



Consolidated Financial Statements of

**THE INDEPENDENT ORDER OF
FORESTERS**

Year ended December 31, 2008

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MANAGEMENT STATEMENT ON RESPONSIBILITY FOR FINANCIAL REPORTING

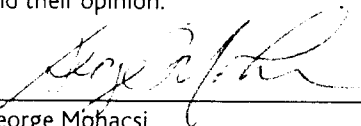
The consolidated financial statements have been prepared by management, who are responsible for their integrity, objectivity and reliability. Canadian generally accepted accounting principles including the accounting requirements of the Superintendent of Financial Institutions Canada ("OSFI") have been applied and management has exercised its judgement and made best estimates where deemed appropriate. In the opinion of management, the consolidated financial statements fairly reflect the financial position, results of operations and cash flows of The Independent Order of Foresters ("Foresters") within reasonable bounds of materiality.

Preparation of financial information is an integral part of management's broader responsibilities for the ongoing operations of Foresters. Management maintains an extensive system of internal accounting controls designed to ensure that transactions are accurately recorded on a timely basis, are properly approved and result in reliable financial statements. The adequacy of operation of the control systems is monitored by an internal audit department.

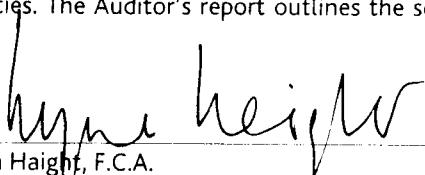
The Board of Directors, acting through the Inspection and Audit Committee, which comprises directors who are not officers or employees of Foresters, oversees management responsibility for the financial reporting and internal control system.

The Appointed Actuary is appointed by the Board of Directors to carry out an annual valuation of liabilities for future benefits. In performing this valuation, the Appointed Actuary is responsible for ensuring that the assumptions and methods used in the valuation of actuarial liabilities are in accordance with accepted actuarial practice and requirements. The Appointed Actuary is required to provide an opinion regarding the appropriateness of actuarial liabilities at the balance sheet date to meet all certificateholder obligations. Examination of supporting data for accuracy and completeness and analysis of assets for their ability to support the amount of actuarial liabilities are important elements of the work required to form this opinion. The Appointed Actuary is also required each year to analyze the financial condition of Foresters and prepare a report for the Board of Directors. The analysis tests the capital adequacy of Foresters under adverse economic conditions using the relevant Standards of Practice of the Canadian Institute of Actuaries. In carrying out her work the Appointed Actuary makes use of the work of the internal audit department and KPMG LLP Chartered Accountants ("Auditors"). The Actuary's report outlines the scope of the valuation and the Actuary's opinion.

Foresters engages Auditors to express an opinion on the financial statements. The responsibility of these Auditors is to carry out an independent and objective audit of the consolidated financial statements in accordance with Canadian generally accepted auditing standards and report regarding the fairness of presentation of Foresters consolidated financial statements in accordance with Canadian generally accepted accounting principles including the accounting requirements of OSFI. In carrying out their audit, the Auditors also make use of the work of the Appointed Actuary and her report on the actuarial liabilities. The Auditor's report outlines the scope of their audit and their opinion.



George Mohacsi
Chief Executive Officer



Lynn Haight, F.C.A.
Chief Financial Officer & Chief Membership Officer

Toronto, Canada
February 17, 2009



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AUDITORS' REPORT

To the Board of Directors of The Independent Order of Foresters

We have audited the consolidated balance sheets of The Independent Order of Foresters ("Foresters") and the separate statements of segregated funds' net assets as at December 31, 2008 and 2007 and the consolidated statements of income, comprehensive income (loss), surplus, cash flows and changes in segregated funds for the years then ended. These financial statements are the responsibility of Foresters management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of Foresters and its segregated funds as at December 31, 2008 and 2007 and the results of its operations, cash flows and changes in net assets of its segregated funds for the years then ended in accordance with Canadian generally accepted accounting principles.

Chartered Accountants, Licensed Public Accountants

Toronto, Canada

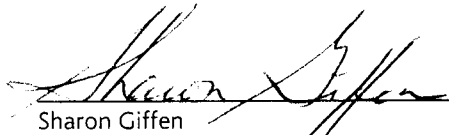
February 17, 2009

APPOINTED ACTUARY'S REPORT

The Board of Directors, The Independent Order of Foresters

I have valued the actuarial liabilities in the consolidated balance sheets of The Independent Order of Foresters as at December 31, 2008 and 2007 and their change in the consolidated statements of income (loss) for the years then ended in accordance with accepted actuarial practice, including selection of appropriate assumptions and methods.

In my opinion, the amount of actuarial liabilities makes appropriate provision for all certificate holder obligations and the consolidated financial statements fairly present the results of the valuation.



Sharon Giffen
Fellow, Canadian Institute of Actuaries
Toronto, Canada
February 17, 2009

THE INDEPENDENT ORDER OF FORESTERS

Consolidated Balance Sheets

As at December 31 (In thousands of Canadian dollars)

	2008	2007
Assets		
Investments (note 5)		
Cash and short-term securities	\$ 98,297	\$ 81,510
Bonds and other fixed-term securities	4,670,963	3,641,233
Mortgages	21,067	30,122
Stocks	969,166	1,215,531
Real estate	26,468	19,058
Loans to certificateholders	214,619	171,498
Other invested assets	105,248	147,798
	<u>6,105,828</u>	<u>5,306,750</u>
Other assets		
Interest due and accrued	56,064	46,992
Other assets	38,670	34,834
	<u>94,734</u>	<u>81,826</u>
Total assets	\$ 6,200,562	\$ 5,388,576

(See accompanying notes)

THE INDEPENDENT ORDER OF FORESTERS

Consolidated Balance Sheets

As at December 31 (In thousands of Canadian dollars)

	2008	2007
Liabilities and Surplus		
Liabilities		
Actuarial liabilities (note 8)		
Insurance	\$ 3,505,162	\$ 2,859,986
Annuities	849,069	615,547
Fraternal	359,242	331,320
	<u>4,713,473</u>	<u>3,806,853</u>
Other insurance certificate and contract liabilities		
Benefits payable and provision for unreported claims	64,585	32,532
Certificateholders' amounts on deposit	74,861	54,386
	<u>139,446</u>	<u>86,918</u>
Other liabilities	80,222	56,002
Deferred net gains realized on disposal of real estate	24,086	22,472
	<u>80,222</u>	<u>56,002</u>
Total liabilities	<u>4,957,227</u>	<u>3,972,245</u>
Surplus	<u>1,243,335</u>	<u>1,416,331</u>
Total liabilities and surplus	<u>\$ 6,200,562</u>	<u>\$ 5,388,576</u>

Contingent liabilities (note 12)
Subsequent event (note 13)

(See accompanying notes)

On behalf of the Board:



Director



Director

THE INDEPENDENT ORDER OF FORESTERS

Consolidated Statements of Income (Loss)

For the years ended December 31 (In thousands of Canadian dollars)

	2008	2007
Revenue		
Premiums		
Insurance	\$ 352,898	\$ 324,895
Annuities	97,745	57,984
Net investment income (loss) (note 5)	(94,725)	378,377
Other income	21,973	16,906
	<u>377,891</u>	<u>778,162</u>
Certificateholder benefits and expenses		
Certificateholder benefits	367,161	341,451
Change in actuarial liabilities (note 8)	(103,897)	48,424
Dividends	44,996	40,256
Agent compensation	92,843	55,507
Operating expenses	146,825	130,493
Fraternal investment	16,800	17,402
	<u>564,728</u>	<u>633,533</u>
Income (loss) before income taxes	<u>(186,837)</u>	<u>144,629</u>
Income taxes (note 9)		
Current	8,101	8,531
Future	2,188	(2,737)
	<u>10,289</u>	<u>5,794</u>
Net income (loss)	<u>\$ (197,126)</u>	<u>\$ 138,835</u>

(See accompanying notes)

THE INDEPENDENT ORDER OF FORESTERS

Consolidated Statements of Comprehensive Income (Loss)

For the years ended December 31 (In thousands of Canadian dollars)

	2008	2007
Net income (loss)	\$ (197,126)	\$ 138,835
Other comprehensive income (loss)		
Unrealized gains (losses) on available for sale assets, net of income tax of (\$2,288) (2007 - \$152)	(203,119)	(37,574)
Recognition of realized gains (losses) on available for sale assets, net of income tax of \$137 (2007 - \$849), to net income	10,912	(36,316)
Unrealized foreign currency translation gains (losses)	216,337	(221,595)
	<u>24,130</u>	<u>(295,485)</u>
Total comprehensive income (loss)	\$ (172,996)	\$ (156,650)

(See accompanying notes)

THE INDEPENDENT ORDER OF FORESTERS

Consolidated Statements of Surplus

For the years ended December 31 (In thousands of Canadian dollars)

	2008	2007
Retained earnings		
Balance, beginning of year	\$ 1,559,731	\$ 1,420,896
Net income (loss)	<u>(197,126)</u>	<u>138,835</u>
Balance, end of year	<u>\$ 1,362,605</u>	<u>\$ 1,559,731</u>
Accumulated other comprehensive income (loss)*		
Balance, beginning of year	\$ (143,400)	\$ 152,085
Other comprehensive income (loss)	<u>24,130</u>	<u>(295,485)</u>
Balance, end of year	<u>\$ (119,270)</u>	<u>\$ (143,400)</u>
Total surplus	<u>\$ 1,243,335</u>	<u>\$ 1,416,331</u>
* Accumulated other comprehensive income (loss), net of income taxes:		
Balance, end of year consists of:		
Unrealized gains (losses) on available for sale assets	\$ (143,499)	\$ 48,708
Unrealized foreign currency translation gains (losses)	<u>24,229</u>	<u>(192,108)</u>
	<u>\$ (119,270)</u>	<u>\$ (143,400)</u>

(See accompanying notes)

THE INDEPENDENT ORDER OF FORESTERS

Consolidated Statements of Cash Flows

For the years ended December 31 (In thousands of Canadian dollars)

