

**Western Financial Group Inc.**

**ANNUAL INFORMATION FORM**

**MARCH 30, 2007**

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## **GLOSSARY OF SELECTED TERMS**

actuarial analysis	Evaluation of risks in order to attempt to assure that premiums and loss reserves adequately reflect expected future loss experience and claims payments; in evaluating risks, mathematical models are used to predict future loss experience and claims payments based on past claims ratios and loss development patterns and other relevant data and assumptions.
agent	An intermediary appointed by an insurer to procure applications for insurance, receiving a commission from the insurer for policies written.
basic commission	A fee received by a broker for selling a P&C insurance policy on behalf of a P&C insurer.
broker	A person or firm who negotiates contracts of insurance or reinsurance, receiving a commission for placement and other services rendered, between (1) a policy holder and a primary insurer, on behalf of the insured party, (2) a primary insurer and reinsurer, on behalf of the primary insurer, or (3) a reinsurer and a retrocessionaire, on behalf of the reinsurer.
cede; ceding company	When a party reinsures its liability with another, it "cedes" business and is referred to as the "ceding company".
claim	The amount demanded under a policy of insurance or reinsurance arising from the loss relating to an insured event. A claim is also referred to as a loss.
contingent commission	A fee received by a broker on an annual basis based on the previous years' business written with the particular P&C insurer. The amount of these commissions are based primarily on the profitability (based on claims ratios) of the aggregate policies sold by the broker for a given P&C insurance company and may also include volume, concentration of business and year-over-year growth.
critical illness insurance	An individual insurance policy which pays a lump sum of cash should the policyholder be diagnosed with an illness specified in the policy.
direct premiums written	The total premiums from the primary insured in respect of insurance underwritten by an insurer during a specified period.
disability income insurance	An individual insurance policy which pays a monthly cash benefit should the policyholder be unable to perform the substantial duties of his/her occupation due to illness or accident.
excess coverage	Additional coverage for any amounts provided by government-owned subsidiaries.
excess insurance	Additional casualty coverage above a specified layer of existing insurance coverage.

liability insurance	Insurance which is primarily concerned with losses caused by negligent acts and/or omissions of the insured in the conduct of its business resulting in bodily injury and/or property damage to third parties, injury resulting from the use of a product manufactured or distributed by a business, or injury occurring in the general operation of a business.
loss	Event that triggers the payment of a claim which is covered by an insurance policy. An event or series of events arising from a particular cause which gives rise to an insured or reinsured loss. Depending on the wording of the reinsurance agreement, such "event" may also include continuous exposure to conditions giving rise to losses, which may be generated under certain forms of casualty insurance coverage.
Managing General Agents	An organization that contracts with a life insurance company to provide distribution and administration services in connection with supplying insurance products of the company to licensed insurance agents and brokers.
MCCSR	Minimum continuing capital and surplus requirements that federal life and health insurance companies must meet pursuant to applicable regulatory requirements. It is determined by applying factors for each of the following five risk components to specific on- and off-balance sheet assets or liabilities and by adding the results: asset default risk, mortality/morbidity/lapse risks, interest margin pricing risk, changes in interest rate environment risk and segregated funds risk.
P&C	Property and casualty.
property insurance	Insurance that provides coverage to a person with an insurable interest in tangible property for that person's property loss, damage or loss of use.
reinsurance	An arrangement in which an insurance company, the reinsurer, agrees to indemnify another insurance or reinsurance company, the ceding company, against all or a portion of the insurance or reinsurance risks underwritten by the ceding company under one or more policies.
retention	The amount or portion of risk that an insurer retains for its own account.
term life insurance	An individual life insurance policy insuring the life of the policyholder which pays the specified insurance amount at death in cash to the designated beneficiary. Premium rates do not change during each renewal period.
Third Party Administrator	An organization that contracts with a life insurance company to perform the administrative service requirements necessary to service a program of insurance or product line of business on behalf of the insurance company.
underwriter	An individual who examines, accepts or rejects risks and classifies accepted risks in order to charge an appropriate premium for each accepted risk. The underwriter is expected to select business that will produce an

average risk of loss no greater than that anticipated for the class of business.

underwriting                      The insurer's or reinsurer's process of reviewing applications submitted for insurance coverage, deciding whether to accept all or part of the coverage requested and determining the applicable premiums; also refers to the acceptance of such coverage.

universal life insurance        An individual life insurance policy insuring the life of the policyholder, which pays the specified insurance amount at death in cash to the designated beneficiary. Premium rates include an investment element which accrues earnings on behalf of the policyholder and can therefore provide policy benefits during the lifetime of the policyholder.

### **FORWARD LOOKING STATEMENTS**

Certain information included or incorporated by reference herein is forward-looking. Forward-looking statements include, without limitation, statements regarding the future financial position, business strategy, budgets, litigation, projected costs, capital expenditures, financial results, taxes and plans and objectives of or involving us or our subsidiaries. Many of these statements can be identified by looking for words such as "believe", "expects", "expected", "will", "intends", "projects", "anticipates", "estimates", "continues" or similar words. Forward looking statements in this annual information form ("AIF") include, but are not limited to, capital expenditures, business strategy and objectives, acquisition and growth strategy, industry trends including expected continued consolidation, P&C insurance industry premium growth rates, contingent commission rates, expansion plans and future revenues. We believe the expectations reflected in such forward-looking statements are reasonable but no assurance can be given that these expectations will prove to be correct and such forward-looking statements should not be unduly relied upon.

In addition to other assumptions identified in this AIF, assumptions have been made regarding, among other things:

- our ability to continue to locate suitable acquisition targets at economic prices;
- our ability to market our products and services successfully to existing and new customers;
- the timely receipt of required regulatory approvals and the costs of continued compliance with regulatory requirements; and
- our ability to obtain financing on acceptable terms.

Forward-looking statements are not guarantees of future performance and involve a number of risks and uncertainties some of which are described herein. Such forward-looking statements necessarily involve known and unknown risks and uncertainties, which may cause our actual performance and financial results in future periods to differ materially from any projections of future performance or results expressed or implied by such forward-looking statements. These risks and uncertainties include but are not limited to the risks identified in this AIF under the heading "Risk Factors". Any forward-looking statements are made as of the date hereof and we do not undertake any obligation to publicly update or revise such statements to reflect new information, subsequent or otherwise.

## **MARKET AND INDUSTRY DATA**

This AIF includes market share and industry data and other statistical information that we have obtained from independent industry publications, government publications, market research reports and other published independent sources, including Canadian Underwriter and the Insurance Journal, monthly industry publications, The Insurance Brokers Association of Canada ("IBAC"), a federation of 11 provincial and regional associations representing P&C insurance brokers in Canada, A.M. Best Company ("A.M. Best"), a worldwide insurance-rating and information agency, Canadian Life and Health Insurance Association ("CLHIA"), a voluntary trade association representing member life and health insurers and Statistics Canada, the Canadian national statistics agency. Industry publications and surveys generally state that the information contained therein has been obtained from sources believed to be reliable. Although we believe these industry publications to be reliable, we have not independently verified any of the data contained therein, nor have we ascertained the underlying economic or other assumptions relied upon by these sources, and cannot provide any assurance as to the accuracy or completeness of the information.

Unless otherwise indicated, all P&C insurance market share and industry data contained in this AIF relates to the private Canadian P&C insurance industry and does not include data relating to government-owned automobile insurance companies.

