assumptions.

#### 9.1 Movements in claims liabilities

Table 9.1 – Movements in claims liabilities

For the three-month periods ended	Direct	Ceded	Net
<b>June 30, 2018</b>			
Balance, beginning of period	10,567	707	9,860
Current period claims	1,662	22	1,640
Unfavourable (favourable) prior year claims development	(10)	22	(32)
Increase (decrease) due to changes in discount rate	(46)	(7)	(39)
Total claims incurred	1,606	37	1,569
Claims paid	(1,579)	(33)	(1,546)
Business combinations	(2)	-	(2)
Exchange rate differences	42	9	33
<b>Balance, end of period</b>	<b>10,634</b>	<b>720</b>	<b>9,914</b>
<b>June 30, 2017</b>			
Balance, beginning of period	8,599	457	8,142
Current period claims	1,403	13	1,390
Unfavourable (favourable) prior year claims development	(44)	(4)	(40)
Increase (decrease) due to changes in discount rate	(36)	-	(36)
Total claims incurred	1,323	9	1,314
Claims paid	(1,333)	(34)	(1,299)
<b>Balance, end of period</b>	<b>8,589</b>	<b>432</b>	<b>8,157</b>
For the six-month periods ended	Direct	Ceded	Net
<b>June 30, 2018</b>			
Balance, beginning of period	10,475	729	9,746
Current period claims	3,405	48	3,357
Unfavourable (favourable) prior year claims development	(82)	16	(98)
Increase (decrease) due to changes in discount rate	(102)	(11)	(91)
Total claims incurred	3,221	53	3,168
Claims paid	(3,154)	(82)	(3,072)
Business combinations	(2)	-	(2)
Exchange rate differences	94	20	74
<b>Balance, end of period</b>	<b>10,634</b>	<b>720</b>	<b>9,914</b>
<b>June 30, 2017</b>			
Balance, beginning of period	8,536	465	8,071
Current period claims	2,900	42	2,858
Unfavourable (favourable) prior year claims development	(134)	(11)	(123)
Increase (decrease) due to changes in discount rate	(22)	-	(22)
Total claims incurred	2,744	31	2,713
Claims paid	(2,691)	(64)	(2,627)
<b>Balance, end of period</b>	<b>8,589</b>	<b>432</b>	<b>8,157</b>

## INTACT FINANCIAL CORPORATION

### Notes to the interim Consolidated financial statements (unaudited)

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

#### Note 10 – Reinsurance

##### 10.1 Company's reinsurance net retention and coverage limits by nature of risk

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

Table 10.1 – Company's reinsurance net retention and coverage limits by nature of risk

As at	June 30, 2018	December 31, 2017
<b>Single risk events</b>		
Retentions Canada:		
on property policies	7.5	7.5
on liability policies	3 - 10	3 - 10
Retentions U.S. (USD):		
on property and liability policies	3	3
<b>Multi-risk events and catastrophes</b>		
Retention	100	100
Coverage limits	3,725	3,600

For certain special classes of business or types of risks, the retention for single risk events may be lower through specific treaties or the use of facultative reinsurance. For multi-risk events and catastrophes, the Company retains participations averaging 5.6% as at June 30, 2018 (December 31, 2017 – 5.1%) on reinsurance layers between the retention and coverage limit. The coverage limit prudently exceeds the Company's risk assessment of an earthquake in Western Canada at a 1-in-500 year return period.

Since January 1, 2018, the Company's U.S. operations are covered by the multi-risk events and catastrophes reinsurance program. Until April 30, 2018, the losses resulting from any single catastrophe above US\$20 million and up to US\$130 million of losses were being reinsured.

In connection with the acquisition of OneBeacon, the Company entered into a reinsurance contract pursuant to which a major reinsurer will assume 80% of negative reserve development with respect to OneBeacon's claims liabilities for accident years 2016 and prior. The maximum amount recoverable under the reinsurance agreement is US\$200 million and is subject to some exclusions and limitations.

##### 10.2 Components of reinsurance assets

Table 10.2 – Components of reinsurance assets

As at	June 30, 2018	December 31, 2017
Reinsurers' share of claims liabilities ( <i>Table 9.1</i> )	720	729
Reinsurers' share of unearned premiums	105	93
	825	822

## INTACT FINANCIAL CORPORATION

### Notes to the interim Consolidated financial statements (unaudited)

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

#### Note 11 – Other assets and other liabilities

##### 11.1 Other assets

Table 11.1 – Components of other assets

As at	June 30, 2018	December 31, 2017
Industry pools receivable	109	100
Guaranteed loan <sup>1</sup>	109	96
Restricted funds	107	111
Other receivables and recoverables	93	112
Financial assets related to investments	82	34
Accrued investment income	78	76
Investments, at cost	54	54
Prepays	52	43
Premium and sale taxes receivable	39	38
Pension plans in a surplus position	30	5
Reinsurance receivable	21	60
Other	54	53
	<b>828</b>	<b>782</b>

<sup>1</sup> Recorded at fair value based on a discounted cash flow model using information as of the measurement date and classified in Level 3 of the fair value hierarchy.