	2008	2007
Cash flows from operating activities		
Net income (loss)	\$ (197,126)	\$ 138,835
Items not affecting cash:		
Increase in policy liabilities	(103,897)	48,424
Amortization of deferred net investment gains	(2,580)	(3,159)
Change in fair value of investments	360,555	(127,119)
Amortization of premium and discount on bonds	21,084	(3,207)
Other non-cash items	(1,649)	(2,066)
Net change in other assets and other liabilities	14,104	2,035
Decrease due to operating activities	<u>90,491</u>	<u>53,743</u>
Cash flows from investing activities		
Investments sold or matured:		
Bonds and other fixed-term securities	2,282,740	1,676,535
Stocks	701,874	684,784
Mortgages	14,170	13,278
Investments acquired:		
Bonds and other fixed-term securities	(2,266,898)	(1,742,240)
Stocks	(760,201)	(650,520)
Real estate	(13,969)	(2,256)
Other items, net	1,776	(21,485)
Acquisitions, net	(34,381)	-
Decrease due to investing activities	<u>(74,889)</u>	<u>(41,904)</u>
Foreign exchange gain (loss) on cash held in foreign currencies	<u>1,185</u>	<u>(8,541)</u>
Net increase in cash and cash equivalents for the year	<u>16,787</u>	<u>3,298</u>
Cash and cash equivalents, beginning of year	<u>81,510</u>	<u>78,212</u>
Cash and cash equivalents, end of year	<u>\$ 98,297</u>	<u>\$ 81,510</u>
Represented by:		
Cash	\$ 63,141	\$ 36,091
Short-term securities (note 5(b))	<u>35,156</u>	<u>45,419</u>
	<u>\$ 98,297</u>	<u>\$ 81,510</u>

(See accompanying notes)

THE INDEPENDENT ORDER OF FORESTERS

Consolidated Statements of Changes in Segregated Funds

For the years ended December 31 (In thousands of Canadian dollars)

	2008	2007
Net assets, beginning of year	\$ 107,847	\$ 112,420
Net assets acquired from Unity Life of Canada (note 4a)	59,668	-
	<u>167,515</u>	<u>112,420</u>
Additions during the year		
Premiums from contractholders	9,480	9,895
Investment income	3,045	2,623
Net realized gains on sale of investments	6,882	7,641
Net change in unrealized gains on investments	(37,858)	(7,905)
	<u>(18,451)</u>	<u>12,254</u>
Deductions during the year		
Withdrawals by contractholders	23,432	14,566
Management fees and other operating costs	2,360	2,261
	<u>25,792</u>	<u>16,827</u>
Net assets, end of year	\$ 123,272	\$ 107,847

(See accompanying notes)

Consolidated Statements of Segregated Funds' Net Assets

As at December 31 (In thousands of Canadian dollars)

	2008	2007
Bonds	\$ 17,237	\$ 20,099
Equities	99,929	83,190
Cash and short-term securities	7,087	4,430
Accrued investment income	228	217
Other assets	169	91
Liabilities	(1,378)	(180)
	<u>\$ 123,272</u>	<u>\$ 107,847</u>

(See accompanying notes)

THE INDEPENDENT ORDER OF FORESTERS

Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

The Independent Order of Foresters ("Foresters") is a Fraternal Benefit Society, incorporated under the laws of Canada, and operates principally in the life insurance industry in Canada, the United States ("U.S.") and the United Kingdom ("U.K."). Its operations cover the development and marketing of individual life and annuity products.

Foresters is subject to the Insurance Companies Act – Canada ("the Act"), and is regulated by the Office of the Superintendent of Financial Institutions Canada ("OSFI"). Under regulations and guidelines prescribed by OSFI, Foresters is required to maintain prescribed levels of capital (Minimum Continuing Capital and Surplus Requirement ("MCCSR") which are dependent on the type and amount of insurance certificates in force and the nature of its assets. Foresters currently exceeds the capital requirements of OSFI. In addition, Foresters foreign branch and subsidiary operations are regulated by the statutory authorities in the United States and the United Kingdom, which may restrict its distribution of surplus.

1. Change in accounting policies

Effective January 1, 2008, Foresters adopted the Canadian Institute of Chartered Accountants Handbook Section 1535, Capital Disclosures, Section 3862, "Financial Instruments – Disclosures", and 3863, "Financial Instruments – Presentation".

Handbook Section 1535 requires the following disclosures: (i) qualitative information about an entity's objectives, policies and processes for managing capital; (ii) quantitative data about what the entity manages as capital; (iii) whether the entity has complied with any externally imposed capital requirements; and (iv) if it has not complied, the consequences of such non-compliance. The new disclosures are included as note 7.

Sections 3862 and 3863 replace Handbook Section 3861 "Financial Instruments – Disclosure and Presentation". Section 3863 carries forward unchanged the presentation requirements of Section 3861 while Section 3862 places increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks. Handbook Section 3862 requires qualitative and quantitative disclosure of: (i) exposures to risks arising from financial instruments, how they arose and the potential impact on the amount, timing and certainty of future cash flows; (ii) information about the risk management function and the reporting and measurement systems used; (iii) the entity's policies for hedging or mitigating risk and avoiding concentrations of risk; and (iv) the sensitivity to individual market risk factors together with the methodology for performing the analysis. The new disclosures are included in note 6.

2. Significant accounting policies

These consolidated financial statements have been prepared in accordance with the Act, which states that, except as otherwise specified by OSFI, the consolidated financial statements are to be prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The significant accounting policies used in the preparation of these consolidated financial statements are summarized below. These accounting policies conform, in all material respects, to GAAP.

THE INDEPENDENT ORDER OF FORESTERS

Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

2. Significant accounting policies (continued)

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the year. Actual results could differ from those estimates. The most significant estimates are related to the determination of actuarial liabilities that are discussed in note 8.

(a) Basis of consolidation

These financial statements include the accounts of Foresters and its subsidiaries Foresters Holdings (Europe) Ltd. ("FHE"), Unity Life of Canada ("Unity"), Foresters Securities (Canada) Inc. ("FSCI"), Sylvan Agency (Canada) Inc., Foresters Equity Services, Inc., and Foresters Financial Partners Holdings, Inc. Inter-company balances and transactions are eliminated and non-controlling interests in subsidiaries are included in other liabilities on the consolidated balance sheet and in general expenses on the consolidated statement of income.

(b) Invested assets

- **Cash and short-term securities**

Cash and short-term investments comprise cash, current operating accounts, overnight bank and term deposits.

- **Bonds and other fixed-term securities**

Bonds are designated as either held-for-trading or available-for-sale. Purchases and sales of bonds are recognized on the balance sheets on the trade dates, the date that Foresters commits to purchase or sell the bond.

The fair value of publicly traded bonds is determined using quoted market bid prices. For non-publicly traded bonds, fair value is determined using a discounted cash flow approach that includes provisions for credit risk and the expected maturities of the securities. Foresters does not have any bonds for which the fair value is determined using a valuation technique based on assumptions that are not supported by observable market prices or rates.

Held-for-trading bonds are recorded on the consolidated balance sheets at fair value, with realized gains and losses and changes in the fair value of these bonds recorded in net investment income on the consolidated statements of income.

Available-for-sale bonds are recorded at fair value with changes in the fair value of these bonds recorded in unrealized gains and losses on the consolidated statements of comprehensive income (loss). Realized gains and losses on sale are reclassified from accumulated other comprehensive income ("AOCI") and recorded in net investment income on the consolidated statements of income.

THE INDEPENDENT ORDER OF FORESTERS

Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

2b. Significant accounting policies – Invested assets (continued)

- **Mortgages**

Mortgages are classified as loans and receivables and are carried at amortized cost. The difference between the proceeds on sale and outstanding principal balance is recorded in net investment income on the consolidated statements of income.

The fair value of mortgages is calculated by discounting estimated cash flows using a market interest rate. The fair value of non-performing mortgages is based on estimated cash flows discounted using a rate which approximates the risk associated with the estimated cash flows.

- **Stocks**

Stocks are designated as either held-for-trading or available-for-sale. Purchases and sales of stocks are recognized on the consolidated balance sheets on the trade dates, the date that Foresters commits to purchase or sell the stocks.

The fair value of publicly traded stocks is determined using quoted market bid prices. For non-publicly traded stocks, fair value is estimated on the basis of dealer quotes or recent transactions of similar investments.

Held-for-trading stocks are recorded on the balance sheets at fair value, with realized gains and losses and changes in the fair value of these stocks recorded in net investment income on the consolidated statements of income.

Available-for-sale stocks are recorded on the consolidated balance sheets at their fair values with changes in the fair value of these stocks recorded in unrealized gains and losses on the consolidated statements of comprehensive income (loss). Realized gains and losses on sale are reclassified from AOCI and recorded in net investment income on the consolidated statements of income.

- **Real estate**

Real estate held for investment, which includes own-use property, is carried at moving average market value whereby the carrying value of the portfolio is adjusted towards market value at 3% per quarter. Net realized gains and losses are deferred and amortized to income at 3% per quarter on a declining balance basis. Market values on each property are reviewed each year and external appraisals are carried out at least every three years by qualified appraisers. The market value established is an estimate of the realizable value of each property and thus recognizes an element of depreciation in that determination. No further provision for depreciation is therefore required or calculated.

The fair value of real estate properties is based on recent external appraisals obtained on a three-year cycle. The appraised value is adjusted, if necessary, each year to reflect current market conditions.

THE INDEPENDENT ORDER OF FORESTERS

Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

2b. Significant accounting policies – Invested assets (continued)

- **Loans to certificateholders**

Loans to certificateholders are classified as loans and receivables and are carried at their unpaid balance. These loans are fully secured by the cash surrender value of the policies on which the respective loans are made.

- **Other invested assets:**

Derivative financial instruments

Foresters utilizes certain derivative financial instruments in portfolios supporting actuarial liabilities in order to hedge against fluctuations in foreign exchange rates and stock market indices. These derivative financial instruments are classified as held-for-trading and are recorded on the consolidated balance sheets at fair value, with realized gains and losses and changes in the fair value of these contracts recorded in net investment income on the consolidated statements of income. The fair value of derivative financial instruments is based on quoted market prices.

Limited partnerships

Limited partnerships are classified as available-for-sale and are recorded on the consolidated balance sheets at cost plus Foresters pro-rata share of net income (loss) less any distributions paid. Where fair values are available, the cost of these assets is adjusted to fair value with changes in fair value recorded in unrealized gains and losses on the consolidated statements of comprehensive income (loss). Realized gains and losses on sale are reclassified from AOCI and recorded in net investment income on the consolidated statements of income.