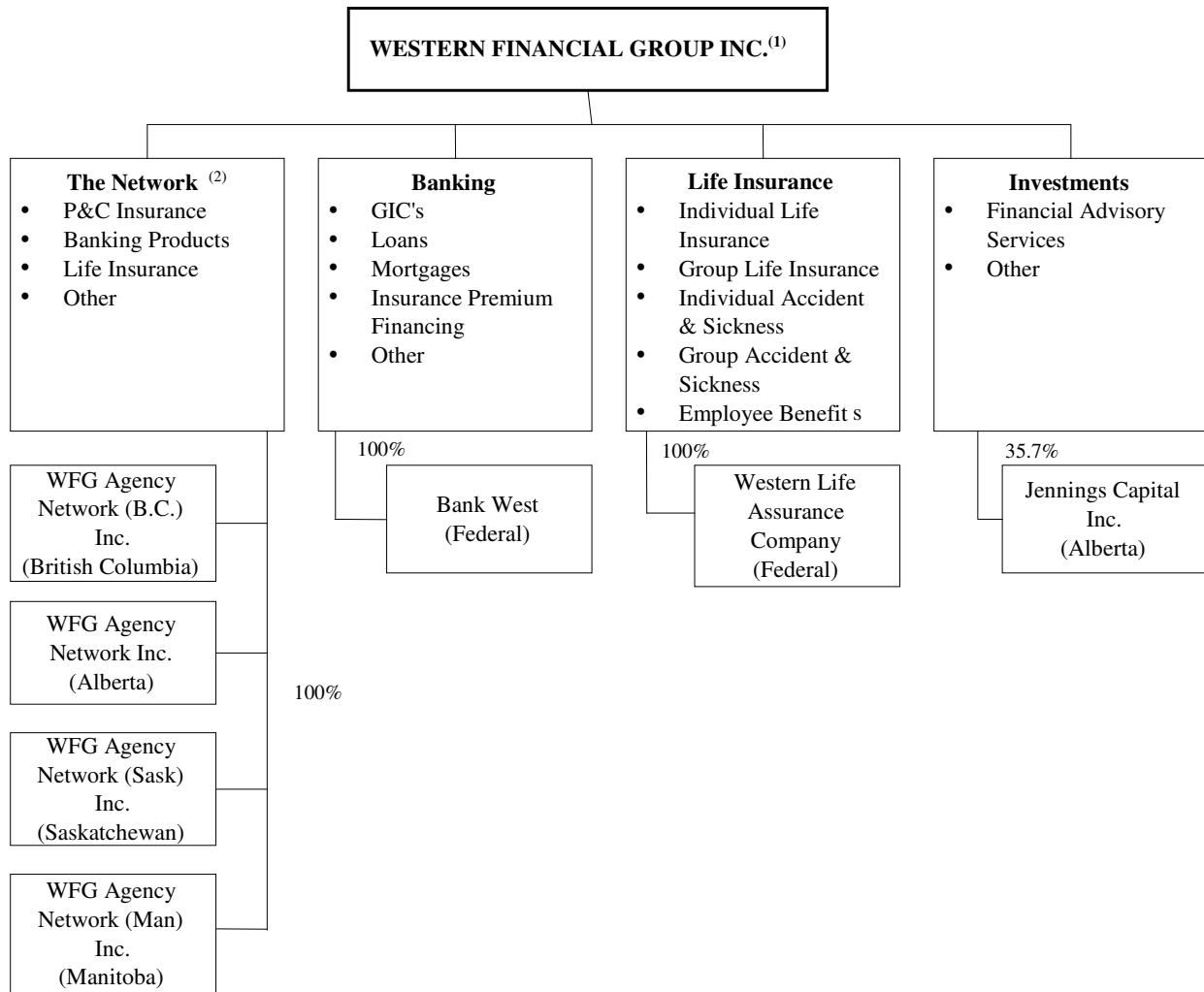
## **GROWTH MEASURES**

Throughout this AIF, we use the terms "compound annual growth rate" or "CAGR" in reference to the rates of growth of various financial or operational data. CAGR is a mathematical formulae that provides a smoothed rate of return over a period of time and does not detail any volatility in such rate. Readers are cautioned that CAGRs may suggest a steady growth rate even when the growth of the underlying data being measured can vary significantly depending on the period of time measured.

## CORPORATE STRUCTURE

We were incorporated as 674658 Alberta Inc. by certificate of incorporation issued under the *Business Corporations Act* (Alberta) on November 14, 1995. We changed our name to Hi-Alta Capital Inc. by certificate of amendment dated January 22, 1996, after which we commenced active business operations. We changed our name to Western Financial Group Inc. by certificate of amendment dated May 27, 2002. Our head office is located at 1010 - 24 Street West, High River, Alberta, T1V 2A7 and our registered address is 3700, 400 - 3rd Avenue S.W., Calgary, Alberta, T2P 4H2.

The following chart illustrates our organizational structure by business unit and our material subsidiaries (including their respective jurisdictions of incorporation) that operate within each of those business units.



**Notes:**

- (1) All of the legal entities in the above chart are wholly-owned direct or indirect subsidiaries except where otherwise indicated.
- (2) The Network also has strategic investments which consist of equity investments ranging from 20% - 50% in two companies which have an aggregate of 14 affiliated offices representing 11 communities in the Provinces of British Columbia and Saskatchewan. Western Financial Group has a strategic investment which consists of an equity investment of 25% in the largest independent insurance broker/administrator in Manitoba with offices in Ontario, Quebec and Nova Scotia with 6 offices in 4 communities.

## DEVELOPMENT OF THE BUSINESS

### History

We commenced business in January 1996 as Hi-Alta Capital Inc. and our common shares ("Common Shares") were listed on the Alberta Stock Exchange in May of that year after we acquired our first broker in High River, Alberta. The Common Shares were subsequently listed on the Toronto Stock Exchange ("TSX") in 1998. Since inception, we expanded our business and that of WFG Agency Network (the "Network") through the acquisition and integration of 94 wholly-owned, affiliate and partner offices, consisting primarily of insurance brokerages but including travel agencies and related businesses in 77 communities most of which are located in Western Canada.

In 2000, to broaden our product offering to our customers, we introduced financial products and services such as agency banking, life insurance and mutual funds in nearly half of our then existing branch offices. This decision, and our customers' desire to have a diversified product and service offering, propelled the growth of assets under administration ("AUA"), in the form of agency deposits, segregated funds and mutual funds. In 2002, we took advantage of an opportunity to further expand our financial services offering to our customers by acquiring a 26.5% equity interest in Jennings, a full service investment dealer headquartered in Calgary, Alberta, which interest we subsequently increased to 35.7%. Also in 2002, we obtained a Canadian bank charter for our wholly owned direct subsidiary, Bank West, enabling us to offer our customers proprietary banking products such as deposits, residential and commercial mortgages and insurance policy premium financing. To reflect our regional focus and our diversified financial services product offering we changed our name to Western Financial Group Inc. on May 27, 2002.

In late 2003, to further expand the services available to our customers, we established The Western Mutual Fund Company ("WMFC") to provide third party mutual funds and mutual fund services, including supervisory and processing services, to the Network.

In an effort to continue to expand our financial products and services offering, we acquired Western Life, a federally regulated life and health insurance company for an aggregate purchase price of \$20.0 million (the "Acquisition") on February 28, 2005. The Acquisition was funded from our public offering of subscription receipts ("Subscription Receipts") pursuant to an underwriting agreement dated January 26, 2005 among us and CIBC World Markets Inc., First Associates Investments Inc. and Jennings Capital Inc. (the "Underwriting Agreement"). The public offering was completed February 3, 2005 and raised approximately \$22.3 million in gross proceeds. The Acquisition added a comprehensive suite of "house brand" life and health insurance products to our product and services offering. See "Description of Our Business - Western Life". For additional information relating to the Acquisition, please refer to our Business Acquisition Report dated May 12, 2005 which is incorporated by reference herein and is available on SEDAR at [www.sedar.com](http://www.sedar.com).

During 2005, we entered into a business relationship with Harvard Developments to combine two well known Regina insurance brokers, Cooks McCallum Hill Insurance and our ISI Agency with an aggregate of four offices, under one company, Harvard Western Ventures Inc. Both local brand names were combined and the offices now operate under the name Cooks ISI Insurance. This partnership forms the first step in a major initiative to expand the traditional Network presence into strong insurance brokers in the larger metropolitan markets in Western Canada. We acquired five additional brokerages in Western Canada and purchased 20% of Falkins Insurance Group Limited, with ten offices in British Columbia.

At the end of 2005, we made a business decision to cease operations of WMFC and to transfer our clients' mutual fund accounts that were being managed by WMFC to Jennings. See "Description of Our Business - Investment Businesses - The Western Mutual Fund Company Ltd."

During 2006, we acquired a 25% interest in Hayhurst Elias Dudek Inc. ("HED"), which is one of the largest independently owned insurance brokers in Canada, with approximately 190 employees nationwide. HED's head office and the majority of employees are located in Winnipeg, with additional offices in Toronto, Montreal and Halifax. HED operates three core product segments: commercial property and casualty, life and health and pet health insurance through its subsidiary, SecuriCan General Insurance Company, the leading provider of pet insurance in Canada, sold under the Petplan brand.

During 2006, we purchased 25% of Northcountry Insurance Agencies Ltd. which serve seven communities in British Columbia and purchased all of the outstanding shares of Gold Eagle Agencies Ltd. in Vegreville, Alberta, 606065 Alberta Ltd. in Leduc, Alberta, 1176496 Alberta Ltd., and 1194595 Alberta Ltd. in Spruce Grove, Alberta, Willow Creek Insurance (1990) Ltd. in Claresholm, Alberta and Thomsen Fisher Insurance Ltd., in Medicine Hat, Alberta.

In 2006 we also announced that our board of directors had approved a change to our dividend policy such that, upon satisfaction of certain conditions, we plan to commence payment of a quarterly cash dividend on July 1, 2007. See "Dividend Policy"

In the second quarter of 2006, we redeemed all of our approximately \$10.5 million outstanding 9% convertible debentures in exchange for the issuance of approximately 4.2 million Common Shares at a deemed price of \$2.50 per Common Share.

Also in 2006, we raised gross proceeds of \$15.0 million through the issuance of 150,000 First Preferred Shares, Series Two in order to finance our ongoing broker acquisition program. See "Capital Structure - First Preferred Shares, Series Two". In the fourth quarter of 2006 we raised \$26.6 million through a public offering of our Common Shares to finance our ongoing broker acquisition program. The public offering of common shares was made pursuant to an underwriting agreement dated November 10, 2006 among us and Desjardins Securities Inc., Jennings Capital Inc., CIBC World Markets Inc., TD Securities Inc. and Acumen Capital Finance Partners Limited (the "2006 Underwriting Agreement").

In the fourth quarter of 2006 and during the first quarter of 2007, we completed the acquisition of 15 additional locations in northern British Columbia with the acquisition of the Sawchuk Group, with offices in Dawson Creek, Fort St. John, Fort Nelson and Northcountry Insurance Agencies Ltd. with locations in 100 Mile House, Burns Lake, Fraser Lake, Houston, Smithers, Vanderhoof and Williams Lake, British Columbia. Finally, in the first quarter of 2007, we acquired Silver Star Brokers in Vernon, British Columbia and the remaining 75% of Northcountry Insurance Agencies Ltd.

Through these acquisitions and the expansion of our financial products and services offering, we have built a strong regional distribution network that we intend to further leverage to provide our customers with a full range of financial products and services under a unified and recognizable brand.

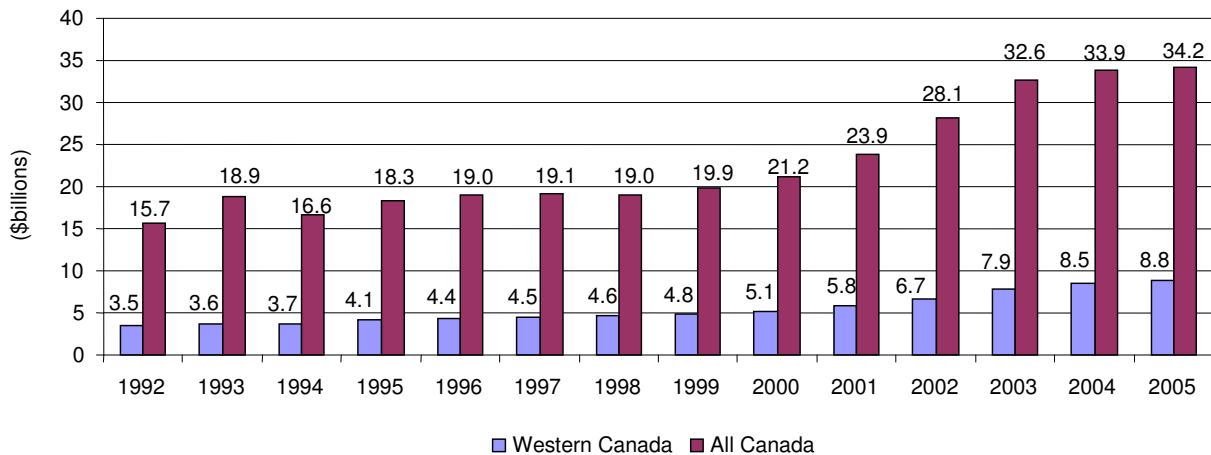
## INDUSTRY OVERVIEW

### The P&C Insurance Industry

#### General

The P&C insurance industry provides automobile, personal and commercial property, liability and other types of P&C insurance to individuals and businesses. P&C insurance provides coverage for losses or liability arising from the occurrence of certain events. The graph below depicts the growth in total direct premiums written since 1993 in Western Canada and the rest of Canada.