During the six-month period ended June 30, 2018, there were no events or changes in circumstances that indicated that the carrying value of Investments at cost may not be recoverable.

##### 11.2 Other liabilities

Table 11.2 – Components of other liabilities

As at	June 30, 2018	December 31, 2017
Deposits received in connection with insurance contracts <sup>1</sup>	339	197
Premium and sale taxes payable	194	233
Commissions payable	177	199
Accrued salaries and other short-term benefits	129	177
Pension plans in a deficit position and unfunded plans	109	140
Account payables and accrued expenses	102	175
Industry pools payable	100	99
Other post-employment benefits and other post-retirement benefits	53	52
Deposits received from reinsurers	17	25
Other payables and other liabilities	308	322
	<b>1,528</b>	<b>1,619</b>

<sup>1</sup> Unrestricted collateral held by the Company primarily in relation with the surety business.

## INTACT FINANCIAL CORPORATION

### Notes to the interim Consolidated financial statements (unaudited)

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

## Note 12 – Debt outstanding

### 12.1 Summary of debt outstanding

Table 12.1 – Carrying value of debt outstanding

As at	Maturity date	Initial term (years)	Fixed rate	Coupon (payment)	Principal amount	Carrying value (net of fees)	
						June 30, 2018	December 31, 2017
<b>Term notes</b>							
Series 1	Sept. 2019	10	5.41%	Mar. & Sept.	250	250	250
Series 2	Nov. 2039	30	6.40%	May & Nov.	250	248	248
Series 3	July 2061	50	6.20%	Jan. & July	100	99	99
Series 4	Aug. 2021	10	4.70%	Feb. & Aug.	300	299	299
Series 5	June 2042	30	5.16%	June & Dec.	250	249	249
Series 6	Mar. 2026	10	3.77%	Mar. & Sept.	250	249	249
Series 7	June 2027	10	2.85%	June & Dec.	425	422	422
<b>2012 U.S. Senior Notes</b>	Nov. 2022	10	4.60%	May & Nov.	USD 275	<b>380</b>	365
<b>Credit facility</b>						<b>70</b>	60
						<b>2,266</b>	2,241

The term notes are accounted for at amortized cost which equals their carrying value. They may be redeemed at the option of the issuer, in whole or in part at any time, at a redemption price equal to the greater of a value calculated using the yield on Government of Canada bonds at the date of redemption plus a margin or their par value.

Fair value of debt outstanding amounted to \$2,457 million as at June 30, 2018 (December 31, 2017 – \$2,449 million), and was established using valuation data from a benchmark firm. As at June 30, 2018, the Company was in compliance with all debt covenants.

## Note 13 – Preferred shares

### 13.1 New financing

<b>Series 7 Preferred Shares</b>	<ul style="list-style-type: none"> <li>On May 29, 2018, the Company completed a Series 7 offering of preferred shares (the "Series 7 Preferred Shares") by issuing and selling 10,000,000 Series 7 Preferred Shares, at a price of \$25.00 per share, for aggregate gross proceeds of \$250 million. Share issuance costs of \$7 million (\$5 million after tax), were accounted for as a reduction in preferred shares on the interim Consolidated financial statements.</li> <li>The holders of the Series 7 Preferred Shares are entitled to receive fixed quarterly non-cumulative preferential cash dividends, if, as and when declared by the Board of Directors of the Company, on the last day of March, June, September and December in each year at an annual rate equal to \$1.225 per share. The initial dividend, if declared, will be payable on September 28, 2018, and will be \$0.4162 per share.</li> <li>The holders of the Series 7 Preferred Shares will have the right, at their option, to convert their Series 7 Preferred Shares into Non-cumulative Floating Rate Class A Shares, Series 8 (the "Series 8 Preferred Shares"), subject to certain conditions, on June 30, 2023, and on June 30 every five years thereafter. The holders of Series 8 Preferred Shares will be entitled to receive quarterly floating rate non-cumulative preferential cash dividends, as and when declared by the Board of Directors of the Company, on the last day of March, June, September and December in each year at an annualized rate equal to the 90-day Canadian Treasury Bill rate plus 2.55%.</li> </ul>
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## INTACT FINANCIAL CORPORATION