Segregated fund investments

Foresters manages a number of segregated funds on behalf of certificateholders. Substantially all risks and rewards of ownership accrue to segregated fund certificateholders; consequently, these assets are segregated and presented separately from Foresters general fund. The assets of these funds are carried at market values. Income earned from fund management fees is included in other income of the general fund.

(c) Provisions for asset defaults

Foresters makes specific provisions against invested assets where there has been other than a temporary decline in the underlying value of an asset. When an asset is identified as impaired, the carrying value of the investment is reduced to the estimated realizable amount and a charge is included in income in the year in which the impairment in value is identified. Any further reduction in the estimated realizable amount subsequent to the initial recognition of impairment is included in income in the period in which the change occurs as a charge for impaired assets.

THE INDEPENDENT ORDER OF FORESTERS

Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

2. Significant accounting policies (continued)

(d) Other Assets

Other assets consist primarily of accounts receivable and fixed assets. Accounts receivable are carried at cost and fixed assets at cost less accumulated depreciation.

The fair value of these assets approximates the carrying value due to the short-term nature of these financial instruments.

(e) Actuarial liabilities

Actuarial liabilities have been calculated using the Canadian Asset Liability Method ("CALM"). Actuarial liabilities represent an estimate of the amount, which together with future premiums and investment income will be sufficient to pay future benefits, dividends and expenses on insurance and annuity contracts. The carrying value of actuarial liabilities is based on the present value of expected cash flows plus provisions for adverse deviations and is considered to be an indicator of fair value, as there is no ready market for the trading of insurance policies

(f) Premium revenues

Gross premiums are recognized as revenue when due. When premiums are recognized, the related actuarial liabilities are recorded, resulting in the matching of benefits and expenses with such revenue.

(g) Transaction costs

Transaction costs on the purchase or sale of an investment are expensed as incurred for all investments classified as both held-for-trading and available-for-sale.

(h) Fraternal investment

Fraternal investment represents the contribution made by Foresters in the three countries where Foresters operates. These contributions include donations to charities for family's causes, sponsorship for various fund raising programs, support for the volunteer branch system, scholarships and other benevolent activities.

(i) Income taxes

Income taxes are accounted for by the asset and liability method, whereby future tax assets and liabilities are recognized for future tax consequences attributable to differences between the financial statement carrying amount of existing assets and liabilities and their respective tax bases, operating losses and tax loss carryforwards. Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the year in which those temporary differences are expected to be recovered or settled.

THE INDEPENDENT ORDER OF FORESTERS

Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

2. Significant accounting policies (continued)

Future tax assets and liabilities are included in other assets or other liabilities, as applicable, in the consolidated balance sheets.

(j) Foreign currency translation

Foresters operations in the United States and the United Kingdom are considered to be self-sustaining and are translated using the current rate method. Under this method, all assets and liabilities are translated at year-end exchange rates and revenues and expenses are translated at average rates of exchange for the year. Translation gains and losses are included in AOCI.

(k) Employee benefit plans

Obligations under employee benefit plans (including pension plans and post-retirement plans other than pensions) and the related costs, net of plan assets, are accrued as the employees render the service necessary to earn the pension and other employee future benefits. Foresters has adopted the following policies:

- The cost of pensions and other retirement benefits earned by employees is actuarially determined using the projected benefit method prorated on service and management's best estimate of expected plan investment performance, salary and other escalation, and retirement ages of employees.
- For the purposes of calculating the expected return on plan assets, those assets are valued at fair value.
- Past service costs arising from plan amendments are deferred and amortized on a straight-line basis over the average remaining service period of employees active at the date of amendment.
- Actuarial gains (losses) arise from the difference between the actual long-term rate of return on plan assets for a period and the expected long-term rate of return on plan assets for that period or from changes in actuarial assumptions used to determine the accrued benefit obligation. The excess of the net accumulated actuarial gain (loss) over 10% of the greater of the benefit obligation and the fair value of pension plan assets, determined at the beginning of each year, is amortized over the average remaining service period of active employees. The average remaining service period of the active employees covered by the pension plans (on a weighted average basis) was 11.8 years (2007 – 11.9 years). The average remaining service period of the active employees covered by the other retirement benefit plans (on a weighted average basis) was 28.9 years (2007 – 30.2 years).
- Foresters adopted CICA 3461 on a prospective basis as of January 1, 2000. The transitional asset (obligation) is being amortized over the remaining service period, determined as of January 1, 2000. The remaining amortization period (on a weighted average basis) as of December 31, 2008 was approximately 11.6 years for the pension plans and 6.2 years for the other retirement benefit plans.
- Employee benefit plan liabilities or assets are included in other assets or other liabilities, as applicable, in the consolidated balance sheets.

THE INDEPENDENT ORDER OF FORESTERS

Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

3. Future accounting change

In February 2008, the CICA announced that Canadian generally accepted accounting principles will be replaced by International Financial Reporting Standards ("IFRS") for fiscal years beginning on or after January 1, 2011. Although the CICA permits early adoption of IFRS, federally regulated institutions have been precluded from early adoption by OSFI. Foresters will begin reporting under IFRS for the first quarter ending March 31, 2011 and will be required to prepare an opening balance sheet together with information for comparative periods.

Foresters has developed an IFRS transition plan to address key areas of the conversion to IFRS including:

- accounting policy changes
- financial disclosure requirements
- information technology impacts
- education and training requirements

Foresters has completed the assessment phase of its IFRS project which included the following:

- Initial training of key actuarial and finance staff
- Initial assessment of accounting differences between IFRS and Canadian GAAP
- Insurance contract classification
- High level project plan for 2009 and 2010

As the implementation process develops, Foresters will continue to revisit its changeover plan; accordingly, changes to the plan may be required as more information on the adoption of IFRS becomes known.

4. Acquisitions and dispositions

Acquisitions

- a) On April 2, 2008, Foresters acquired 100% of the common shares of Unity for cash consideration of \$51,404 including transaction costs of \$1,404. This transaction resulted in an increase in total assets of \$564,458, total liabilities of \$512,324 and a gain of \$730 that was recorded in other income on the consolidated statements of income (loss). In addition, this acquisition resulted in an increase in Foresters segregated fund assets of \$59,668. Net income from operations of \$5,586 was included in Foresters consolidated statements of income (loss) since the date of acquisition
- b) On December 31, 2008, Unity purchased the insurance business of Forethought Life Insurance Company, the Canadian branch of Forethought Financial Group, Inc. for cash consideration of \$5,179 including transaction costs of \$307. This transaction added \$87,400 to total assets and \$80,165 to total liabilities. A gain of \$2,056 was recorded in other income on the consolidated statements of income (loss).

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

4. Acquisitions and dispositions (continued)

- c) On December 31, 2008, Unity purchased the Canadian individual life and occupational disability insurance business of Washington National Insurance Company, a wholly owned subsidiary of Conseco Life Insurance Company of Texas and incurred transaction costs of \$118. This transaction added \$1,894 to total assets and \$950 to total liabilities resulting in a gain of \$826 that was recorded in other income on the consolidated statements of income (loss).
- d) On November 1, 2008, Forester Life Limited ("FLL"), the U.K. insurance subsidiary of FHE, acquired the life business assets and liabilities of Domestic and General Life Assurance Company Limited ("DGLA") and incurred transaction costs of \$178. This transaction increased Foresters consolidated assets by \$7,618 and consolidated liabilities of \$6,521. A gain of \$919 was recorded in other income on the consolidated statements of income (loss). Net income from operations of \$227 was included in Foresters consolidated statements of income (loss) since the date of acquisition.

Dispositions

- e) Foresters recorded a gain of \$7,734 on the sale of its U.K. healthcare insurance subsidiary, Forester Health Ltd., on January 2, 2008. The gain was included in other income on the consolidated statements of income (loss). Included in the 2007 consolidated financial statements were net assets of \$8,263 and net income of \$2,207 relating to the operation of this subsidiary.
- f) Foresters sold all of the assets under management in its Canadian subsidiary, FSCI, for consideration of \$376 on May 20, 2008 at which time, FSCI withdrew from the mutual fund business in Canada.

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

5. Invested assets

a) Fair value and carrying value

The fair value and carrying value of invested assets are as follows:

	2008				2007			
	Held for	Available for	Other	Total	Held for	Available for	Other	Total
	Trading	sale			Trading	sale		
	\$	\$	\$	\$	\$	\$	\$	\$
Carrying value *								
Cash and short-term securities	98,297	-	-	98,297	81,510	-	-	81,510
Bonds and other fixed-term securities	4,014,134	656,829	-	4,670,963	3,101,618	539,615	-	3,641,233
Mortgages	-	-	21,067	21,067	-	-	30,122	30,122
Common shares	517,410	451,756	-	969,166	565,225	650,306	-	1,215,531
Real estate	-	-	26,468	26,468	-	-	19,058	19,058
Loans to policyholders	-	-	214,619	214,619	-	-	171,498	171,498
Other invested assets	45,042	60,200	6	105,248	98,184	47,613	2,001	147,798
	<u>4,674,883</u>	<u>1,168,785</u>	<u>262,160</u>	<u>6,105,828</u>	<u>3,846,537</u>	<u>1,237,534</u>	<u>222,679</u>	<u>5,306,750</u>
Fair Value								
Cash and short-term securities	98,297	-	-	98,297	81,510	-	-	81,510
Bonds and other fixed-term securities	4,014,134	656,829	-	4,670,963	3,101,618	539,615	-	3,641,233
Mortgages	-	-	22,120	22,120	-	-	31,628	31,628
Common shares	517,410	451,756	-	969,166	565,225	650,306	-	1,215,531
Real estate	-	-	23,600	23,600	-	-	19,250	19,250
Loans to policyholders	-	-	214,619	214,619	-	-	171,498	171,498
Other invested assets	45,042	60,200	6	105,248	98,184	47,613	2,001	147,798
	<u>4,674,883</u>	<u>1,168,785</u>	<u>260,345</u>	<u>6,104,013</u>	<u>3,846,537</u>	<u>1,237,534</u>	<u>224,377</u>	<u>5,308,448</u>