**P&C Insurance Industry  
Direct Premiums Written by Geographic Region**



Source: Canadian Underwriter 2006 Statistical Issue.

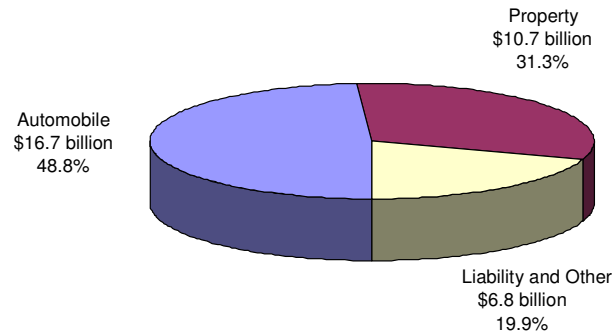
The P&C insurance industry is a mature market and has historically experienced moderate growth. According to Canadian Underwriter, from 1993 to 2000 the CAGR of the P&C insurance industry's direct premiums written in Western Canada was 5.6%. The industry grew faster in Western Canada compared with the rest of the country over the past 10 years with a CAGR in direct premiums written at 8.9% in Western Canada compared to the national rate of 7.2%, reflecting a higher than average population and economic growth rate in the region. We do not expect significant rate changes beyond the normal rate of inflation for the next 12-24 months.

#### **P&C Insurance Products**

The P&C insurance industry classifies its business by the characteristics of the customer. Personal lines business relates to insurance purchased by individuals and includes home, automobile, property and liability insurance products. Commercial lines business relates to insurance purchased by businesses and includes farms, institutions, associations and not-for-profit organizations and consists of commercial liability policies, property insurance, automobile insurance, fidelity insurance, surety insurance, specialized liability policies and other specialty lines.

The chart below indicates the percentage and dollar amounts of the P&C insurance industry's direct premiums written in 2005 by line of business and demonstrates that automobile insurance is the largest component followed by property and liability and other insurance.

### P&C Insurance Industry 2005 Direct Premiums Written By Line of Business<sup>(1)</sup>



Source: Canadian Underwriter 2006 Statistical Issue.

**Note:**

(1) Includes both personal and commercial lines of P&C insurance.

#### ***Automobile Insurance***

Automobile insurance provides coverage against losses incurred from personal bodily injury, bodily injury to third parties, property damage to an insured's vehicle and property damage to other vehicles and other property resulting from the ownership, maintenance or use of automobiles. The automobile insurance markets in Western Canada vary significantly because of the different regulatory regimes that govern the industry in each province. In Alberta, automobile insurance is offered by private insurance companies with a maximum limit on the amount of premiums for a single policy mandated by the province. Commission levels for automobile insurance in Alberta are generally 12.5%. British Columbia, Saskatchewan and Manitoba each have a government-owned insurance company as the primary provider of automobile insurance to the public. In these provinces, private insurance companies are only able to provide excess coverage. In these provinces, brokers are the main distribution channel for the government insurance providers and are paid a combination of fees and commissions for their services. The basic commissions in British Columbia range from 3.0% to 6.0% for mandatory coverage and we estimate the average to be 12.5% for excess coverage of written premiums. In Saskatchewan, we estimate basic commissions are, on average, 2.0% of written premiums on the mandatory coverage and 12.5% on excess coverage. In Manitoba, basic commissions range from 6.0% to 7.0% of written premiums on the mandatory coverage and we estimate the average to be 12.5% on excess coverage.

#### ***Property Insurance***

Property insurance is the second largest component of the P&C insurance industry by direct premiums written. Property insurance provides coverage for loss or damage to buildings, contents, inventory and equipment.

## **Liability Insurance**

Liability insurance provides coverage for liability exposures, including bodily injury and property damage, arising from products sold and general business operations. Specialized liability policies may also include coverage for directors' and officers' liability insurance, fiduciary liability for trustees and sponsors or pension, health and welfare and other employee benefit plans, errors and omissions insurance, as well as umbrella and excess insurance.

### ***Other***

Other types of P&C insurance include fidelity insurance, which protects an insured for loss due to embezzlement or misappropriation of funds by an employee; surety insurance, which is a three-party agreement whereby the insurer agrees to pay a second party or make complete an obligation in response to the default, acts or omissions of a third-party; and other specialty lines including boiler and machinery insurance, marine insurance and aircraft insurance.

## **The P&C Insurance Brokerage Industry**

### **General**

Brokers are the main distribution channel for the P&C insurance industry, representing an estimated 72-78% of direct premiums written in 2005, according to IBAC. The remaining percentage includes P&C insurance products distributed through both the direct channel and through captive agents. According to IBAC, there are approximately 30,000 individuals licensed as brokers in Canada.

Brokers sell policies issued by P&C insurance companies that underwrite the risk. Brokers collect premiums on behalf of the P&C insurance companies and are paid a commission on the premium amount sold. Brokers sell insurance products of more than one P&C insurance company in contrast to the agents of P&C insurance underwriters (direct writers or captive agents) who only sell the products of their respective insurance companies.

Brokers operate as retailers of P&C insurance products and do not assume any liability for claims, expenses or payments if their customers experience losses. The payment of claims and related expenses is the responsibility of the P&C insurance companies that underwrite the risk. The occurrence of claims during a policy term has no direct impact on basic commissions paid to the broker, although it may affect contingent commissions (as described in the next section).

Direct distribution is a method by which P&C insurance companies sell their insurance policies directly to customers without the use of an intermediary. The direct distribution channel conducts business with customers primarily through call centers or through the Internet. Captive agents are a proprietary sales force that exclusively distribute a particular P&C insurance company's products. P&C insurance companies may use any combination of these channels to distribute their insurance products.

### **Commission Structure**

After the broker places the customer's policy with a P&C insurance company, the broker receives a commission from the P&C insurance company as compensation for the services provided. The two types of commissions paid to the broker are basic and contingent.

Basic commissions vary by type of insurance and are paid by P&C insurance companies to brokers on a policy-by-policy basis when policies are written. Commissions range from 5.0% to 20.0% of the written

premium and are typically paid at a rate of 12.5% of written premiums for automobile insurance and 20.0% of written premiums for property and liability insurance.

Contingent commissions are paid to brokers on an annual basis based on previous years' business written with the particular P&C insurer. The amount of these contingent commissions is based primarily on the profitability (based on claims ratios) of the aggregate policies sold by the broker for a given P&C insurance company (the "Portfolio") and may also include volume, concentration of business written, renewal ratios and the year-over-year premium growth of the Portfolio. The quantum of contingent commissions varies from one P&C insurance company to another and between regions, but we believe generally represents approximately 1.0-2.0% of the premiums earned in relation to a Portfolio. As contingent commissions are paid to a broker based on aggregate annual performance, they cannot be directly linked to any individual policy.

Many P&C insurance companies pay us contingent commissions for achieving profitability and premium volume goals set by them and/or based on the loss experience of the insurance we place with them. We generally receive contingent commissions in the first and second quarters of each year in respect of contingent commissions earned in the previous year. However, we have no control over the ability of P&C insurance companies to estimate loss reserves, which is a factor that affects the amount of contingent commissions we will receive. In addition, because no significant incremental operating costs are incurred when contingent commissions are realized, a significant decrease in contingent commissions can cause a disproportionate decrease in net income and would consequently have a negative impact on our financial results.

## **Trends**

We believe that the P&C insurance brokerage industry is sensitive to changes in the P&C insurance industry as a whole. The P&C insurance industry is competitive and highly fragmented with approximately 100 private and government-owned insurers in Canada. In 2005, according to Canadian Underwriter, the top five private P&C insurers accounted for approximately 35.8% of the industry's private direct premiums written. In our management's view, this competition has led P&C insurance companies to seek to reduce costs, including distribution costs, and to increase efficiency. These trends in the P&C insurance industry have generally resulted in P&C insurance companies requiring increased service and efficiency from brokers. The costs of meeting these requirements, which typically include the upgrade and maintenance of technology and information systems and the addition and training of staff, can be significant and are borne by the brokers. Many P&C insurers have also established minimum annual premium volumes as a condition to allowing brokers to distribute their products. We believe that a significant number of brokers are either unable or unwilling to meet these volume demands or increase their investments in their businesses and staff, leading to consolidation opportunities in the P&C insurance brokerage industry. Brokerage consolidators, such as ourselves, have adopted a strategy of acquiring and consolidating small to medium-sized independent brokers with a view to strengthening their competitive positions and increasing their market share. We believe these trends have resulted in significant consolidation in the P&C insurance brokerage industry in recent years and we expect this trend to continue for the foreseeable future.

In addition to consolidation trends, the P&C insurance brokerage industry is facing increasing competition for the sale of policies from P&C insurance companies that have established direct distribution channels primarily through call centers or the Internet. Competition is also expected to emerge from other financial groups, such as the Canadian chartered banks, which continue to lobby for the right to create and market all types of insurance products through their branch networks.