### Notes to the interim Consolidated financial statements (unaudited)

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

#### 13.2 Issued and outstanding shares

Table 13.2 – Issued and outstanding shares

As at	June 30, 2018		December 31, 2017	
	Number of shares	Amount	Number of shares	Amount
<b>Preferred shares - Class A Shares</b>				
Series 1	10,000,000	244	10,000,000	244
Series 3	8,405,004	206	8,405,004	206
Series 4	1,594,996	39	1,594,996	39
Series 5	6,000,000	147	6,000,000	147
Series 6	6,000,000	147	6,000,000	147
Series 7	10,000,000	245	-	-
<b>Total Class A</b>	<b>42,000,000</b>	<b>1,028</b>	<b>32,000,000</b>	<b>783</b>

Table 13.3 – Reconciliation of number of shares outstanding

As at	Preferred shares Class A shares (in shares)	
	June 30, 2018	December 31, 2017
Balance, beginning of period	32,000,000	20,000,000
Issued	10,000,000	12,000,000
<b>Balance, end of period</b>	<b>42,000,000</b>	<b>32,000,000</b>

Issued and outstanding Class A shares rank in priority to common shares with regards to payment of dividends.

## Note 14 – Capital management

### 14.1 Capital management objectives

The Company's objectives when managing capital consist of:

- maintaining strong regulatory capital levels (see Regulatory capital section below), while ensuring policyholders are well protected; and
- maximizing long-term shareholder value by optimizing capital used to operate and grow the Company.

The Company seeks to maintain adequate capital margin to ensure the probability of breaching the regulatory minimum requirements is very low. Such levels may vary over time depending on the Company's evaluation of risks and their potential impact on capital. The Company also keeps higher levels of capital margin when it foresees growth or actionable opportunities in the near term. Furthermore, the Company may return capital to shareholders through annual dividend increases and, when appropriate, through share buybacks.

#### **Regulatory capital**

The amount of capital deployed in any particular company or country is dependent upon local regulatory requirements, as well as the Company's internal assessment of capital requirements in the context of its risk profiles, requirements and strategic plans. The Company's practice is to maintain the capitalization of its regulated operating subsidiaries at a level that will exceed the relevant minimum regulatory capital requirements in the jurisdictions in which they operate (referred to as regulator supervisory minimum levels). Regulatory capital guidelines change from time to time and may impact the Company's capital levels. The Company carefully monitors all changes, actual or proposed.

## INTACT FINANCIAL CORPORATION

### Notes to the interim Consolidated financial statements (unaudited)

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

<b>Canada</b>	The Company's federally chartered Canadian P&C insurance subsidiaries are subject to the regulatory capital requirements defined by OSFI and the <i>Insurance Companies Act</i> , while its Québec provincially chartered subsidiaries are subject to the requirements of the AMF and the <i>Act respecting Insurance</i> . Federal and Québec regulated P&C insurers are required, at a minimum, to maintain a MCT ratio of 100%. OSFI and the AMF have also established a regulator supervisory target capital ratio of 150%, which provides a cushion above the minimum requirement.
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<b>U.S.</b>	The Company's U.S. insurance operations are subject to regulation and supervision in each of the states where they are domiciled and licensed to conduct business. State insurance departments have established the insurer solvency laws and regulatory infrastructure to maintain accredited status with the National Association of Insurance Commissioners ("NAIC"). A key solvency-driven NAIC accreditation requirement is a state's adoption of RBC requirements. Dividends from our major U.S. insurance subsidiary are subject to the New York Regulator's prior approval for a two year period ending September 30, 2019.
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#### 14.2 Capital position

As at June 30, 2018 and December 31, 2017, all the Company's regulated P&C insurance subsidiaries were well capitalized on an individual basis with capital levels well in excess of regulator supervisory minimum levels, as well as CALs. CALs represent the thresholds below which regulator notification is required together with a company action plan to restore capital levels.

Table 14.1 – Estimated aggregate capital position

As at	June 30, 2018			December 31, 2017		
	Canada (MCT)	U.S. (RBC)	IFC Capital margin	Canada (MCT)	U.S. (RBC)	IFC Capital margin
<b>Regulatory capital ratios</b>	<b>201%</b>	<b>405%</b>	-	205%	459%	-
Industry-wide supervisory minimum levels	150%	150%	-	150%	150%	-
CALs	170%	200%	-	170%	200%	-
Capital above CALs (capital margin)	550	415	965	618	438	1,056
Other regulated / unregulated entities <sup>1</sup>	-	-	278	-	-	79
<b>Total capital margin</b>			<b>1,243</b>			<b>1,135</b>

<sup>1</sup> Other regulated entities include Split Rock Insurance, Ltd. (Bermuda) and IB Reinsurance Inc. (Barbados).