* Recognized on the balance sheet

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

5. Invested assets (continued)

b) Cash and short-term securities

Short-term securities comprise notes and commercial paper with a maximum maturity date of April 8, 2009 and effective interest rates of 0.32% to 2.13% (2007 – 4.20% to 4.75%). Cash and short-term securities are comprised of:

	2008	2007
	\$	\$
Cash	63,141	36,091
Short-term securities with an original maturity of 90 days or less	32,722	45,212
	95,863	81,303
Short-term securities with an original maturity of greater than 90 days	2,434	207
	98,297	81,510

c) Bonds and other fixed-term securities

	Average effective yield	
	2008	2007
Corporate	5.89%	5.48%
Government	5.30%	5.42%
Other	-	5.02%

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

5c. Invested assets – Bonds and other fixed-term securities (continued)

The term to maturity of bonds and other fixed term securities was as follows:

	Carrying value	
	2008	2007
	\$	\$
Term to maturity		
Corporate:		
Due in one year or less	121,820	138,922
One through five years	574,262	541,793
After five years	1,421,710	1,253,257
	<u>2,117,792</u>	<u>1,933,972</u>
Government:		
Due in one year or less	19,026	25,477
One through five years	219,908	169,407
After five years	2,314,237	1,506,429
	<u>2,553,171</u>	<u>1,701,313</u>
Other:		
Due in one year or less	-	5,948
	<u>4,670,963</u>	<u>3,641,233</u>

The carrying amount is shown by contractual maturity. Actual maturity may differ from contractual maturity because certain borrowers have the right to call or prepay certain obligations with or without call or prepayment penalties.

d) Mortgages

	2008			2007		
	Carrying value	Average effective rate	Average maturity (years)	Carrying value	Average effective rate	Average maturity (years)
	\$			\$		
Commercial	21,067	7.1%	2.6	28,158	7.2%	2.5
Multiple residential	-	-	-	1,964	8.1%	6.0
	<u>21,067</u>	<u>7.1%</u>	<u>2.6</u>	<u>30,122</u>	<u>7.2%</u>	<u>2.7</u>

e) Loans to certificateholders

Loans to certificateholders have effective interest rates principally ranging from 5% to 8% (2007 - 5% to 8%), with an average effective rate of 5.2% (2007 - 5.3%).

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

5. Invested assets (continued)

f) Net Investment income was derived from the following sources:

	2008				2007			
	Held for Trading \$	Available for sale \$	Other \$	Total \$	Held for Trading \$	Available for sale \$	Other \$	Total \$
Investment income								
Interest income from:								
Cash and short-term securities	4,115	-	-	4,115	3,879	-	-	3,879
Bonds and other fixed-term securities	173,137	33,513	-	206,650	171,315	28,771	-	200,086
Mortgages	-	-	1,929	1,929	-	-	2,703	2,703
Loans to certificateholders	-	-	10,257	10,257	-	-	9,782	9,782
Other invested assets including inter-segment notes *	(2,534)	2,342	139	(53)	(133)	-	(967)	(1,100)
	174,718	35,855	12,325	222,898	175,061	28,771	11,518	215,350
Dividend income from stocks:	25,630	18,762	-	44,392	21,939	18,287	-	40,226
Net rental income from real estate	-	-	(204)	(204)	-	-	(855)	(855)
	200,348	54,617	12,121	267,086	197,000	47,058	10,663	254,721
Net recognized gains (losses)								
Bonds and other fixed-term securities	3,015	(18,320)	-	(15,305)	4,567	(5,044)	-	(477)
Mortgages	-	-	201	201	-	-	205	205
Stocks	(218,350)	(71,962)	-	(290,312)	(11,471)	95,144	-	83,673
Real estate	-	-	2,579	2,579	-	-	3,159	3,159
Other invested assets	(55,140)	-	-	(55,140)	43,718	-	-	43,718
	(270,475)	(90,282)	2,780	(357,977)	36,814	90,100	3,364	130,278
	(70,127)	(35,665)	14,901	(90,891)	233,814	137,158	14,027	384,999
Less: investment expense	(855)	(2,979)	-	(3,834)	(1,809)	(4,813)	-	(6,622)
Net investment income	(70,982)	(38,644)	14,901	(94,725)	232,005	132,345	14,027	378,377

* Intersegment transactions consist primarily of internal financing agreements. They are measured at fair market values prevailing when the arrangements were negotiated. These notes are recorded in other invested assets on the consolidated balance sheets. The intersegment notes and related interest eliminate on consolidation.

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

5. Invested assets – Net investment income (continued)

Cash received on account of investment income, excluding the impact of principal transactions, in 2008 was \$192,798 (2007 - \$414,045).

6. Risk management for financial instruments

The primary goals of risk management are to ensure that the outcomes of activities involving elements of risk are consistent with Foresters objectives and risk tolerance, and to maintain an appropriate risk/reward balance while protecting Foresters balance sheet from events that have the potential to materially impair its financial strength.

Foresters has policies relating to the identification, measurement, monitoring, mitigation, and control of risks associated with financial instruments. The key risks related to financial instruments are credit risk, derivative financial instruments and related risks, market price and interest rate risk (currency, interest rate and equity), insurance risk and liquidity risk. The following sections describe how Foresters manages each of these risks.

a) Credit risk

Credit risk is the risk of financial loss resulting from the failure of a debtor making payments when due. A Board approved Investment Policy sets out the policies and procedures to manage this risk. Specifically guidelines have been established to minimize undue concentration of assets in any single geographic area, industry and company; limit the purchase of fixed income securities to investment-grade assets; and specify minimum and maximum limits for fixed income securities by credit quality ratings.

Portfolios are monitored continuously, and reviewed regularly with the Investment Committee of the Board.

Credit risk also arises from reinsurance activities. All reinsurance counterparties are required to meet minimum risk rating criteria. Reinsurance is placed with counterparties that have a good credit rating and concentration of credit risk is managed by following policy guidelines approved each year by the Board of Directors. Management regularly monitors and performs an assessment of creditworthiness of reinsurers.

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

6a. Risk management for financial instruments – Credit risk (continued)

i) Maximum exposure to credit risk

Foresters maximum exposure to credit risk related to financial instruments is the carrying value of the assets net of any allowances for losses. At December 31, 2008, this amounted to \$6,200,562 (2007 - \$5,388,576).

ii) Concentration of credit risk

Concentration of credit risk arises from exposures to a single debtor, a group of related debtors or groups of debtors that have similar credit risk characteristics in that they operate in the same geographic region or in similar industries.

Foresters establishes enterprise-wide investment portfolio level targets and limits to ensure that portfolios are widely diversified across asset classes and individual investment risks.

Bonds and other fixed term securities

Investment concentration in any one investee or related group of investees, except for Canadian, United Kingdom and United States government and government agencies and guarantees, was limited to U.S. – 3.5% of the U.S. bond portfolio, CDN – 4.0% of the Canadian bond portfolio and £9,000 of the United Kingdom bond portfolio. The U.S. and Canadian dollar limits are for AAA rated bonds, and are further constrained for lower rated bonds.

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

6a. Risk management for financial instruments – Credit risk

ii) Concentration of credit risk (continued)

Forester has no significant exposure to a single corporate bond. The following table provides details of the carrying value of bonds by industry sector and geographic distribution:

	2008			2007		
	Held for Trading	Available for sale	Total	Held for Trading	Available for sale	Total
	\$	\$	\$	\$	\$	\$
Bonds issued or guaranteed by:						
Canadian federal government	150,172	166	150,338	135,219	15,509	150,728
Canadian provincial and municipal government	419,123	70,946	490,069	163,432	15,943	179,375
U.S. treasury and other U.S. agencies	1,139,088	264,038	1,403,126	801,661	51,999	853,660
Other foreign governments	443,767	65,870	509,637	471,542	46,008	517,550
Total government issued or government bonds	2,152,150	401,020	2,553,170	1,571,854	129,459	1,701,313
Corporate bonds by industry sector:						
Asset-backed securities	81,670	16,169	97,839	48,179	20,706	68,885
Communications	18,336	-	18,336	18,334	14,088	32,422
Consumer staples and discretionary	221,003	50,536	271,539	174,124	42,745	216,869
Financials	1,225,870	120,038	1,345,908	1,137,848	256,234	1,394,082
Healthcare	28,590	15,172	43,762	13,168	12,769	25,937
Industrials	123,707	22,399	146,106	47,600	38,686	86,286
Utilities and energy	121,138	8,350	129,488	59,043	1,900	60,943
Other	41,670	23,145	64,815	31,468	23,028	54,496
Total corporate bonds	1,861,984	255,809	2,117,793	1,529,764	410,156	1,939,920
	4,014,134	656,829	4,670,963	3,101,618	539,615	3,641,233
Allocation by geographic region:						
Canada	964,615	45,945	1,010,560	497,160	36,690	533,850
United States	2,597,276	558,042	3,155,318	2,033,211	509,189	2,542,400
United Kingdom	452,243	52,842	505,085	571,247	(6,264)	564,983
	4,014,134	656,829	4,670,963	3,101,618	539,615	3,641,233

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

6a. Risk management for financial instruments - Credit risk

ii) Concentration of credit risk (continued)

Bonds and other fixed term securities

The credit rating of the bond portfolio was as follows:

Bond quality	2008		2007	
	\$	%	\$	%
Investment grade:				
AAA	2,615,064		2,042,532	
AA	1,211,519		944,558	
A	763,330		631,416	
BBB	78,275		22,727	
	<u>4,668,188</u>	99.9%	<u>3,641,233</u>	100.0%
BB and lower	<u>2,775</u>	0.1%	<u>-</u>	-
Total bonds	<u>4,670,963</u>	100.0%	<u>3,641,233</u>	100.0%

Mortgages

Mortgages are secured by first recourse on the underlying property and carry a fixed interest rate.

Foresters limits its concentration in mortgages, including mortgage backed securities, collateralized mortgage obligations and collateralized mortgage backed securities to 25% of the fixed income portfolio of each of the U.S. and Canada.

Stocks

Foresters limits its investment concentration of stocks in any one investee or related group of investees, to the greater of 1.5 times the issuer's weight on the S&P/TSX composite index or 7% of the Canadian equity portfolio to the maximum of 10% of the portfolio. The U.S. large capitalization portfolio is managed with reference to the S&P 500 index. The U.S. mid capitalization portfolio, REITs and international portfolios have a single issue maximum of 10% of its respective portfolio, while in the U.K. the maximum in any one company is 5% of its total assets. In addition, total investment in equities, REITs and real estate is limited to 25% of total invested assets.