## **Life and Health Insurance Industry**

The life and health insurance industry provides Canadians with insurance coverage to mitigate the financial effects of certain events and helps individuals plan their financial future. Traditional insurance products, such as life and health insurance, spread risk across many persons to insure against loss of life, serious disability affecting employment, or the need for additional medical attention.

According to the CLHIA, in 2005, approximately 24 million Canadians and their dependants were covered by some form of life and health insurance, with domestic-based companies accounting for over 90.0% of the premiums. Furthermore, the total value of life insurance owned by Canadians was over \$2.7 trillion.

As of December 31, 2005 the CLHIA indicated that Canada's life and health insurance industry was comprised of 105 firms, down from 163 firms in 1990. According to Statistics Canada, this decline is largely the result of foreign insurers selling their operations to Canadian insurance companies, although there has also been significant consolidation activity amongst Canadian companies.

### **DESCRIPTION OF OUR BUSINESS**

We are a financial services organization which provides insurance, financial services and banking services to more than 350,000 individuals and businesses in Western Canada through our WFG Agency Network (the "Network"), affiliated insurance brokers, Western Life Assurance Company ("Western Life") and Bank West.

Our primary business is the ownership and operation of WFG Agency Network, which serves 61 communities with 74 offices in British Columbia, Alberta, Saskatchewan and Manitoba. The Network employs approximately 630 full time and part time employees. Through the Network, we are one of the largest P&C insurance broker in Canada and the largest in Western Canada. In addition, we have made investments in strategic partnerships in smaller western communities to begin the process of entering key markets through partial ownership of successful firms where our ultimate long-term goal is full ownership. We have affiliated offices in 11 communities with 14 offices in British Columbia and Saskatchewan. These locations offer a broad variety of property and casualty insurance services, including private auto insurance and government auto in B.C., Saskatchewan and Manitoba, home and farm insurance, business and specialty insurance, life products and in many locations, investment and financial services.

We also operate other businesses that complement the products and services offered by the Network. We own Bank West, a Canadian chartered bank, which commenced operations in January 2003. Bank West provides GICs, loans, mortgages, insurance policy premium financing and other banking products, which are sold through the Network as well as through third-party distribution channels. We also own Western Life, a federally regulated insurance company that provides proprietary life and health insurance products to individuals and small to medium-sized businesses in Canada. We also have a 35.7% equity interest in Jennings, a full service investment dealer headquartered in Calgary, Alberta.

In addition, we have a 25% initial investment in Hayhurst Elias Dudek Inc. ("HED"), the largest insurance broker/administrator in Manitoba whose operations are complementary to the Network's. HED's head office and the majority of the employees are located in Winnipeg, with additional offices in Toronto, Montreal and Halifax. HED offers three core product segments: i) Commercial Property & Casualty; ii) Life and Health; and iii) Pet Health Insurance through its subsidiary SecuriCan General Insurance Company, the leading provider of pet insurance in Canada, sold under the Petplan brand.

## Principal Markets

We have become specialists over the past 10 years of operation in providing financial services to customers in smaller communities primarily in Western Canada with similar demographics and economic drivers. This focus on what has been a dynamic region has helped drive our success.

The tables below outline the location by province of the communities where the Network currently has a presence ("Existing Communities") and the communities we have targeted for future expansion over the next five years ("Target Communities"). We estimate that there are approximately 400 brokers in these Target Communities. See "Description of Our Business — Broker Acquisition and Growth Strategy" and "Risk Factors".

<u>Existing Communities by Province</u>		<u>Target Communities by Province</u>	
<u>Province</u>	<u># of Communities<sup>(1)(2)</sup></u>	<u>Province</u>	<u># of Communities</u>
British Columbia.....	17	British Columbia.....	49
Alberta .....	32	Alberta .....	53
Saskatchewan.....	10	Saskatchewan.....	24
Manitoba .....	<u>2</u>	Manitoba .....	<u>20</u>
<b>Total .....</b>	<b>61</b>	<b>Total .....</b>	<b>146</b>

Source: Company data and Statistics Canada.

### **Note:**

- (1) We have 74 branch offices, including multiple branch offices in the communities of Kelowna and Prince George in British Columbia, Lloydminster and Medicine Hat in Alberta and Brandon in Manitoba.
- (2) We also have strategic investments through our affiliated offices in an additional 20 locations serving 15 communities in British Columbia, Saskatchewan, Manitoba, Ontario, Quebec and Nova Scotia which are not reflected in the chart.

We believe our focus on small communities in Western Canada, with similar demographics and economic drivers, provides certain advantages enabling us to:

- efficiently integrate brokers that are located in communities similar to our Existing Communities, minimize integration difficulties and maximize synergies;
- tailor our product and service offerings and expertise to industries prevalent in our Existing Communities (e.g. agriculture, energy and natural resources); and
- emphasize our brand and marketing efforts with a strong regional and rural theme, which we believe is attractive to our customers.

## Our Operating Divisions

### **The Network**

Through the Network's 74 offices in 61 communities we serve a base of over 350,000 customers. Through the Network, we also sell a broad range of complementary financial products and services, including banking, life insurance and investment products from a large number of financial institutions, including Bank West and Western Life.

The Network distributes the vast majority of its products through its branch offices where new business is derived from customer referrals, walk-in customers and telephone inquiries. The Network also utilizes direct sales techniques such as targeted mail and telephone campaigns to distribute its products.

The Network's revenue for the year ended December 31, 2006 represented 56.5% of our total revenue. Of the Network's revenue over this same period, 97.8% originated from sales of P&C insurance products and government automobile coverage. The remainder was from sales of banking products, life insurance and other products and services.

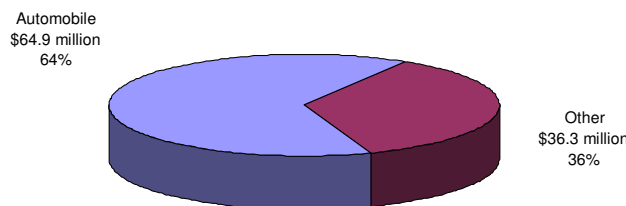
The Network's revenue from the sale of P&C insurance products is derived from commission structures similar to those of the rest of the industry. These include basic commissions and contingent commissions. The contingent commissions earned by the Network in 2006 were approximately 1.6% of premiums sold, which is in-line with our belief of the industry average of 1.0-2.0%. See "Industry Overview".

### ***P&C Insurance Products and Services***

The Network's P&C insurance premium sales for the year ended December 31, 2006 were \$234.8 million, with personal insurance representing 43.1% and commercial insurance representing 56.9% of such premiums.

#### ***Personal Insurance***

The Network offers a wide selection of personal insurance products from a large number of regional and international P&C insurers. The following chart outlines that for the year ended December 31, 2006, the Network sold \$101.2 million of personal insurance premiums with personal automobile insurance accounting for 64.9% of the total.



#### **Notes:**

- (1) For the year ended December 31, 2006.
- (2) Other personal insurance sold includes home, recreational vehicles, travel, excess medical and personal umbrella insurance.

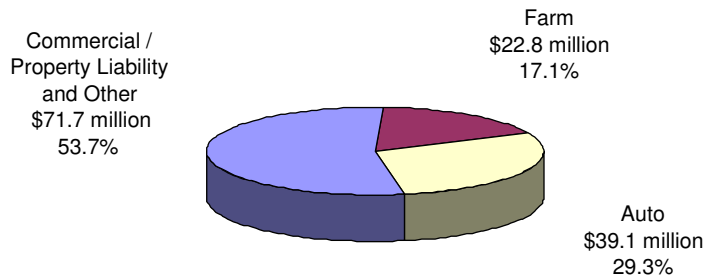
#### ***Commercial Insurance***

The Network offers various types of commercial insurance for small and medium-sized businesses, farms and certain government agencies. For the year ended December 31, 2006, the Network sold \$133.6 million of commercial insurance premiums. For small businesses and farms, insurance policies are "packaged" in one comprehensive policy and include coverages for liability, property and other contingencies. For those with more complicated insurance needs, coverages are arranged separately according to the needs and risk profile of the particular business.

The Network also operates an internal special risk division which deals with specialized P&C insurance providers to assist in placing P&C insurance products for complex accounts or for customers requiring coverage for extraordinary risks.

Several of the Network's branch offices have their own specialized policies and expertise in areas such as: long haul transportation, oil and gas services, agribusiness, assisted living facilities, day cares, schools and others. This specialized expertise is shared throughout the Network's branch offices to enhance its ability to service its customers in all of our markets.

The following chart outlines the Network's product mix of commercial insurance for the year ended December 31, 2006.



**Notes:**

- (1) For the year ended December 31, 2006.
- (2) Other commercial insurance sold includes building, contents, business interruption, general liability, crime, professional liability and builders' risk insurance.

The Network places commercial insurance with a large number of P&C insurers, including regional, national and international insurers. In addition to selling mainstream policies, the Network has arrangements with certain P&C insurers to add unique features which provide its commercial customers with increased coverages for no additional charge.

*Our Guarantee of Value*

In addition to providing the Network's customers with competitively priced products, we believe in providing the Network's customers with superior service. Consistent with this belief and in conjunction with our corporate strategy to provide industry-leading service in our core business, we have developed the "Guarantee of Value". The "Guarantee of Value" represents our view of the ideal qualities that P&C insurance brokers should possess and the standard of service they should provide to their customers. Our "Guarantee of Value" is a set of measurable service promises, which include a highly educated insurance staff who undertake to review and, if necessary, revise each insurance policy; a wide selection of high quality and competitively-priced products; regular, consistent attention; and a fairness guarantee that establishes a protocol for handling disputed claims. We believe the Network provides leadership in the P&C brokerage industry through the "Guarantee of Value" which directly benefits our customers.

***Non-P&C Insurance Products***

Over the last four years, we have increased our emphasis on expanding the Network's product and service offering beyond its core P&C insurance products. These products and services include agency banking (deposits, loans and mortgages), life insurance and employer group health and life. By leveraging the

Network and its core P&C insurance customer base through cross-selling these complementary financial products and services, we are able to take advantage of an additional opportunity for growth.