U.S. capital levels comprise the RBC levels of OneBeacon's U.S. regulated entities consolidated in Atlantic Specialty Insurance Company.

IFC's total capital margin represents the aggregate of capital in excess of CALs in regulated entities as well as unrestricted cash and invested assets in unregulated entities.

**INTACT FINANCIAL CORPORATION**
**Notes to the interim Consolidated financial statements (unaudited)**

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

**Note 15 – Net investment income**

Table 15.1 – Net investment income

For the periods ended June 30,	Three months		Six months	
	2018	2017	2018	2017
Interest income from:				
debt securities				
designated or classified as FVTPL	47	37	97	75
classified as AFS	31	22	58	43
loans and cash and cash equivalents	7	6	13	11
<b>Interest income</b>	<b>85</b>	<b>65</b>	<b>168</b>	<b>129</b>
Dividend income (expense) from:				
common shares, net				
designated or classified as FVTPL	16	16	31	31
classified as AFS	26	21	46	42
preferred shares				
classified as AFS	16	15	30	31
equities sold short positions	(1)	(3)	(2)	(5)
<b>Dividend income</b>	<b>57</b>	<b>49</b>	<b>105</b>	<b>99</b>
<b>Expenses</b>	<b>(8)</b>	<b>(9)</b>	<b>(17)</b>	<b>(18)</b>
	<b>134</b>	<b>105</b>	<b>256</b>	<b>210</b>

**Note 16 – Net gains (losses)**

Table 16.1 – Net gains (losses)

For the three-month periods ended June 30,	2018			2017		
	Fixed income	Equity	Total	Fixed income	Equity	Total
<b>Strategies</b>						
Net gains (losses) from:						
financial instruments:						
designated as FVTPL	(31)	31	-	(43)	(28)	(71)
classified as FVTPL	1	-	1	-	-	-
classified as AFS	(5)	36	31	1	37	38
	(35)	67	32	(42)	9	(33)
derivatives <sup>1</sup> :						
swap agreements	-	(40)	(40)	-	20	20
futures	(2)	(11)	(13)	-	4	4
interest rate contracts	-	-	-	4	-	4
forwards	-	(1)	(1)	-	-	-
	(2)	(52)	(54)	4	24	28
Embedded derivatives	-	(4)	(4)	-	(6)	(6)
Net foreign currency gains (losses), net	(1)	-	(1)	-	18	18
Impairment losses from common shares	-	(3)	(3)	-	(1)	(1)
	(38)	8	(30)	(38)	44	6
Currency derivative gain related to book value						
hedge of OneBeacon <sup>2</sup>			-			41
Other gains (losses) <sup>3</sup>			3			12
			(27)			59

**INTACT FINANCIAL CORPORATION**
**Notes to the interim Consolidated financial statements (unaudited)**

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

For the six-month periods ended June 30,	2018			2017		
	Fixed income	Equity	Total	Fixed income	Equity	Total
Strategies						
Net gains (losses) from:						
financial instruments:						
designated as FVTPL	(83)	(64)	(147)	(40)	(19)	(59)
classified as FVTPL	(3)	(2)	(5)	-	-	-
classified as AFS	(13)	116	103	3	120	123
	(99)	50	(49)	(37)	101	64
derivatives <sup>1</sup> :						
swap agreements	-	45	45	-	2	2
futures	(1)	4	3	-	1	1
interest rate contracts	-	-	-	4	-	4
forwards	-	(1)	(1)	-	-	-
	(1)	48	47	4	3	7
Embedded derivatives	-	(6)	(6)	-	(25)	(25)
Net foreign currency gains (losses), net	(1)	-	(1)	-	32	32
Impairment losses from common shares	-	(22)	(22)	-	(1)	(1)
	(101)	70	(31)	(33)	110	77
Currency derivative gain related to book value hedge of OneBeacon <sup>2</sup>			-			41
Other gains (losses) <sup>3</sup>			9			16
			(22)			134

<sup>1</sup> Excluding foreign currency contracts, which are reported in Net foreign currency gains (losses) in the interim Consolidated statements of income.

<sup>2</sup> See Note 4 – Business combination for details.