Foresters has no significant exposure to any single investee or related group of investees. 100% of Foresters stock portfolio is invested in publicly listed corporations.

Real estate

Investments in real estate are limited to 15% of total Foresters assets.

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

6a. Risk management for financial instruments - Credit risk

iii) Impairments

An allowance for losses on loans is established when a loan becomes impaired as a result of deterioration in credit quality, to the extent there is no longer assurance of timely realization of the carrying value of the loan and related investment income. The carrying value of an impaired loan is reduced to its estimated net realizable value at the time of recognition of impairment. No allowances for losses have been taken in 2008 or in 2007.

Actuarial liabilities include provisions for credit losses for future asset impairments (see Note 8b).

Unrealized gains and losses on available-for-sale assets are recorded in other comprehensive income ("OCI"). For other than temporary impairments on such assets, Foresters reclassifies the unrealized loss on a cumulative basis from OCI and/or AOCI to net income (loss). Forester has recognized other than temporary impairments on available-for-sale bonds of \$13,446 (2007 – nil) and available-for-sale equities of \$10,670 (2007 – nil) by reclassifying the impaired portion of unrealized losses from OCI to net income (loss).

At December 31, 2008, Foresters held bonds on which interest payments were in default (2007 - \$0). These bonds had a carrying value of \$2,775 on the consolidated balance sheets and amortized cost of \$29,131.

b) Derivatives financial instruments and related risks

Foresters utilizes derivative financial instruments, including options and foreign exchange forward contracts, when appropriate, to hedge against fluctuations in foreign exchange rates and changes in stock market indices. Foresters does not enter into these financial instruments for trading or speculative purposes. Foresters only enters into derivative financial contracts with approval from the Board of Directors at which time authorization limits are set for specific personnel and policies are established to limit the size and type of such derivative transactions and counterparty exposure in respect of both the notional amount outstanding and the fair value. Adherence to these policies is monitored regularly and reported to the Investment Committee annually.

Foresters exposure to loss on derivatives is limited to the amount of any net gains that may have accrued with a particular counterparty. All contracts are held with counterparties rated "A" or higher. 100% percent of Foresters derivative exposure was with counterparties rated "AA" or higher as at December 31, 2008 and 2007. The largest single counterparty exposure was \$23,072 (2007 – \$51,545).

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

6b. Risk management for financial instruments - Derivative financial instruments (continued)

The following table summarizes derivative financial instruments outstanding at December 31.

	Notional amount by remaining term to maturity				Fair value			Credit equivalent amount	Risk weighted amount
	Under 1 year	1 to 5 years	Over 5 years	Total	Positive	Negative	Net		
	\$	\$	\$	\$	\$	\$	\$		
2008									
Foreign exchange forward contracts	32,903	124,430	314,393	471,726	59,924	15,505	44,419	90,054	45,027
Options purchased	-	-	-	-	1,731	-	1,731	-	-
Options written	-	-	-	-	-	1,108	(1,108)	-	-
	32,903	124,430	314,393	471,726	61,655	16,613	45,042	90,054	45,027
2007									
Foreign exchange forward contracts	32,478	126,412	295,114	454,004	96,942	-	96,942	125,543	62,861
Options purchased	-	-	-	-	2,407	-	2,407	-	-
Options written	-	-	-	-	-	1,167	(1,167)	-	-
	32,478	126,412	295,114	454,004	99,349	1,167	98,182	125,543	62,861

Notional amount represents the face amount of derivative financial instruments to which a rate or price is applied to determine the amount of cash flows to be exchanged. It represents the volume of outstanding derivative financial instruments and does not represent the potential gain or loss associated with market risk or credit risk of such instruments.

Fair value of a derivative financial instrument is equivalent to the replacement cost based on quoted market prices. Positive fair value, representing an unrealized gain to Foresters, is the maximum credit risk measured as of the balance sheet date if the counterparties were to default on their obligations to Foresters.

Credit equivalent amount is the sum of replacement cost and the potential future credit exposure. The potential future credit exposure represents the potential for future losses that may result from future changes in fair value and is calculated based on a formula prescribed by OSFI.

Risk weighted amount represents the credit risk equivalent, weighted according to the creditworthiness of the counterparty, as prescribed by OSFI.

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

6. Risk management for financial instruments (continued)

c) Market price and interest rate risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate as a result of changes in market factors which include three types of risks: currency risk, interest rate risk and equity risk.

i. Currency Risk

Currency risk for financial instruments arises from a mismatch between the currency of the policy liabilities and the currency of the assets designated to support those liabilities. Foresters matches the currency of its assets with the currency of the liabilities they support to mitigate economic exposure to changes in exchange rates. Additionally, Foresters incurs the majority of its U.S. branch administrative expenses in Canadian dollars and therefore it has entered into foreign exchange forward contracts to limit the exposure to foreign exchange rate fluctuations between the Canadian and U.S. dollars (see note 6(b)). The calculation of policy liabilities includes a provision for future policy maintenance expenses, which are incurred in Canadian dollars on behalf of U.S. branch business based on exchange rates implicit in these contracts. These foreign exchange forward contracts effectively offset the impact of foreign exchange rate fluctuations on U.S. branch expenses and are reflected in the determination of U.S. branch policy liabilities.

A 10% increase in foreign currency rates would be expected to reduce U.S. branch policy liabilities by \$7,235. A 10% decrease in foreign currency rates would be expected to increase U.S. branch policy liabilities by \$7,081.

A substantial portion of Foresters business is denominated in currencies other than Canadian dollars. If the Canadian dollar strengthened relative to non-Canadian currencies, the translated value of reported earnings and surplus from the non-Canadian denominated businesses would decline. Foresters uses financial measures such as constant currency calculations to monitor the effect of such currency fluctuations. The following table shows the impact on net income and surplus of a 1% strengthening in the Canadian dollar relative to the U.S. dollar and the U.K. pound.

	Decrease in total comprehensive income (loss)		Decrease in surplus	
	2008	2007	2008	2007
Impact of 1% strengthening in the Canadian dollar				
U.S. dollar	3,625	(399)	(10,394)	(11,888)
U.K. pound	42	(111)	(748)	(859)

A 1% weakening in rates would have an equal and opposite impact to that displayed above.

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

6c. Risk management for financial instruments - Market price and interest rate risk (continued)

ii. Interest rate risk

Interest rate risk exists if asset and liability cash flows are not closely matched and interest rates change, causing a difference in value between assets and liabilities. Foresters mitigates its exposure to interest rate risk by utilizing a formal process for managing the matching of assets and liabilities which involves grouping general fund assets and liabilities into segments. Assets in each segment are managed in relation to the liabilities in that segment. For products with fixed and highly predictable benefit payments, investments are made in fixed income assets that closely match the product liability cash flows. Protection against interest rate change is achieved as any change in the fair market value of the assets will be offset by a similar change in the fair market value of the liabilities. For products with less predictable timing of benefit payments, investments are made in fixed income assets with cash flows of a shorter duration than the anticipated timing of benefit payments, or equities as described below.

The risk associated with the mismatch in portfolio duration and cash flow, asset prepayment exposure and the pace of asset acquisition are quantified and reviewed regularly.

Projected cash flows from the current assets and liabilities are used in the Canadian Asset Liability Method (CALM) to determine actuarial liabilities. Cash flows from assets are reduced to provide for potential asset default losses. Testing under several interest rate scenarios (including increasing and decreasing rates) is done to assess reinvestment risk.

One way of measuring the interest rate risk associated with this assumption is to determine the effect on the present value of the projected net asset and liability cash flows of the business of Foresters of an immediate 1% increase or decrease in the level of interest rates. These interest rate changes will impact the projected cash flows. For most of the interest sensitive products, annuities and universal life certificates, a decrease in interest rates results in decreased profitability. A sustained 1% decline in the general level of interest rates would result in an increase in actuarial liabilities on these products of approximately \$69,100 (2007 - \$41,300) while the effect of a sustained 1% increase in the general level of interest rates would result in an decrease in actuarial liabilities on these products of approximately \$45,600 (2007 - \$32,000).

Many of the annuity and universal life insurance certificates have minimum credited interest rate guarantees, ranging from 1.5% to 4.0% (2007 – 1.5% to 4.0%). These products are sensitive to a sustained decline in interest rates. The dividend paying traditional life insurance products are also sensitive to a sustained decline in interest rates. However, this impact would only be realized in the long term because dividends would be reduced as the yield on the asset portfolio declines.

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

6c. Risk management for financial instruments – Market price and interest rate risk

ii) Interest rate risk (continued)

It is more difficult to fully reflect the impact of a sharp setback in the market on dividends credited on certificates and particularly on interest rates credited on interest sensitive products. Under Foresters investment policies, the level of tolerable sensitivity to a sustained 1% reduction in interest rates, combined with a sustained 10% reduction in stock markets is benchmarked against a 10% reduction in MCCSR. At December 31, 2008, this benchmark was \$36,200 (2007 - \$34,000), being the surplus reduction which would result in a 10% reduction in MCCSR.

A 1% reduction in interest rates, combined with a sustained 10% reduction in stock markets, results in a \$103,900 increase (2007 - \$27,000 increase) in actuarial liabilities and a corresponding decrease in net income.

Both sensitivity results above assume that a sustained decline in the general level of inflation – and therefore expense inflation – occurs in conjunction with the sustained decline in interest rates. Such a decrease in expense inflation offsets some of the effect of lower interest rates.

Bonds designated as available-for-sale generally do not support actuarial liabilities. Changes in fair value of available-for-sale bonds are recorded in OCI. For Foresters available-for-sale bonds, an immediate 1% parallel increase in interest rates at December 31, 2008, across the entire yield curve, would result in an estimated after-tax decrease in OCI of \$38,200 (2007 - \$36,500). Conversely, an immediate 1% parallel decrease in interest rates would have an equal and opposite effect.

iii) Equity risk

Some policy liabilities are supported by equities such as products with long duration liabilities. There will be additional impacts on these liabilities as equity market values fluctuate. A 10% increase in equity markets would be expected to decrease actuarial liabilities by approximately \$4,500 (2007 - \$2,400). A 10% decrease in equity markets would be expected to increase actuarial liabilities by approximately \$10,100 (2007 - \$5,600).