Non-P&C insurance products represented 2.2% of the Network's revenues for the year ended December 31, 2006. Although the number of non-P&C insurance products sold has been increasing over the years, these products continue to account for a disproportionately smaller percentage of the Network's total revenues because the Network earns, on average, higher commissions on the sale of P&C insurance products. Additionally, the Network's sales of our "house brand" non-P&C insurance products, such as those from Bank West and Western Life, provide both a distribution fee to the Network and additional revenues to us as a whole, and therefore have a greater impact on our total revenues as opposed to the Network's revenues alone. See "Description of Our Business - Bank West" and "- Western Life".

#### *Agency Banking Products*

The Network offers deposit products (GICs, daily interest savings accounts and term deposits) for a wide range of banks (including Bank West), credit unions, trust companies and other third-party financial institutions. In addition, the Network markets loans and mortgages for Bank West on a referral basis. Although agency banking products sold by the Network have not contributed significant revenues to our operations to date, we intend to continue to expand this aspect of our business by cross-selling these products as well as our other financial products to the Network's customers.

The Network acts as a referral point for Bank West mortgages and loans. Customer inquiries are generated through direct mail and database marketing campaigns. Rate quotes and application information on these mortgages and loans can be obtained at each Network branch office and prospects are referred directly to Bank West's office in High River, Alberta for follow up by a loans officer. The Network also acts as an agent for Bank West in the provision of insurance policy premium financing, which enables purchasers of insurance policies to make monthly premium payments.

#### *Life Insurance Products*

The Network sells life insurance products to existing customers of the Network through its licensed life insurance sales force (consisting of 23 professionals). Life insurance products include financial protection products such as term life, critical illness and disability insurance for individuals and groups, as well as products that have an added investment component such as universal life policies and segregated funds. The Network currently has contracts to sell products for a small number of life insurance companies and markets these life insurance products to existing customers through database marketing programs. Since acquiring Western Life we have expanded the life and health insurance products the Network offers to include the products of Western Life. See "Description of Our Business - Western Life".

#### ***Broker Acquisition and Growth Strategy***

We believe that consolidation is the most efficient means of building a network in the fragmented P&C insurance brokerage industry in Canada, as it creates economies of scale, increases buying power, facilitates integration of new technology and fosters an overall pooling of resources. Accordingly, we actively search for brokers primarily in smaller communities in Western Canada to which our management, financial resources, industry experience and marketing skills can be applied in order to enhance the profitability of the acquired business. Within these markets, we tend to acquire the leading broker in the service area. These brokers are then fully integrated into our management, financial, administrative and electronic communications systems, thereby aligning their operations with the Network's and positioning them for growth. We have demonstrated our success in integrating new brokers into the Network by growing the revenues of each of the brokers we have acquired.

We have identified 146 Target Communities in Western Canada for expansion over the next five years and we estimate that there are approximately 400 brokers in these Target Communities. We look for some or all of the following criteria in brokers we seek to acquire:

- leading market share and strong competitive position;
- growth potential;
- sound financial results;
- economically favourable acquisition terms;
- ease of integration of our product offering;
- balanced mix between personal and commercial P&C insurance; and
- compatible corporate culture.

We negotiate our acquisitions on a case-by-case basis. In most cases, vendors are paid a combination of cash and Common Shares. Typically, a portion of the Common Shares that are used as consideration are placed in escrow and released to the vendor based on either the passage of time or the satisfaction of certain performance criteria (such as a threshold of cash flow), which provide incentives to the vendor to participate in the successful transition of the business. See "Description of Our Business - Principal Markets".

We are actively looking for brokers to acquire. Any potential acquisitions could individually, or in the aggregate, be material to us. As of the date hereof, we have not reached agreement on the price or terms of any potential material acquisitions. We cannot predict whether any current or future opportunities will result in one or more material acquisitions.

## **Bank West**

### ***General***

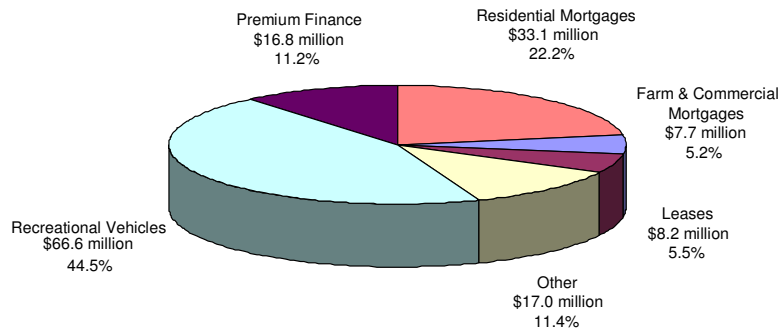
Bank West represents our entry into the manufacturing of products, which are sold through the Network as well as through third-party distribution channels. In December 2002, Bank West became the first start-up bank to receive a federal charter under new ownership rules following amendments to the *Bank Act* (Canada) (the "Bank Act") in 2001. Bank West commenced operations in January 2003 and provides GICs, loans, mortgages, insurance policy premium financing and other banking products. Bank West currently employs 19 people in its office in High River, Alberta.

### ***Products and Services***

Bank West offers both deposit and loan products to its customers. Bank West's deposit products consist of GICs with terms of 30 days to five years. The total amount of these deposit products has grown to \$146.9 million as of December 31, 2006.

Bank West's loan products include residential, farm and commercial mortgages, insurance policy premium financing, personal loans and commercial equipment financing. Bank West also has a dealer referral program to finance automobiles, recreational vehicles and boats. Bank West's loan portfolio has grown to \$149.4 million as of December 31, 2006.

As shown in the chart below, recreational vehicles, premium finance and residential mortgage comprise the majority of Bank West's loan portfolio as of December 31, 2006.



**Note:**

(1) As at December 31, 2006.

***Distribution***

Bank West's products are distributed by third-party distribution channels, including deposit, mortgage and loan brokers and dealers, as well as through the Network's branch offices. To date, distribution of Bank West products by the Network, particularly loan products, has been a component of Bank West's growth. As such, the Network represented \$25.0 million or 16.7% of Bank West's total loans distributed as of December 31, 2006 with the remaining \$124.4 million being sold or distributed directly by Bank West and/or through third-party distribution channels. The Network also distributed approximately \$7.9 million or 5.4% of Bank West's outstanding GICs as at December 31, 2006, with the remaining 94.6%, or \$141.5 million, being distributed through third-party distribution channels.

***Lending and Investment Policies***

Bank West's lending policies, standards and procedures recognize the requirements of the Bank Act, as well as other regulatory requirements such as those issued by the Office of the Superintendent of Financial Institutions ("OSFI") and the Canada Deposit Insurance Corporation. The board of directors of Bank West are responsible for ensuring that proper policies and procedures are in place and the management and employees of Bank West are responsible to implement such policies and procedures to ensure that quality loans are granted. Credit risk with respect to mortgages and loans is mitigated through conservative underwriting policies and charges against real property and cash holdbacks that reduce Bank West's risk exposure on those loans. Certain of the residential mortgages are insured through Canada Mortgage and Housing Corporation.

Securities portfolio management at Bank West is defined as the overall conduct and control of investment activity and mitigation of exposure of risk. Bank West's board of directors, through the Audit and Risk Committee, delegates operational responsibility for investing surplus and capital funds to the Asset/Liability Management Committee within the established policies. Policies are designed to minimize portfolio risks with credit, liquidity, interest rate, market, solvency and foreign exchange.

***Acquisition and Growth Strategy***

Bank West's growth strategy is to continue to expand and develop its market penetration among the Network's customers. In addition, Bank West will continue to develop relationships with third-party distribution channels, such as deposit, mortgage and loan brokers and dealers in Western Canada.

Bank West is actively looking for acquisition opportunities of portfolios of loans that fit with its product and geographic emphasis. We will evaluate potential direct or indirect acquisitions of other financial institutions intended to increase the size and scope of Bank West's operations. Any potential acquisitions could individually, or in aggregate, be material to us. As of the date hereof, we have not reached agreement on the price or terms of any potential material acquisitions. We cannot predict whether any current or future opportunities will result in one or more material acquisitions. While Bank West has grown its assets since inception, it is still in the early stages of its development. However, in 2006, Bank West's pre-tax earnings increased by approximately \$1.0 million over 2005. We expect Bank West's performance to continue to improve over the coming year.

## **Western Life**

### ***General***

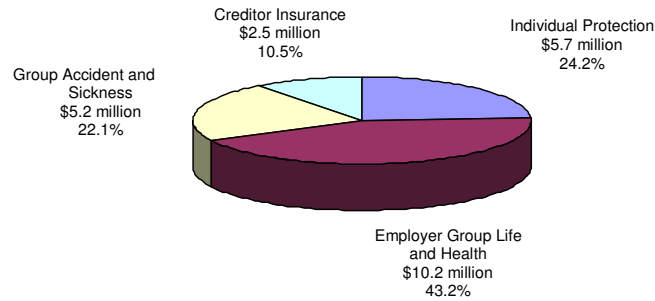
On May 26, 2004, we entered into a share purchase and sale agreement (the "Share Purchase Agreement") with Federated Holdings Company of Canada ("Federated Holdings"), Federated Life and Federated Insurance Company of Canada ("Federated Insurance") to purchase all of the issued and outstanding shares of Western Life for a purchase price of \$20.0 million. We completed our acquisition of Western Life on February 28, 2005.

Licensed in all provinces and territories in Canada, Western Life offers life and health insurance products to small to medium-sized commercial businesses and individuals. Western Life is an established participant in the Canadian life insurance and group health markets, with approximately 44 years experience and 18 years experience, respectively. Western Life serves policyholders, representing in excess of 19,000 individuals throughout Canada.