<sup>3</sup> Including net gains on investments in associates and joint ventures related to a change in ownership interests and foreign currency.

**Note 17 – Income taxes**
**17.1 Income tax expense recorded in Net income**

Table 17.1 – Components of income tax expense recorded in Net income

For the periods ended June 30,	Three months		Six months	
	2018	2017	2018	2017
Current income tax expense				
Current year	39	69	54	146
Deferred income tax expense (benefit)				
Change related to temporary differences	(1)	(17)	1	(59)
	38	52	55	87

## INTACT FINANCIAL CORPORATION

### Notes to the interim Consolidated financial statements (unaudited)

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

#### 17.2 Effective income tax rate

The effective income tax rates are different from the combined statutory income tax rates. The interim Consolidated statements of income contain items that are non-taxable or non-deductible for income tax purposes, which cause the income tax expense to differ from what it would have been if based on statutory tax rates.

The following table presents the reconciliation of the effective income tax rate to the income tax expense calculated at statutory rates.

Table 17.2 – Effective income tax rate reconciliation

For periods ended June 30,	Three months		Six months	
	2018	2017	2018	2017
Income tax expense calculated at statutory tax rates	26.9%	26.9%	26.9%	26.9%
Increase (decrease) in income tax rates resulting from:				
non-taxable investment income	(4.8)%	(3.1)%	(6.0)%	(3.8)%
non-deductible losses (non-taxable income) from subsidiaries	(2.4)%	(1.1)%	(1.4)%	(0.8)%
foreign income taxed at different rates	(0.9)%	-	(2.2)%	-
non-taxable income	(0.5)%	(0.6)%	(1.2)%	(0.6)%
non-taxable gains	(0.4)%	(5.1)%	(0.3)%	(3.9)%
non-deductible expenses	0.8%	0.7%	0.7%	0.6%
other	0.4%	(0.1)%	0.7%	(0.1)%
<b>Effective income tax rate</b>	<b>19.1%</b>	<b>17.6%</b>	<b>17.2%</b>	<b>18.3%</b>

#### Note 18 – Earnings per share

EPS was calculated by dividing the Net income attributable to common shareholders of the Company by the weighted-average number of common shares outstanding during the period. Dilution is not applicable and, therefore, diluted EPS is the same as basic EPS.

Table 18.1 – Earnings per share

For the periods ended June 30,	Three months		Six months	
	2018	2017	2018	2017
Net income attributable to shareholders	161	243	264	389
Less: dividends declared on preferred shares, net of tax	(8)	(4)	(16)	(9)
<b>Net income attributable to common shareholders</b>	<b>153</b>	<b>239</b>	<b>248</b>	<b>380</b>
<b>Weighted-average number of common shares outstanding</b> (in millions)	<b>139.2</b>	<b>131.0</b>	<b>139.2</b>	<b>131.0</b>
<b>EPS – basic and diluted (in dollars)</b>	<b>1.10</b>	<b>1.82</b>	<b>1.78</b>	<b>2.90</b>

## INTACT FINANCIAL CORPORATION

### Notes to the interim Consolidated financial statements (unaudited)

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

#### Note 19 – Share-based payments

##### 19.1 Long-term incentive plan

Table 19.1 – Movements in LTIP share units

For the periods ended June 30,	Three months		Six months	
	2018 (in units)	2017 (in units)	2018 (in units)	2017 (in units)
Outstanding, beginning of period	941,097	772,638	774,783	702,246
Awarded	248,243	2,023	444,482	194,492
Net change in estimate of units outstanding	20,462	18,881	47,831	(24,812)
Units settled	(196,540)	(177,534)	(253,834)	(255,918)
<b>Outstanding, end of period</b>	<b>1,013,262</b>	<b>616,008</b>	<b>1,013,262</b>	<b>616,008</b>

The LTIP expense was \$14 million and \$23 million for the three- and six-month periods ended June 30, 2018, respectively (\$6 million and \$7 million for the three- and six-month periods ended June 30, 2017, respectively).

##### 19.2 Employee share purchase plan

Table 19.2 – Movements in restricted common shares

For the periods ended June 30,	Three months		Six months	
	2018 (in units)	2017 (in units)	2018 (in units)	2017 (in units)
Outstanding, beginning of period	134,229	139,005	132,491	145,368
Accrued	37,424	32,140	71,437	66,717
Awarded and vested	(34,686)	(27,273)	(65,009)	(66,084)
Forfeited	(1,976)	(1,649)	(3,928)	(3,778)
<b>Outstanding, end of period</b>	<b>134,991</b>	<b>142,223</b>	<b>134,991</b>	<b>142,223</b>

The ESPP expense was \$3 million and \$8 million for the three- and six-month periods ended June 30, 2018 and 2017.