Equities designated as available-for-sale generally do not support actuarial liabilities. Changes in fair value of available-for-sale equities are recorded in OCI. For Foresters available-for-sale equities, an immediate 10% increase in stock prices at December 31, 2008, would result in an estimated after-tax increase in OCI of \$46,100 (2007 - \$72,800). Conversely, an immediate 10% decrease in stock prices would have an equal and opposite effect.

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

6. Risk management for financial instruments (continued)

d) Insurance risk

Insurance risk is the risk of loss due to actual experience differing from the experience assumed when a product was designed and priced with respect to claims, policyholder behaviour and expenses. A variety of assumptions are made related to the future level of claims, policyholder behaviour, expenses and sales levels when products are designed and priced as well as in the determination of actuarial liabilities. The development of assumptions for future claims and policyholder behaviour are based on company and industry experience. Such assumptions require a significant amount of professional judgment and therefore, actual experience may be materially different than the assumptions made by Foresters.

e) Liquidity Risk

Liquidity risk is the risk that Foresters will not be able to meet all cash outflow obligations as they come due. Foresters liquidity requirements are closely managed through cash flow matching of assets and liabilities and forecasting earned and required yields to ensure consistency between certificateholder requirements and the yield of assets.

Operating and strategic liquidity levels are managed against established minimums. Foresters ensures adequate liquidity on a day-to-day operational basis by maintaining a specified minimum level of highly liquid assets (defined as all short-term investments issued by major banks and the governments of Canada, the U.S. and the U.K.). Operating liquidity remains well above minimum requirements.

Strategic liquidity is measured under both immediate (within one month) and ongoing (within one year) stress scenarios. Foresters target liquidity ratio under both scenarios is 200%, a ratio that would more than support the highest claims-paying ratings for Foresters, in addition to providing a wide margin of safety. Foresters liquidity ratio is defined as Allowable Liquid Assets/ Risk-Adjusted Liquidity of Liabilities. The Risk-Adjusted Liquidity of Liabilities is calculated by assessing the probability of a policyholder surrendering a policy for cash under each of the two scenarios, adjusted for the ability of the policyholder to surrender under its contractual provisions.

The following chart shows Foresters strategic liquidity ratio:

	2008		2007	
	Immediate scenario	Ongoing scenario	Immediate scenario	Ongoing scenario
Allowable Liquid Assets	5,236,215	5,407,972	4,469,385	4,681,497
Risk-Adjusted Liquidity of Liabilities	1,803,664	2,253,261	1,402,588	1,807,786
Liquidity ratio	290.3%	240.0%	318.7%	259.0%

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

6. Risk management for financial instruments (continued)

f) Securities lending

Foresters lends its own securities for periods of time to other institutions on a fully collateralized basis in order to generate additional income. The value of the collateral received is at least 102% (105% in Canada) of the market value of the security loaned and the collateral is marked to market daily while Foresters security is on loan. The securities lending program is managed by regulated financial institutions in Canada and the United States.

The market value of the loaned securities is monitored on a daily basis with additional collateral obtained or refunded as the market values fluctuate. As at December 31, 2008, securities with an estimated market value of \$741,689 (2007 - \$453,281) were on loan. Foresters has received collateral with an estimated market value of \$757,528 (2007 - \$462,337).

7. Capital Management

Foresters capital base consists of retained earnings and accumulated other comprehensive income (loss) as stated on the Consolidated Statement of Surplus.

Foresters objective with respect to capital management is to maintain a consistently strong capital position, to comply with local solvency requirements in all jurisdictions in which Foresters operates and to build on Foresters value by taking advantage of business and investment opportunities as they arise.

In accordance with the Board approved capital management policy, Foresters has established internal targets for capital adequacy at both a total company and a divisional level. These targets exceed local minimum capital requirements in each jurisdiction in which Foresters operates. Foresters forecasts capital requirements over a three year period. On a quarterly basis, management monitors performance against internal targets and forecasts, and initiates action when appropriate.

Annually as part of Dynamic Capital Adequacy Testing ("DCAT"), Foresters assess the strength of its capital position under plausible adverse scenarios including mitigating management actions. These scenarios reflect Foresters business plans and risk profile.

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

7. Capital Management (continued)

In Canada, OSFI has established a capital adequacy measure for life insurance companies incorporated under the Insurance Companies Act (Canada) and their subsidiaries, known as the MCCR. OSFI generally expects life insurance companies to maintain a minimum MCCR of 150% or greater, based on the risk profile of the relevant insurance company.

The MCCR ratios as at December 31, 2008 and December 31, 2007, shown below, were above the levels that would require any regulatory or corrective action.

		2008	2007
Capital available	A	1,243,792	1,413,440
Capital required:			
Asset default and market risk		165,468	199,761
Insurance risks		113,090	79,184
Interest rate risks		83,120	89,554
Other		-	(20,587)
Total capital required	B	361,678	347,912
MCCR ratio (A / B)		344%	406%

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

8. Actuarial liabilities

(a) Nature of actuarial liabilities

Actuarial liabilities are an estimate of the amount which, together with estimated future premiums and investment income, will be sufficient to pay future benefits, dividends, expenses and taxes (other than income taxes) on certificates in force.

Actuarial liabilities are determined using accepted actuarial practice, according to the standards established by the Canadian Institute of Actuaries ("CIA"). The method prescribed by the CIA is CALM.

In determining actuarial liabilities, assumptions are made about future cash flows, thus there is significant risk that actual results will vary from those estimates. The risk varies in proportion to the length of the estimation period and the potential volatility of each assumption. To recognize uncertainty in establishing those estimates and to allow for possible deviation in experience, the Actuary is required to include a margin in each assumption, which has the effect of increasing the actuarial liabilities. A range of allowable margins is prescribed by the CIA. For interest rate risk, the Actuary projects multiple cash flow scenarios for each material product line in order to determine the appropriate provision for adverse deviation. In general, in setting these provisions for adverse deviation, the Actuary has aimed for a reasonable level of conservatism. With the passage of time, and resulting reduction in estimation risk, these provisions will be included in future income to the extent they are not required to cover adverse experience. If estimates of future conditions change throughout the life of a certificate, the effect of those changes is recognized in income immediately.

(b) Actuarial liabilities and supporting assets

Foresters segments its business, taking into account the different liability profiles of its products and in the case of certain United Kingdom business restrictions on the distribution of its surplus. Based on these profiles, Foresters has invested in fixed income securities, equities, mortgages and real estate that have characteristics appropriate for the related actuarial liabilities. In those cases where the characteristics of the invested assets do not fully reflect the needs of the liabilities, derivative financial instruments are used when appropriate (note 7). Actuarial liabilities are matched with assets denominated in the same currency in order to avoid unintended exposure to foreign currency fluctuations.

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

8. Actuarial liabilities (continued)

Assets and liabilities, by geographic segment and by line of business, are comprised as follows:

2008	United States				United Kingdom				Canada				Corporate	Total	
	Insurance	Annuities	Fraternal	Total	Insurance	Annuities	Fraternal	Total	Insurance	Annuities	Fraternal	Total			
	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	
Assets															
Cash and short-term securities	88	477	2,565	3,130	184	27,663	(538)	27,309	18,529	2,749	2,555	23,833	44,025	98,297	
Bonds and fixed-term securities	1,781,829	449,711	273,735	2,505,275	312,953	100,417	28,873	442,243	702,098	200,173	44,332	946,603	776,842	4,670,963	
Mortgages	10,860	10,207	-	21,067	-	-	-	-	-	-	-	-	-	21,067	
Stocks	95,582	12,353	-	107,935	265,289	37,867	-	303,156	41,808	60,749	3,097	105,654	452,421	969,166	
Real estate	-	-	-	-	-	-	-	-	4,000	-	-	4,000	22,468	26,468	
Loans to certificateholders	169,846	-	-	169,846	-	7,528	-	7,528	37,258	-	-	37,258	(13)	214,619	
Other invested assets	36,997	625	11,111	48,733	-	-	-	-	(14,954)	9,878	-	(5,076)	61,591	105,248	
Total invested assets	2,095,202	473,373	287,411	2,855,986	578,426	173,475	28,335	780,236	788,739	273,549	49,984	1,112,272	1,357,334	6,105,828	
Interest due and accrued	22,324	5,600	2,831	30,755	5,063	1,364	-	6,427	5,639	2,187	360	8,186	10,696	56,064	
Other assets	21,586	-	2,964	24,550	170	2,278	3,062	5,510	4,949	601	(880)	4,670	3,940	38,670	
Total assets	2,139,112	478,973	293,206	2,911,291	583,659	177,117	31,397	792,173	799,327	276,337	49,464	1,125,128	1,371,970	6,200,562	
Liabilities and Surplus															
Liabilities															
Net actuarial liabilities	2,177,939	443,701	271,869	2,893,509	586,550	128,164	40,799	755,513	740,675	277,203	46,573	1,064,451	-	4,713,473	
Other policy liabilities	36,087	46,962	-	83,049	7,283	697	-	7,980	48,417	-	-	48,417	-	139,446	
Other liabilities	5,469	3,237	111	8,817	3,769	6,032	24	9,825	24,204	1,709	1,728	27,641	33,939	80,222	
Net deferred gains	17,934	2,010	2,359	22,303	-	-	-	-	149	-	1,416	1,565	218	24,086	
Total liabilities	2,237,429	495,910	274,339	3,007,678	597,602	134,893	40,823	773,318	813,445	278,912	49,717	1,142,074	34,157	4,957,227	
Surplus															
Retained earnings	(98,317)	(16,937)	18,867	(96,387)	(13,943)	42,224	(9,426)	18,855	(14,118)	(2,575)	(253)	(16,946)	1,457,083	1,362,605	
Accumulated other comprehensive income	-	-	-	-	-	-	-	-	-	-	-	-	(119,270)	(119,270)	
Total surplus	(98,317)	(16,937)	18,867	(96,387)	(13,943)	42,224	(9,426)	18,855	(14,118)	(2,575)	(253)	(16,946)	1,337,813	1,243,335	
Total Liabilities and Surplus	2,139,112	478,973	293,206	2,911,291	583,659	177,117	31,397	792,173	799,327	276,337	49,464	1,125,128	1,371,970	6,200,562	

* Intersegment transactions consist primarily of internal financing agreements. They are measured at fair market values prevailing when the arrangements were negotiated. Interest is recorded in net investment income on the consolidated statements of income (loss). The intersegment notes and related interest eliminate on consolidation.