Western Life, which had \$23.6 million in net premium revenues and \$26.4 million in total revenues for the year ended December 31, 2005, provides life and health insurance products to individuals and small to medium-sized businesses throughout Canada, with a focus on Western Canada and Ontario. The acquisition of Western Life represents our second foray into the manufacturing of products, which are sold through the Network as well as third-party distribution channels. As of the date hereof, Western Life has 41 employees serving policyholders and insuring in excess of 19,000 individuals across Canada. Western Life's products are sold through: (i) approximately 95 captive agents, employed by Federated Insurance, who sell Western Life's life and health insurance products exclusively pursuant to a Strategic Support and Marketing Agreement between Federated Insurance and Western Life (the "Support Agreement"); (ii) 20 life Managing General Agents, representing approximately 1,600 life insurance brokers; (iii) 12 Third Party Administrators who distribute group health and specialty accident and sickness products; and (iv) 74 of the Network's branch offices. Nearly all of Western Life's employer group life and health premiums are sold to businesses with between four and 50 employees.

### ***Products***

Western Life's product line includes employer group life and health products, individual protection products, group accident and sickness products and creditor insurance products. The chart below depicts Western Life's net premium revenues for each of these product categories for the year ended December 31, 2006.



**Note:**

(1) For the year ended December 31, 2006.

*Employer Group Life and Health Products*

This product group includes the common form of employee benefit insurance plans offered in many businesses in Canada today. Specific coverages within the group life and health insurance product line include group life, dependent life, out-of-country emergency medical, extended health, dental, and short and long-term disability.

Employer group health insurance plans are a common condition of employment with a specific employer and terminate upon cessation of employment. Employers purchasing these products negotiate the policy coverage with Western Life. The cost of this coverage is based on the age and gender demographics of the entire employee group, and is subject to an annual renewal rate change depending on claims experience, inflation and usage trend factors. Western Life has a comprehensive employee benefits product offering that targets small and medium-sized business employee groups. Western Life outsources the core administration of this line to Green Shield Canada ("Green Shield"), a leading provider of health and dental insurance services in Canada.

*Individual Protection Products*

Individual protection products include term life insurance, universal life insurance, disability income insurance and critical illness insurance. Term life insurance is often used for temporary needs such as until a mortgage is repaid or children are grown and no longer dependent. This type of policy pays a benefit if the insured dies during the policy term. Universal life insurance provides flexibility in premiums and face amounts and can be customized. It includes life insurance protection and allows for the accumulation of tax deferred investment growth. Disability income insurance provides continued income to individuals who become disabled due to illness or accident. Critical illness insurance provides lump sum cash benefits to insured individuals who have been diagnosed with one of a number of critical illnesses specified in the policy.

*Group Accident and Sickness Products*

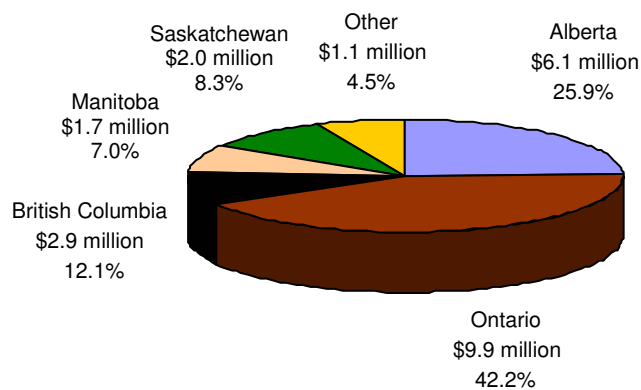
This product group includes accidental death and dismemberment and critical illness insurance. These products are provided on a group basis, rather than on an individual basis and, therefore, the cost of the coverage is a function of the risk associated with the group and subject to change annually with claims experience.

### *Creditor Insurance Products*

Creditor insurance products include life insurance, disability insurance and critical illness insurance marketed to insured debtors to reduce the credit risk associated with events such as death, disability or critical illness.

### *Principal Markets*

Western Life is licensed to carry on business in all provinces and territories in Canada, but is focused predominantly on Western Canada and Ontario. As detailed in the chart below, approximately 95.5% of Western Life's net premium revenues were generated in Western Canada and Ontario during the year ended December 31, 2006 with Western Canada and Ontario representing 53.3% and 42.2%, respectively.



**Notes:**

- (1) For the year ended December 31, 2006.
- (2) Other includes Quebec, New Brunswick, Nova Scotia, Newfoundland and Prince Edward Island.

### *Distribution*

Western Life establishes commission rates for the sale of its insurance products for each product category and type of product as part of its pricing decisions. The commission rate for the first year of a life or health insurance policy is often substantially higher than the commission rate for renewals. Western Life's commissions often include payments to both the agent who sold the policy and to a related entity such as the Managing General Agent or broker acting as an intermediary. Western Life does not pay contingent commissions to any of its distributors, including its captive agents. The commission rates Western Life pays on the sale of its life and health insurance products do not vary materially among the different distribution channels and are within what we believe to be industry standards. Western Life strives to offer competitive commission rates in order to attract and retain its distribution relationships, while maintaining the profit margins of its insurance products.

### *Captive Agents*

Western Life's products are distributed by approximately 95 captive agents, employed by Federated Insurance. These agents are dual-licensed (life/health and P&C insurance) and sell life and health insurance products exclusively for Western Life and P&C insurance products exclusively for Federated Insurance. These captive agents are compensated solely on a commission basis for sales of Western Life

insurance products. These traveling agents operate throughout Canada, with a focus on Western Canada and Ontario. These captive agents, who are employees of Federated Insurance sell life and health insurance products for Western Life based on their commission schedule in force prior to the Acquisition pursuant to the Support Agreement. See "Description of Our Business - Western Life - Share Purchase Agreement".

#### *Broker Distribution*

Western Life entered the broker market in 2000 with the introduction of its Internet-based insurance application program called @pprove™. @pprove™ is an e-commerce support tool which provides a completely electronic process for submitting and managing an insurance application. Agents selling Western Life products are contracted through life Managing General Agents. As of December 31, 2006, the number of authorized agents using @pprove™, excluding the approximately 95 captive agents, was 2,517.

#### *Third Party Administrators*

Western Life has developed specialty products such as accidental death and small value critical illness insurance for distribution by certain Third Party Administrators. These Third Party Administrators develop market opportunities for Western Life's insurance products, coordinate and execute the selling cycle, provide sales administration for these products and provide policy administration and client relationship management services for Western Life while the insurance policies remain in force.

#### *The Network*

Starting in 2005, the Network began offering Western Life's products in the majority of its branch offices and by the end of 2005 Western Life's products were available in all of the Network's branch offices.

#### ***Pricing and Underwriting Liability***

Western Life utilizes actuarial analysis on mortality and morbidity as well as current industry data to establish product pricing parameters. Profit margin targets are verified through financial modeling that employs industry standard projection tools. Western Life verifies its product pricing assumptions through its reinsurance partners as part of its reinsurance treaty negotiations.

Western Life determines underwriting criteria as part of its product pricing analysis before an insurance product is marketed. The underwriting criteria and procedures are developed by Western Life's senior underwriters, each with over 20 years experience, in conjunction with the reinsurance companies that share the risk with Western Life. Each reinsurance company publishes its own underwriting manual which becomes the model for risk acceptance that is followed by Western Life's underwriting personnel for each product underwritten. Once the underwriting criteria have been established, all distribution channel participants are educated in the underwriting procedures to be used in assessing an application for insurance. Underwriting audits are performed annually by Western Life's reinsurance partners to ensure compliance with the established underwriting criteria.

Western Life typically limits its single loss exposure to no more than \$100,000 through the use of reinsurance treaties placed among leading reinsurance carriers. When launching new products, 75% to 90% of risk is ceded to experienced reinsurance partners until claims experience over time validates Western Life's pricing assumptions.

Western Life focuses on minimizing the credit risk associated with its reinsurance agreements by partnering with reinsurers with strong credit ratings. Western Life regularly evaluates the financial condition of its reinsurers, monitors the concentration of credit risk and, where possible, obtains security to support the reinsurance obligations. Accordingly, Western Life purchases 95% of its reinsurance from three highly-rated reinsurance companies, which are all rated "A" or better by A.M. Best.

### ***Claims Management***

Western Life's claims management objective is to provide prompt and fair claims adjudication to its customers, while controlling fraudulent claims and settlement expenses. Western Life utilizes an experienced internal claims staff, which is supported, as required, by third parties such as reinsurance partners, medical experts, independent investigators and industry consultants.

Immediately upon notification of a claim event, Western Life establishes actuarial reserves using industry-standard actuarial procedures. Reserves are also established in consultation with Western Life's reinsurance partners' own reserve procedures to ensure a proper matching of reserves for the entire claim amount. Western Life establishes "incurred but not reported" reserves on a conservative basis in accordance with actuarial data and reviews its reserves after analyzing actual experience and related premium volumes on a quarterly basis. Western Life monitors adherence to its claims policy and procedures on a weekly basis and external claims audits are performed by our reinsurance partners annually.

Western Life's employer group health product line, which includes both health and dental claims adjudication, is outsourced to Green Shield. Through Green Shield's technology, Western Life is provided with point-of-service electronic claims adjudication services and receives the benefit of a robust data processing service that monitors and manages all aspects of this high volume claims service.

### ***Financial Strength***

Western Life's financial strength rating, as quoted by A.M. Best, is "B++" with a stable outlook. According to A.M. Best, this rating is based on a comprehensive quantitative and qualitative evaluation of a company's balance sheet strength, operation performance and business profile. The "B++" rating is described as a "very good" rating and is assigned to companies that A.M. Best believes have a good ability to meet their ongoing obligations to policyholders. The stable outlook indicates a company is experiencing stable financial and market trends and there is a low likelihood its rating will change in the near term. A.M. Best affirmed Western Life's rating of B++ with a stable outlook on May 10, 2006.

Our issuer long term credit rating, as quoted by A.M. Best, is "bbb" with a stable outlook. According to A.M. Best, a long term credit rating is an opinion as to the ability of the rated entity to meet its senior obligations. These ratings are assigned to insurance companies, holding companies or other legal entities authorized to issue financial obligations. Ratings may be enhanced with a plus (+) or minus (-) sign to indicate whether credit quality is near the top or bottom of a category. A.M. Best issued our long term credit rating of bbb with a stable outlook on May 10, 2006.