##### 19.3 Deferred share unit

The DSU provision amounted to \$10 million as at June 30, 2018 and December 31, 2017.

##### 19.4 Common shares repurchased for share-based payments

The settlement in shares with regards to the Company's LTIP and ESPP plans is presented below.

Table 19.3 – Settlement in shares (LTIP and ESPP plans)

For the periods ended June 30,	Three months		Six months	
	2018	2017	2018	2017
Value of common shares repurchased for share-based payments	21	20	29	30
Cumulative cost of the units for the Company	17	15	24	23
Excess of market price over the cumulative cost for the Company	4	5	5	7
Amount recognized in Retained earnings, net of taxes	3	3	4	5

The cumulative cost of the units that vested during the period through the plan administrator purchasing common shares on the market and remitting them to the participants was removed from Contributed surplus. The difference between the market price of the shares and the cumulative cost for the Company of these vested units, net of income taxes, was recorded in Retained earnings in the interim Consolidated financial statements.

**INTACT FINANCIAL CORPORATION**

**Notes to the interim Consolidated financial statements (unaudited)**

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

**Note 20 – Employee future benefits**

**20.1 Employee future benefit expense recognized in Net income**

Table 20.1 – Employee future benefit expense recognized in Net income

For the periods ended June 30,	Pension plans			
	Three months		Six months	
	2018	2017	2018	2017
Current service cost	19	17	38	33
Net interest expense				
Interest expense on defined benefit obligation	19	18	38	36
Interest income on plan assets	(17)	(18)	(35)	(35)
Other	1	1	2	2
	22	18	43	36

**20.2 Actuarial gains (losses) recognized in OCI**

Table 20.2 – Actuarial gains (losses) recognized in OCI

For the periods ended June 30,	Pension plans			
	Three months		Six months	
	2018	2017	2018	2017
Re-measurements related to:				
change in discount rate used to determine the benefit obligation	37	(121)	66	(165)
actual return on plan assets	35	24	6	47
	72	(97)	72	(118)

**20.3 Discount rates used**

Table 20.3 – Discount rates used

For the periods ended June 30,	Pension plans			
	Three months		Six months	
	2018	2017	2018	2017
<b>To determine the defined benefit obligation as at:</b>				
beginning of period	3.6%	3.7%	3.5%	3.8%
end of period	3.7%	3.4%	3.7%	3.4%
Increase (decrease) in discount rate	0.1%	(0.3)%	0.2%	(0.4)%
<b>To determine the benefit expense for the periods</b>				
Current service cost	3.6%	3.9%	3.6%	3.9%
Interest expense	3.3%	3.3%-3.5%	3.3%	3.3%- 3.5%

## INTACT FINANCIAL CORPORATION

### Notes to the interim Consolidated financial statements (unaudited)

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

#### Note 21 – Segment information

##### 21.1 Reportable segments

The Company has two reportable segments, in line with its management structure and internal financial reporting which is based on geography and the nature of its activities.

###### Canada

- Underwriting of automobile, home and business insurance contracts to individuals and businesses in Canada distributed through a wide network of brokers and directly to consumers.
- Distribution operations, including the results from the Company's wholly-owned subsidiary (BrokerLink) and broker affiliates.

###### U.S.

- Underwriting of specialty contracts to small and midsize businesses in the United States. The Company distributes insurance through independent agencies, brokers, wholesalers and managing general agencies.

Corporate and Other ("Corporate") consists of centralized investing, treasury and capital management activities, as well as other corporate activities.

##### 21.2 Segment operating performance

All segment operating revenues presented in *Table 21.1 – Segment operating performance* are generated from external customers.

Management measures the profitability of the Company's segments based on pre-tax operating income ("PTOI"). PTOI excludes elements that are not representative of the Company's operating performance because they relate to special items, bear significant volatility from one period to another, or because they are not part of the Company's normal activities.

The reconciliation of the segment information to the amounts reported in the interim Consolidated statements of income is presented in *Table 21.2 - Reconciliation of segment information to amounts reported in the interim Consolidated statements of income*. Other underwriting revenues are netted against underwriting expenses when assessing segment performance for MD&A presentation and, as such, are not included in segment operating revenues. Revenues and expenses not allocated to segments mainly represent non-operating items excluded from PTOI.