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

8. Actuarial liabilities (continued)

2007	United States				United Kingdom				Canada				Corporate	Total
	Insurance	Annuities	Fraternal	Total	Insurance	Annuities	Fraternal	Total	Insurance	Annuities	Fraternal	Total		
	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$
Assets														
Cash and short-term securities	8,802	5,958	2,794	17,554	240	301	927	1,468	473	3,435	136	4,044	58,444	81,510
Bonds and fixed-term securities	1,429,985	397,223	206,003	2,033,211	356,331	85,066	43,850	485,247	358,025	85,161	40,474	483,660	639,115	3,641,233
Mortgages	14,038	16,084	-	30,122	-	-	-	-	-	-	-	-	-	30,122
Stocks	113,458	10,392	-	123,850	337,166	52,596	-	389,762	46,476	-	4,064	50,540	651,379	1,215,531
Real estate	-	-	-	-	-	-	-	-	-	-	145	145	18,913	19,058
Loans to certificateholders	137,864	-	-	137,864	-	8,485	-	8,485	25,149	-	-	25,149	-	171,498
Other invested assets	75,579	1,242	26,236	103,057	-	-	-	-	-	-	-	-	44,741	147,798
Total invested assets	1,779,726	430,899	235,033	2,445,658	693,737	146,448	44,777	884,962	430,123	88,596	44,819	563,538	1,412,592	5,306,750
Interest due and accrued	17,073	5,268	2,351	24,692	5,851	1,493	-	7,344	3,408	792	365	4,565	10,391	46,992
Other assets	21,184	(79)	9,904	31,009	814	1,070	3,657	5,541	255	96	9,979	10,330	(12,046)	34,834
Total assets	1,817,983	436,088	247,288	2,501,359	700,402	149,011	48,434	897,847	433,786	89,484	55,163	578,433	1,410,937	5,388,576
Liabilities and Surplus														
Liabilities														
Net actuarial liabilities	1,769,706	387,845	234,102	2,391,653	681,775	137,417	47,175	866,367	408,506	90,284	50,043	548,833	-	3,806,853
Other policy liabilities	26,384	40,669	-	67,053	8,229	623	15	8,867	10,962	36	-	10,998	-	86,918
Other liabilities	4,213	3,849	146	8,208	5,824	7,518	-	13,342	1,214	464	1,699	3,377	31,075	56,002
Net deferred gains	16,486	1,848	2,169	20,503	-	-	-	-	168	-	1,600	1,768	201	22,472
Total liabilities	1,816,789	434,211	236,417	2,487,417	695,828	145,558	47,190	888,576	420,850	90,784	53,342	564,976	31,276	3,972,245
Surplus														
Retained earnings	1,194	1,877	10,871	13,942	4,574	3,453	1,244	9,271	12,936	(1,300)	1,821	13,457	1,523,061	1,559,731
Accumulated other comprehensive income	-	-	-	-	-	-	-	-	-	-	-	-	(143,400)	(143,400)
Total surplus	1,194	1,877	10,871	13,942	4,574	3,453	1,244	9,271	12,936	(1,300)	1,821	13,457	1,379,661	1,416,331
Total Liabilities and Surplus	1,817,983	436,088	247,288	2,501,359	700,402	149,011	48,434	897,847	433,786	89,484	55,163	578,433	1,410,937	5,388,576

THE INDEPENDENT ORDER OF FORESTERS

Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

8. Actuarial liabilities (continued)

Provisions made for anticipated future losses of principal and interest on investments and included as a component of actuarial liabilities are as follows:

	2008	2007
	\$	\$
Balance, beginning of year*	13,053	12,207
Net strengthening (release) of provision**	57,511	2,438
Impact of change in foreign exchange rates	7,818	(1,592)
Balance, end of year*	78,382	13,053

* Provisions are net of losses passed-through via credited interest rates and dividends

** The provision increased in 2008 to reflect the deterioration in credit quality of the held-for-trading bonds backing liabilities

(c) Actuarial assumptions

The nature and method of determining the more significant assumptions made by Foresters in the computation of actuarial liabilities are described in the following paragraphs. In all cases, the assumptions are supplemented by the use of margins for adverse deviation.

Certificate claims and benefits

Estimates of the amounts and timing of future claims and benefit payments are based on both Foresters and industry experience over extended periods. Although the pattern of claims and benefit payments may be close to that indicated by past experience, some deviation in that pattern is probable. Annual studies are performed to examine mortality; the actual mortality experience of Foresters is compared to both our expected assumptions and industry expected values to confirm that appropriate assumptions are being made about the projected benefit patterns.

Certificate lapse rates

Certificateholders may allow their certificates to lapse by choosing to discontinue payment of their premiums. On some of the life insurance products, a certain percentage of certificates are expected to lapse prior to maturity. If certificate lapse rates are lower than expected, aggregate claims will be increased and profit will be reduced from anticipated levels. This type of certificate is described as being lapse-supported. On other blocks of business, if certificate lapse rates are higher than originally anticipated, the per unit cost of maintaining certificates in force could rise above levels assumed in the computation of actuarial liabilities. Foresters bases its estimate of future lapse rates on previous experience for each block of business.

THE INDEPENDENT ORDER OF FORESTERS

Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

8. Actuarial liabilities (continued)

Investment income

The computation of actuarial liabilities takes into account projected net investment income on assets supporting these liabilities and income expected to be earned or foregone on reinvestments or financing of mismatched cash flows. Uncertainties exist with respect to the projections of interest rates and the magnitude of credit losses from asset defaults. Foresters accounts for such uncertainties by incorporating provisions for credit losses into projections of investment income (in addition to the allowances for impairment applied as direct reductions to the carrying values of the invested assets).

Certificate maintenance expenses

Amounts are included in actuarial liabilities to provide for the costs of administering certificates in force and include the costs of premium collection, adjudication and processing of claims, periodic actuarial calculations, preparation and mailing of certificate statements, related indirect expenses and overhead. The process of forecasting expenses requires estimates to be made of such factors as inflation, salary rate increases, productivity changes, business volumes and indirect tax rates. Estimates of future certificate maintenance expenses are based on Foresters experience.

The actuarial valuation is somewhat sensitive to this assumption; a 1% ongoing increase in the future maintenance costs assumed would increase the actuarial liabilities by approximately \$5,600.

Certificateholder dividends

Future certificateholder dividends are included in the determination of actuarial liabilities for participating certificates, with the assumption that certificateholder dividends will change in the future to reflect the experience of the respective participating accounts, consistent with the participating certificateholder dividend policy.

(d) Sensitivity to interest rate changes and market risk

Major factors that could impact future interest rate assumptions are changes in the yields available on new investments and changes in future returns expected on the stock market from a change in outlook for capital appreciation (see note 6 c).

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

8. Actuarial liabilities (continued)

(e) Explanation of changes in actuarial liabilities during the year

Changes in actuarial liabilities during the year result from a number of different factors including business activities and changes in actuarial assumption and methods.

	2008	2007
	\$	\$
Actuarial liabilities, beginning of year	3,806,853	4,313,310
Acquisitions	549,965	-
	<u>4,356,818</u>	<u>4,313,310</u>
New business	127,398	115,479
Renewals, maturity, claims and surrenders	(137,569)	(22,913)
Refinement of assumptions (see i) below)	101,259	(19,104)
Refinement of methods and models (see ii) below)	(28,732)	(14,975)
Impact of fair value movement	(166,253)	(10,063)
	<u>(103,897)</u>	<u>48,424</u>
Impact of change in foreign exchange rates	460,552	(554,881)
Actuarial liabilities, end of year	<u>4,713,473</u>	<u>3,806,853</u>

An impact analysis of the major actuarial factors in 2008 and 2007 is as follows:

- i) Changes in actuarial liabilities from assumption refinements in 2008 included: increases due to falling interest rates and decreases due to reduced unit maintenance expense factors for Fraternal benefits, exchange rate movement and improved mortality, lapse and renewal commission assumptions.

Changes in actuarial liabilities from assumption refinements in 2007 included: increases due to falling interest rates, exchange rate movement and dividend scale increases; decreases due to updated mortality and renewal commission assumptions, and decreases related to the expected cost of Havens benefit and reduced unit maintenance expense factors, offset in the fraternal line by the establishment of a new provision for enhancement of member value.

- ii) Changes in actuarial liabilities from refinement of methods and models in 2008 are comprised of an adjustment of mortality assumptions for Life First plans and disability riders, and modeling improvements for Fraternal benefits. In 2007, changes were an adjustment to cost of insurance rates in Universal Life, and modeling improvements for dividend-paying traditional life.

THE INDEPENDENT ORDER OF FORESTERS

Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

9. Income taxes

(a) The components of the total income taxes reported in the consolidated financial statements are:

	2008 \$	2007 \$
Canadian		
Current income taxes	5,788	4,193
Future income taxes	1,649	-
	<u>7,437</u>	<u>4,193</u>
United Kingdom		
Current income taxes	2,313	4,338
Future income taxes	539	(2,737)
	<u>2,852</u>	<u>1,601</u>
Total	<u>10,289</u>	<u>5,794</u>

(b) The components of future income tax balances are as follows:

	2008 \$	2007 \$
Future income tax assets		
Actuarial liabilities	55,876	61,535
Deferred net gains	(12,013)	(10,401)
Tax loss carryforwards	15,982	5,732
Other	1,639	859
	<u>61,484</u>	<u>57,725</u>
Less valuation allowance	(57,186)	(39,672)
Future income tax liabilities arising from investments	(24,511)	(29,116)
Net future income tax asset (liability)	<u>(20,213)</u>	<u>(11,063)</u>

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

9. Income taxes (continued)

(c) Cash taxes paid in 2008 were \$11,308 (2007 - \$8,331).

(d) Income tax expense differs from the amount that would be computed by applying the federal and provincial statutory tax rates to income before taxes for the following reasons:

	2008 %	2007 %
Combined federal and provincial statutory income tax rate for the current year	32.28	34.98
Increase (decrease) in rate due to:		
Lower net average tax rate of foreign jurisdictions and Canadian fraternal operations *	(34.70)	(33.86)
Other	(3.08)	2.89
Effective income tax rate	(5.50)	4.01

* As a fraternal benefit society, Foresters is exempt from paying (recovering) taxes on income (losses) earned in the U.S. and on income (losses) earned on its fraternal operations in Canada. The U.K. tax rates are generally lower than Canadian tax rates.