A security or credit rating is not a recommendation to buy, sell or hold securities and may be subject to revision at any time by the rating organization.

### ***Investment Management***

Western Life's investment portfolio, which was \$57.2 million as of December 31, 2006, is currently managed by two investment managers, QVGD Investors Inc. and Baker Gilmore & Associates Inc., each

of which is an experienced asset management company. Western Life's investment guidelines stress preservation of capital, market liquidity and diversification of risk and are based on a long-term value-oriented style. As at December 31, 2006, Western Life's investment portfolio consisted of approximately 8.2% cash and short-term investments, 80.7% fixed income securities and 11.1% of pooled funds and equities.

### ***Share Purchase Agreement***

Pursuant to the terms of the Share Purchase Agreement we acquired all of the shares of Western Life for a purchase price of \$20.0 million, payable in cash. The Share Purchase Agreement contains representations and warranties which are typical for transactions of this type, the majority of which survive for two years after closing of the Acquisition. The Share Purchase Agreement also contains covenants typical for transactions of this type. The Share Purchase Agreement contains mutual indemnification provisions for material breaches of representations and warranties or failure to perform any material covenants or obligations.

As a condition of the Share Purchase Agreement, we entered into certain ancillary agreements such as the Support Agreement and various non-competition agreements. The Support Agreement provides us with access to Federated Insurance's P&C insurance customers for the sale of life and health insurance products. Federated Insurance's approximately 95 captive agents sell Western Life products under the "Western Life" banner on their existing commission schedule. The Support Agreement is designed to assist us with the transition of the Western Life business and to enable us to grow and develop the sales of its product lines through Federated Insurance's established network and through the Network. The Support Agreement has a term of three years with automatic renewals for subsequent one-year terms thereafter unless cancelled by either party on 180 days notice after expiry of the initial term.

The various non-competition agreements provide that Federated Insurance and Western Life will not compete with each other in their respective product lines during the term of the Support Agreement and for five years thereafter. In addition, Northbridge Financial Corporation, the parent of Federated Insurance agreed, subject to certain exceptions, not to carry on any life and health insurance business for a period of five years from closing. Finally, for the term of the Support Agreement, and three years thereafter, we agreed not to solicit or accept any commercial P&C insurance business from a person who is both a customer of Western Life and Federated Insurance until 12 months expire since the customer was last a Federated Insurance customer. To the extent that a person is a commercial P&C insurance customer of Federated Insurance only, for a period of 12 months following the date the customer was last a Federated Insurance customer, we agreed not to solicit, but may accept, such business from that customer.

### **Investment Businesses**

#### ***The Western Mutual Fund Company Ltd.***

In April 2004, WMFC commenced business as a mutual fund dealer providing third party mutual funds and mutual fund services, including supervisory and processing services, to the Network. These services were previously performed by third parties unrelated to us. We established WMFC to allow the Network to control its customer service process and have the "Western" brand linked to these services. However, in 2005 WMFC experienced declining sales and increased costs and by the third quarter this segment of our business was significantly below budget. Believing that products and services in this area were not capturing customer interest and that a turnaround seemed unlikely, we made the business decision at the end of 2005 to cease operations of WMFC and transfer our clients' mutual fund accounts that were being managed by WMFC to Jennings.

## ***Jennings Capital Inc.***

We have a 35.7% equity interest in Jennings, a full-service investment dealer with offices in Calgary, Toronto and Vancouver. Jennings is a member of the Investment Dealers Association ("IDA"), the primary regulatory body for investment banking and brokerage firms in Canada. Our equity interest in Jennings contributed \$1.5 million to our net income for the year ended December 31, 2006.

We view the ownership of Jennings as strategically important for building our long-term capability of selling investment products to customers of the Network and Western Life.

## **Other Service Businesses**

Integrated with the Network's operations are certain specialty services provided at various locations where, through opportunity or acquisition legacy we have been granted a concession to provide these services. We have established travel services as a secondary focus in five Alberta communities. In addition, we also offer government registries services in other Network branch offices. We continue to advertise and market these services within the Network and, where practical, share staff and premises to save costs and maximize benefits. These businesses have not contributed significant revenues to our operations to date and we do not expect them to do so in the short to medium-term.

## **Employees**

As of the date hereof, we employ approximately 780 people on a full-time and part-time basis, approximately 610 of whom are employed in the Network's branch offices, 75 of whom are employed in our head office and the balance of whom are employed in Bank West, Western Life and our other service businesses. With the exception of approximately 18 employees who are compensated on a commission basis, all of the Network's employees are paid a salary. None of our employees are represented by a union and we have never experienced a work stoppage. We believe our relationship with our employees is good.

## **Facilities**

Our head office is located at 1010 - 24 Street West, High River, Alberta, T1V 2A7. We have 74 branch office locations throughout Western Canada. In addition, we have strategic investments in two regional brokerages and an independent broker/administrator with an aggregate of 20 affiliated offices in the Provinces of British Columbia, Saskatchewan, Manitoba, Ontario, Quebec and Nova Scotia. Bank West's and Western Life's head offices are located in High River, Alberta. We own 11 Network branch offices. The remainder of our facilities are leased from third parties with terms ranging from one to ten years. The size of the Network's branch office locations range from 200 to 5,000 square feet. Our aggregate rent expense for our facilities was approximately \$2.2 million for the year ended December 31, 2006. We believe our facilities are adequate for our business and that our leases and mortgages are in good standing.

## **Information Technology**

Our information technology group provides computer, network, telecommunication and business support for the Network, Bank West, Western Life, Jennings and our head office. These services are provided in a secure and cost effective manner. Our various business units are connected through a secured wide area network. Our core information technology assets are located in a secured, environmentally-controlled data centre that provides both connectivity and power source redundancy. The group's philosophy is to implement only proven applications and technologies based on the requirements of our various business units. This approach provides us with standard information technology processes and the infrastructure to enable the growth of our business now and in the future.

## **Competition**

We face competition from the estimated 800 independent brokers delivering P&C and life insurance products in smaller communities in Western Canada. We also face competition from certain P&C insurance companies, including some owned by Canadian chartered banks, who distribute their products directly to consumers. In addition, Canadian chartered banks pose a potential competitive threat as they are attempting to obtain the legal right to sell insurance at their branches to compete directly with insurance companies and brokers. There are also a number of companies operating in the P&C insurance brokerage industry in Canada that compete with us, including Hub International Limited, Anthony Clark International Insurance Brokers Ltd. and Canada Brokerlink Inc. We also face competition from banks, financial planners and other financial service providers in the sale of non-P&C insurance products. In general, we also face future competition from financial institutions who are delivering or preparing to deliver financial services and insurance products and services by electronic means, most notably through the Internet. Frequently, competition is based on pricing, product selection and the ability to provide value added services to customers, including highly personalized service and local decision making.

The insurance business we engage in through Western Life is also highly competitive. Western Life's products compete not only with those offered by other insurers, but in many cases with those offered by mutual funds, banks, and other providers. Insurers compete on the basis of pricing and terms, service provided to distribution channels and policyholders and claims paying financial strength ratings.

## **DIVIDENDS**

Since incorporation, we have not declared or paid any dividends on our outstanding Common Shares. However, on October 12, 2006, our board of directors approved a change to our dividend policy such that, upon satisfaction of certain conditions, we plan to commence payment of a quarterly dividend on July 1, 2007. The payment of dividends and the amount of such dividends will be subject to the discretion of our board of directors and will depend on, among other things, our financial condition, general business conditions and other factors that our board of directors may in the future consider to be relevant. We expect that such dividends will be paid to shareholders quarterly on each of January 1, April 1, July 1 and October 1.

On December 12, 2006, our board of directors declared a dividend of \$3.4397 per share on the First Preferred Shares, Series Two for the six months ended December 31, 2006 to the shareholders of record of such shares at the close of business on December 19, 2006.

## **PRIOR SALES**

Since January 1, 2006, we have issued the following securities that are not listed or quoted on a marketplace:

<u>Date</u>	<u>Number of Securities</u>	<u>Issue Price Per Security</u>	<u>Aggregate Issue Price</u>
June 29, 2006.....	150,000 <sup>(1)</sup>	\$100.00	\$15,000,000

**Note:**

(1) First Preferred Shares, Series Two. See "Capital Structure - First Preferred Shares, Series Two".

## **ESCROWED SECURITIES**

As part of our acquisition strategy, we often pay a portion of the purchase price in Common Shares which are subject to escrow until either or both of certain financial tests are met or a certain amount of time has elapsed. This provides the vendor with an incentive to cooperate in the successful completion of an

acquisition. The number of securities of each of our classes of securities currently held, to the best of our management's knowledge, in escrow and the percentage that number represents of the outstanding securities of that class, are as follows:

<u>Designation of Class</u>	<u>Number of Securities Held in Escrow</u>	<u>Type of Escrow</u>	<u>Percentage of Class</u>
Common Shares .....	64,690 <sup>(1)</sup>	performance <sup>(3)</sup>	<1.0%
Common Shares .....	40,650 <sup>(2)</sup>	Performance <sup>(4)</sup>	<1.0%
Common Shares .....	138,415 <sup>(2)</sup>	performance <sup>(5)</sup>	<1.0%
Common Shares .....	65,447 <sup>(2)</sup>	Time <sup>(6)</sup>	<1.0%
Common Shares .....	128,074 <sup>(2)</sup>	performance <sup>(7)</sup>	<1.0%
Common Shares .....	35,266 <sup>(2)</sup>	performance <sup>(8)</sup>	<1.0%

**Notes:**

- (1) The escrow agent for these securities is Meighen, Haddad & Co., Barristers & Solicitors.
- (2) The escrow agent for these securities is L.M. Gordon Law Office.
- (3) One Common Share released for each \$7.54 cash flow produced by certain assets.
- (4) One Common Share released for each \$4.92 cash flow produced by certain assets.
- (5) One Common Share released for each \$5.90 cash flow produced by certain assets.
- (6) One third of these Common Shares will be released annually commencing December 1, 2006.
- (7) One Common Share released for each \$5.85 cash flow produced by certain assets.
- (8) One Common Share released for each \$7.65 cash flow produced by certain assets.