Table 21.1 – Segment operating performance<sup>1</sup>

For the three-month periods ended June 30,	2018				2017			
	Canada	U.S.	Corporate	Total	Canada	U.S.	Corporate	Total
<b>Operating income</b>								
NEP	2,070	340	-	2,410	2,051	-	-	2,051
Investment income	-	-	142	142	-	-	114	114
Other	35	-	2	37	32	-	7	39
<b>Segment operating revenues</b>	<b>2,105</b>	<b>340</b>	<b>144</b>	<b>2,589</b>	<b>2,083</b>	<b>-</b>	<b>121</b>	<b>2,204</b>
Net claims incurred (before MYA)	(1,391)	(194)	-	(1,585)	(1,345)	-	-	(1,345)
Underwriting expenses <sup>2</sup>	(607)	(125)	-	(732)	(603)	-	-	(603)
Investment expenses	-	-	(8)	(8)	-	-	(9)	(9)
Share of profit from invest. in associates & JV	20	-	-	20	18	-	-	18
Finance costs	-	-	(26)	(26)	-	-	(19)	(19)
Other	(3)	-	(11)	(14)	-	-	(8)	(8)
<b>PTOI<sup>3</sup></b>	<b>124</b>	<b>21</b>	<b>99</b>	<b>244</b>	<b>153</b>	<b>-</b>	<b>85</b>	<b>238</b>
<b>Comprised of:</b>								
underwriting income	72	21	-	93	103	-	-	103
net investment income	-	-	134	134	-	-	105	105
net distribution income	52	-	-	52	50	-	-	50
finance costs	-	-	(26)	(26)	-	-	(19)	(19)
other income (expense)	-	-	(9)	(9)	-	-	(1)	(1)

## INTACT FINANCIAL CORPORATION

### Notes to the interim Consolidated financial statements (unaudited)

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

For the six-month periods ended June 30,	2018				2017			
	Canada	U.S.	Corporate	Total	Canada	U.S.	Corporate	Total
<b>Operating income</b>								
NEP	4,090	654	-	4,744	4,048	-	-	4,048
Investment income	-	-	273	273	-	-	228	228
Other	64	-	4	68	59	-	15	74
<b>Segment operating revenues</b>	<b>4,154</b>	<b>654</b>	<b>277</b>	<b>5,085</b>	<b>4,107</b>	<b>-</b>	<b>243</b>	<b>4,350</b>
Net claims incurred (before MYA)	(2,823)	(375)	-	(3,198)	(2,726)	-	-	(2,726)
Underwriting expenses <sup>2</sup>	(1,191)	(243)	-	(1,434)	(1,184)	-	-	(1,184)
Investment expenses	-	-	(17)	(17)	-	-	(18)	(18)
Share of profit from invest. in associates & JV	29	-	-	29	26	-	-	26
Finance costs	-	-	(51)	(51)	-	-	(38)	(38)
Other	(17)	-	(14)	(31)	(11)	-	(11)	(22)
<b>PTOI<sup>3</sup></b>	<b>152</b>	<b>36</b>	<b>195</b>	<b>383</b>	<b>212</b>	<b>-</b>	<b>176</b>	<b>388</b>
<b>Comprised of:</b>								
underwriting income	76	36	-	112	138	-	-	138
net investment income	-	-	256	256	-	-	210	210
net distribution income	76	-	-	76	74	-	-	74
finance costs	-	-	(51)	(51)	-	-	(38)	(38)
other income (expense)	-	-	(10)	(10)	-	-	4	4

<sup>1</sup> See Table 21.2 for the reconciliation to the interim Consolidated statements of income.

<sup>2</sup> Other underwriting revenues are netted against underwriting expenses when assessing segment performance.

<sup>3</sup> See Section 14 – Non IFRS financial measures of the Company's interim MD&A for the definition of related operating measures.

Table 21.2 – Reconciliation of segment information to amounts reported in the interim Consolidated statements of income

For the periods ended June 30,	Three months		Six months	
	2018	2017	2018	2017
<b>Segment operating revenues (Table 21.1)</b>	<b>2,589</b>	<b>2,204</b>	<b>5,085</b>	<b>4,350</b>
Add: other underwriting revenues	27	26	54	54
Add: NEP exited lines <sup>1</sup>	14	-	34	-
<b>Revenues, as reported</b>	<b>2,630</b>	<b>2,230</b>	<b>5,173</b>	<b>4,404</b>
<b>Segment PTOI (Table 21.1)</b>	<b>244</b>	<b>238</b>	<b>383</b>	<b>388</b>
<b>Non-operating items:</b>				
net gains (losses)	(27)	59	(22)	134
positive (negative) impact on MYA on underwriting integration and restructuring costs	39	34	91	21
amortization of intangible assets recognized in business combinations	(14)	(8)	(39)	(12)
difference between expected return and discount rate on pension assets	(23)	(13)	(43)	(25)
underwriting results from OneBeacon exited lines	(13)	(11)	(25)	(22)
other non-operating costs	(4)	-	(19)	-
other non-operating costs	(3)	(4)	(7)	(8)
<b>Pre-tax income, as reported</b>	<b>199</b>	<b>295</b>	<b>319</b>	<b>476</b>

<sup>1</sup> Includes the results of the U.S. Commercial's business lines Programs and Architects and Engineers.