10. Employee benefit plans

Foresters has a number of funded and unfunded defined benefit and defined contribution pension plans, that provide pension, other retirement and post-retirement benefits to its employees in Canada, the United States and the United Kingdom. The defined benefit pension plans provide benefits based on a final average earnings formula. Foresters also provides post-retirement health benefits to certain employee groups in Canada and the U.S.

Actuarial valuations of the pension and post-retirement benefit plans are performed periodically for accounting purposes, based on the market-related discount rate and management's best estimate assumption.

THE INDEPENDENT ORDER OF FORESTERS

Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

10. Employee benefit plans (continued)

Foresters measures its accrued benefit obligations and the fair value of plan assets for accounting purposes as at December 31 of each year. The most recent actuarial valuation of the pension plans for funding purposes was December 31, 2006 for the North American plans and March 2008 for the U.K. The effective date of the next required valuation is December 31, 2009 for the North American plans and March 2011 for the U.K.

The following table presents information related to Foresters defined benefit plans, including amounts recorded on the consolidated balance sheets and the components of net periodic benefit cost:

	2008		2007	
	Pension benefits \$	Other benefits \$	Pension benefits \$	Other benefits \$
Reconciliation of accrued benefit obligation				
Accrued benefit obligation, beginning of year	157,118	17,714	165,444	21,881
Acquisitions during the year – Unity	-	1,039	-	-
Service cost	5,585	742	5,446	302
Employee contributions	-	-	52	-
Interest cost	9,037	831	8,355	827
Benefits paid	(7,568)	(904)	(7,201)	(904)
Actuarial (gains)/losses	(37,783)	(1,126)	(10,515)	(1,756)
Impact of change in foreign exchange rates	1,361	3,191	(4,463)	(2,636)
Accrued benefit obligation, end of year	127,750	21,487	157,118	17,714
Reconciliation of fair value of plan assets:				
Fair value of plan assets, beginning of year	225,768	-	229,489	-
Return on plan assets	(18,503)	-	8,615	-
Employer contributions	855	-	703	-
Employee contributions	-	-	52	-
Benefits paid	(7,568)	-	(7,201)	-
Impact of change in foreign exchange rates	2,537	-	(5,890)	-
Fair value of plan assets, end of year	203,089	-	225,768	-
Funded status:				
Funded status – plan surplus (deficit)	75,339	(21,487)	66,950	(17,714)
Unamortized net actuarial gains/(losses)	(30,671)	(8,470)	(23,851)	(6,408)
Unamortized transitional obligation	(28,498)	447	(30,516)	496
Accrued benefit asset (liability)	16,170	(29,510)	12,583	(23,626)

The net accrued benefit liability of \$13,340 (2007 – \$11,043) has been recorded on the consolidated balance sheets in other liabilities.

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

10. Employee benefit plans (continued)

Included in the above accrued benefit obligations and fair value of plan assets at year end were the following amounts in respect of plans that were not fully funded:

	2008		2007	
	Pension benefits \$	Other benefits \$	Pension benefits \$	Other benefits \$
Accrued benefit obligation	(9,153)	(21,487)	(25,716)	(17,714)
Fair value of plan assets	-	-	14,500	-
Funded status – plan deficit	(9,153)	(21,487)	(11,216)	(17,714)

The total cash payments made by Foresters to the pension plans and other benefit plans were as follows:

	2008		2007	
	Pension Benefits \$	Other Benefits \$	Pension Benefits \$	Other Benefits \$
Defined benefit	855	905	704	904
Defined contribution	1,564	-	1,575	-
Total	2,419	905	2,279	904

A breakdown of the fair value of plan assets by major asset category was as follows:

	2008		2007	
	Pension Benefits %	Other Benefits %	Pension Benefits %	Other Benefits %
Stocks	35	-	41	-
Fixed income securities	62	-	58	-
Other	3	-	1	-
Total	100	-	100	-

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Notes to Consolidated Financial Statements

For the years ended December 31 (In thousands of Canadian dollars)

10. Employee benefit plans (continued)

Foresters net defined benefit plan expense is as follows:

	2008		2007	
	Pension benefits \$	Other benefits \$	Pension benefits \$	Other benefits \$
Actual costs arising in the period				
Service cost (employer portion)	5,585	742	5,446	302
Interest cost	9,037	831	8,355	827
Actual return on plan assets	18,503	-	(8,615)	-
Actuarial (gains) losses	(37,783)	(1,126)	(10,515)	(1,756)
Pension costs incurred before adjustment	(4,658)	447	(5,329)	(627)
Differences between costs arising in the year and cost recognized in respect of:				
Return on plan assets	(31,430)	-	(4,177)	-
Actuarial (gains) losses	37,245	607	9,827	1,414
Plan amendments	-	-	-	(95)
Amortization of net transitional obligations	(2,258)	50	(2,263)	50
Net benefit plan (income) expense	(1,101)	1,104	(1,942)	742

The defined contribution plan expense for 2008 was \$1,564 (2007- \$1,575).

The weighted average actuarial assumptions used in the measurement of Foresters benefit obligation and expenses were as follows:

	2008		2007	
	Pension benefits	Other benefits	Pension benefits	Other Benefits
Assumptions used to calculate benefit expense				
Discount rate	5.6%	5.7%	5.2%	5.7%
Expected long-term rate of return on plan assets	5.8%	-	5.7%	-
Rate of compensation increase	3.7%	-	3.7%	-
Assumptions used to calculate benefit obligations				
Discount rate	7.3%	6.5%	5.6%	5.7%
Rate of compensation increase	3.7%	-	3.7%	-

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10. Employee benefit plans (continued)

The healthcare cost inflation assumption for Canadian benefits was 6.1% per year, (2007 – 7.0% per year), decreasing to 4.7% in 2013 and thereafter. The post medicare inflation assumption for the United States benefits was 9.0% for 2008 (2007 – 9.4%) decreasing to 4.5% by 2028 and thereafter.

A 1% change in the assumed healthcare trend rate would have the following effects:

	1% Increase	1% Decrease
Effect on service cost plus interest cost for 2008	92	(77)
Effect on accrued benefit obligation as at December 31, 2008	1,164	(1,011)

11. Segmented information

Foresters manages its business and distributes its general fund insurance and annuity products and its and segregated fund products through operating segments in the United States, Canada and the United Kingdom. Each operating segment includes both insurance and fraternal operations which work together to develop and distribute products in the local markets. The basis of accounting used in the presentation of these segments is consistent with that described in the summary of significant accounting policies (see note 2).

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11. Segmented information (continued)

	2008					2007				
	United States \$	United Kingdom \$	Canada \$	Corporate \$	Total \$	United States \$	United Kingdom \$	Canada \$	Corporate \$	Total \$
Revenue										
Premiums										
Insurance	169,578	125,651	57,669	-	352,898	140,275	159,246	25,374	-	324,895
Annuities	19,837	37,575	40,333	-	97,745	31,853	21,456	4,675	-	57,984
Net investment income	32,780	(73,253)	(14,789)	(39,463)	(94,725)	175,575	50,895	16,545	135,362	378,377
Other income	3,497	-	2,498	15,978	21,973	8,110	534	2,837	5,425	16,906
	<u>225,692</u>	<u>89,973</u>	<u>85,711</u>	<u>(23,485)</u>	<u>377,891</u>	<u>355,813</u>	<u>232,131</u>	<u>49,431</u>	<u>140,787</u>	<u>778,162</u>
Certificateholder benefits and expenses										
Certificateholder benefits	204,389	99,652	63,120	-	367,161	209,628	93,158	38,665	-	341,451
Changes in actuarial liabilities	(39,506)	(36,317)	(28,074)	-	(103,897)	(8,169)	90,644	(34,051)	-	48,424
Dividends	26,690	5,178	13,128	-	44,996	25,953	6,643	7,660	-	40,256
Agent compensation	53,306	14,138	25,084	315	92,843	35,688	14,761	3,122	1,936	55,507
Operating expenses	88,440	11,794	28,369	18,222	146,825	77,600	14,935	20,578	17,380	130,493
Fraternal investment	9,044	1,572	6,184	-	16,800	10,355	1,848	5,199	-	17,402
	<u>342,363</u>	<u>96,017</u>	<u>107,811</u>	<u>18,537</u>	<u>564,728</u>	<u>351,055</u>	<u>221,989</u>	<u>41,173</u>	<u>19,316</u>	<u>633,533</u>
Net income (loss) before income taxes	(116,671)	(6,044)	(22,100)	(42,022)	(186,837)	4,758	10,142	8,258	121,471	144,629
Income taxes	-	2,240	2,366	5,683	10,289	-	881	-	4,913	5,794
Net income (loss)	<u>(116,671)</u>	<u>(8,284)</u>	<u>(24,466)</u>	<u>(47,705)</u>	<u>(197,126)</u>	<u>4,758</u>	<u>9,261</u>	<u>8,258</u>	<u>116,558</u>	<u>138,835</u>
Other comprehensive income (loss)	-	-	-	24,130	24,130	-	-	-	(295,485)	(295,485)
Total comprehensive income (loss)	<u>(116,671)</u>	<u>(8,284)</u>	<u>(24,466)</u>	<u>(23,575)</u>	<u>(172,996)</u>	<u>4,758</u>	<u>9,261</u>	<u>8,258</u>	<u>(178,927)</u>	<u>(156,650)</u>

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12. Contingent liabilities

From time to time in connection with its operations, Foresters and its subsidiaries are named as defendants in actions for damages and costs allegedly sustained by the plaintiffs. While it is not possible to estimate the outcome of the various proceedings at this time, such actions have generally been resolved with minimal damages or expense in excess of amounts provided in actuarial liabilities and Foresters does not believe that it will incur any significant additional loss or expense in connection with such actions.

13. Subsequent event

Acquisition of the business segment of GeniSys Management Systems

Unity entered into an agreement during 2008 to acquire certain assets of GeniSys Management Systems for approximately \$1,949. This transaction is expected to be completed by the end of the first quarter of 2009.