### 21.3 Selected segment assets and liabilities

Table 21.3 – Selected segment assets and liabilities

As at	June 30, 2018				December 31, 2017			
	Canada	U.S.	Corporate	Total	Canada	U.S.	Corporate	Total
<b>Investments</b>	-	-	16,946	16,946	-	-	16,853	16,853
<b>Net claims liabilities (Table 9.1)</b>	<b>8,208</b>	<b>1,706</b>	<b>-</b>	<b>9,914</b>	<b>8,098</b>	<b>1,648</b>	<b>-</b>	<b>9,746</b>

## INTACT FINANCIAL CORPORATION

### Notes to the interim Consolidated financial statements (unaudited)

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

#### 21.4 Information by geographic areas

Table 21.4 – Information by geographic areas

	Revenues				Total assets	
	For the periods ended June 30				As at	
	Three months		Six months		June 30,	December 31,
	2018	2017	2018	2017	2018	2017
Canada	2,252	2,230	4,441	4,404	22,049	22,093
U.S.	378	-	732	-	6,361	5,835
	<b>2,630</b>	2,230	<b>5,173</b>	4,404	<b>28,410</b>	27,928

Revenues and assets are allocated based on the country where the risks originate.

### Note 22 – Additional information on the interim Consolidated statements of cash flows

#### 22.1 Adjustments for non-cash items

Table 22.1 – Adjustments for non-cash items

For the periods ended June 30,	Three months		Six months	
	2018	2017	2018	2017
Depreciation of property and equipment	9	9	18	17
Amortization of intangible assets	31	17	58	34
Net premiums on debt securities classified as AFS	5	3	10	5
Defined benefit pension expense	22	18	43	36
Share-based payments expense	17	9	31	15
Share of profit from investments in associates and joint ventures	(15)	(11)	(17)	(13)
Other	(1)	1	-	-
	<b>68</b>	46	<b>143</b>	94

#### 22.2 Changes in other operating assets and liabilities

Table 22.2 – Changes in other operating assets and liabilities

For the periods ended June 30,	Three months		Six months	
	2018	2017	2018	2017
Unearned premiums, net	433	420	102	105
Premium receivables, net	(393)	(363)	(129)	(87)
Deferred acquisition costs, net	(86)	(75)	(41)	(29)
Other operating assets	46	26	50	(3)
Other operating liabilities	101	65	(87)	(147)
Dividends received from investments in associates and joint ventures	5	4	7	8
	<b>106</b>	77	<b>(98)</b>	(153)

**Notes to the interim Consolidated financial statements (unaudited)**

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

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**Note 23 – Standards issued but not yet effective**

There have been no significant updates to Note 32 – *Standards issued but not yet effective* of the annual Consolidated financial statements for the year ended December 31, 2017, except as described below.

**23.1 Plan amendment, curtailment or settlement (amendments to IAS 19 – *Employee Benefits*)**

In February 2018, the IASB issued amendments to IAS 19 – *Employee Benefits* (“IAS 19”) to specify how companies determine pension expense when changes to a defined benefit pension plan occur. A company now uses updated assumptions from the remeasurement of the net defined benefit asset (liability) to determine the current service cost and net interest for the period. Previously, it would not have updated its calculation of these costs until year-end.

The amendments are to be applied prospectively, effective for annual periods beginning on or after January 1, 2019, with earlier application permitted. The Company will not early adopt the amendments to IAS 19.

**23.2 Conceptual framework for financial reporting**

In March 2018, the IASB issued a comprehensive set of concepts for financial reporting: the revised Conceptual Framework for Financial Reporting (“Conceptual Framework”), which replaces its previous version. It assists companies in developing accounting policies when no IFRS standard applies to a particular transaction and it helps stakeholders more broadly to better understand the standards.

The revised Conceptual Framework’s effective date is January 1, 2020, with earlier application permitted. The Company does not expect any impact upon its adoption.