### MARKET FOR SECURITIES

The Common Shares of Western are, and the 9% Debentures were in 2006, listed on the TSX. The following table summarizes the trading activities of our listed securities for the year ended December 31, 2006 on the TSX:

<b>Common Shares: WES</b>	<b>High</b>	<b>Low</b>	<b>Volume</b>
January	2.79	2.55	1053332
February	2.80	2.60	1032478
March	2.80	2.66	1188140
April	3.49	2.75	1601197
May	3.25	2.90	1186799
June	3.14	2.75	1493475
July	3.04	2.95	861359
August	3.45	2.97	906867
September	3.35	3.02	350629
October	3.95	3.30	1016821
November	3.91	3.47	1817604
December	4.24	3.53	1278420
<b>2006</b>			

<b>Debentures: WES.DB.A</b>	<b>High</b>	<b>Low</b>	<b>Volume</b>
January	117.00	110.25	1320
February	112.00	108.50	350
March	112.00	107.50	1227
April	136.00	112.00	2280
May	130.00	118.00	11707
June <sup>(1)</sup>	120.00	107.01	6330
<b>2006</b>			

**Note:**

- (1) These Debentures were redeemed in June of 2006 in exchange for the issuance of Common Shares.

## DIRECTORS AND EXECUTIVE OFFICERS

The following table sets out as at the date hereof, the names and locations of residence, positions held with us and principal occupations within the last five years of our directors and executive officers. The table also sets out the date each director first became one of our directors. As of the date hereof, our directors and executive officers as a group owned, directly or indirectly, 2,959,493 Common Shares representing approximately 6.7% of our issued and outstanding Common Shares.

<u>Name and Province/State and Country of Residence</u>	<u>Position</u>	<u>Principal Occupation</u>	<u>Director Since</u>
Scott A. Tannas..... Alberta, Canada	President, Chief Executive Officer and Director	President and Chief Executive Officer since our inception in 1996.	January 19, 1996
Robert G. Jennings..... Alberta, Canada	Director	Chairman of Jennings (an investment dealer) since August 1993. Senior Vice-President and Director of Midland Walwyn Capital Inc. (an investment bank) from August 1988 to August 1993.	August 30, 1996
J. Gregg Speirs <sup>(1)</sup> ..... Alberta, Canada	Director	Presently retired. Formerly, Director of Administration at Bennett Jones Verchere (a law firm) from January 1993 to May 1996. Senior Vice President of Reed Stenhouse (an insurance brokerage and risk manager) from 1986 to 1992 and Assistant Manager at Reed Stenhouse from 1989 to 1992.	October 21, 1996
Gabor Jellinek <sup>(2)</sup> ..... Quebec, Canada	Director	President of G.J. Holdings Inc. (a private investment company) From 1987 to 1999, was Vice President and Officer of The Seagram Company Ltd. (a distilling company), and from 1991 to 1999, was Chairman of Joseph E. Seagram & Sons Limited (a distilling company).	February 1, 2000
Phillip L. Webster <sup>(1)</sup> ..... Quebec, Canada	Director	President of Imperial Windsor Group since 1998 and President of Emster Holdings Inc. since 1982 (both are private investment holding companies).	February 1, 2000
Tom C. Dutton <sup>(3)</sup> ..... Alberta, Canada	Executive Vice-President and Director	Executive Vice-President since November 2004. President and Chief Operating Officer of the Network from September 2001 to 2004. President of Independent Agencies (1969) Ltd. ("Independent Agencies"), one of our subsidiaries, from January 1999 to September 2001. Prior to our acquisition, was an owner of Independent Agencies (an insurance brokerage).	September 1, 2001

<u>Name and Province/State and Country of Residence</u>	<u>Position</u>	<u>Principal Occupation</u>	<u>Director Since</u>
Jim Dinning <sup>(1)(2)</sup> ..... Alberta, Canada	Chairman and Director	Chairman of the Board of Directors of the Corporation since September 2004. From August 1, 1997 to December 31, 2004 Executive Vice President of TransAlta Corporation (a utility company).	November 20, 2002
Diane Brickner <sup>(1)</sup> ..... Alberta, Canada	Director	President and Chief Executive Officer of Peace Hills Insurance since 1990.	May 11, 2006
Bill Yuill <sup>(2)</sup> ..... Alberta, Canada	Vice-Chairman and Director	President and CEO of The Monarch Corporation (a private holding company with investments in telecommunications, sports properties, real estate properties and transportation).	September 22, 2004
Catherine A. Rogers ..... Alberta, Canada	Executive Vice-President Finance and Administration, Chief Financial Officer and Corporate Secretary	Joined us in 1997 as Comptroller and was promoted to Vice President of Finance and Administration in 1998 and Chief Financial Officer in 1999.	—
Bruce David Ratzlaff ..... Alberta, Canada	President, Western Life	President of Western Life since the Acquisition. Prior thereto, President of Federated Life and other positions since 1980.	—
Lana J. Wood ..... Alberta, Canada	President, WFG Agency Network	President of the Network since November, 2004. Prior thereto, Western Regional Manager, Commercial Insurance with Royal & Sun Alliance, an insurance company, from July 2002 to October 2004.	—
Doug Foster ..... Alberta, Canada	President, Bank West	President of Bank West since September 2002. Prior thereto, from 1995 to September 2002, Director of Corporate Banking for Scotia Capital, an investment bank.	—

**Notes:**

- (1) Member of the Audit Committee.
- (2) Member of the Corporate Governance, Conduct Review and Management Resources Committee.
- (3) Mr. Dutton has indicated that he will not stand for re-election at our upcoming annual shareholders' meeting. Mr. Dutton will continue to serve as our Executive Vice-President.

The directors are elected by our shareholders to hold office until the close of the first annual meeting of our shareholders following their election, unless such office is earlier vacated in accordance with our by-laws.

**Board Committees**

Our board of directors has established two committees, the Audit Committee and the Corporate Governance, Conduct Review and Management Resources Committee, which are described below.

## Audit Committee

The Audit Committee is comprised of four directors, J. Gregg Spiers (Chairman), Phillip L. Webster, Jim Dinning and Diane Brickner. All members of the Audit Committee are independent and financially literate (as determined by Multilateral Instrument 52-110, *Audit Committees* ("MI 52-110")). In determining whether a member of the Audit Committee is financially literate our Board considers the ability of the member to read and understand financial statements of a public company and such member's financial education or work experience. Mr. Speirs has six years experience as a senior officer of an insurance brokerage. Mr. Webster has been a president of private investment holding companies, which regularly evaluate financial statements related to potential investments, for over 20 years. Mr. Dinning was the president of TransAlta Corporation for seven years and was previously the Provincial Treasurer of Alberta. Diane Brickner has held the position of President and Chief Executive Officer of Peace Hills Insurance since 1990.

The Audit Committee reviews our interim unaudited consolidated financial statements and annual audited consolidated financial statements and certain corporate disclosure documents including the annual information form, management's discussion and analysis and annual and interim earnings press releases before they are approved by the Board. The Committee reviews and makes a recommendation to the Board in respect of the appointment and compensation of the external auditor and it monitors accounting, financial reporting, control and audit functions. The Audit Committee meets to discuss and review the audit plans of external auditors and is directly responsible for overseeing the work of the external auditor with respect to preparing or issuing the auditor's report or the performance of other audit, review or attest services, including the resolution of disagreements between management and the external auditor regarding financial reporting. The Committee questions the external auditor independently of management and reviews a written statement of its independence based on the criteria found in the recommendations of the Canadian Institute of Chartered Accountants. The Committee must be satisfied that adequate procedures are in place for the review of our public disclosure of financial information extracted or derived from our financial statements and it periodically assesses the adequacy of those procedures. The Audit Committee must approve or pre-approve, as applicable, any non-audit services to be provided to us by the external auditor. In addition, it reviews and reports to the Board on our risk management policies and procedures and reviews the internal control procedures to determine their effectiveness and to ensure compliance with our policies and avoidance of conflicts of interest. The Committee has established procedures for dealing with complaints or confidential submissions which come to its attention with respect to accounting, internal accounting controls or auditing matters. The terms of reference of the Audit Committee, which describes in detail its obligations and responsibilities, are disclosed as Schedule "A" to this AIF.

PricewaterhouseCoopers LLP has served as our auditor since December, 2002. Fees paid to PricewaterhouseCoopers LLP for the two most recently completed fiscal years are detailed in the following table:

	<b>Year Ended December 31, 2006</b>	<b>Year Ended December 31, 2005</b>
Audit	\$480,339	\$226,256
Audit related fees	72,126	24,671
Tax fees	-	-
All other fees	139,717	50,861
	<hr/>	<hr/>
	\$692,182	\$301,788

Audit and audit-related fees were paid for professional services rendered by the auditors for the audit of our annual financial statements or services provided in connection with statutory and regulatory filings, review of our quarterly financial statements and attendance at quarterly audit meetings. All other fees

were paid for services related to the completion of private placements and a public financing we conducted in 2005 and 2006 and for the completion of certain regulatory filings. All permissible categories of non-audit services to be provided by our external auditor must be pre-approved by the Audit Committee subject to certain statutory exceptions.

### **Corporate Governance, Conduct Review and Management Resources Committee**

The Corporate Governance, Conduct Review and Management Resources Committee consists of three independent directors, Gabor Jellinek (Chairman), Jim Dinning and Bill Yuill. The Committee is responsible for recommending to the Board suitable candidates for director positions. The selection assessment includes a wide array of factors deemed appropriate, all in the context of an assessment of the perceived needs of our Board and us at the time. In addition, the Committee assists our Board on corporate governance issues including assessing the effectiveness of the Board, its members and its committees.

The Corporate Governance, Conduct Review and Management Resources Committee's mandate also includes reviewing our human resources policies and procedures and compensation and incentive programs. The Committee is responsible for assessing senior management's performance and recommending senior management compensation to the Board. The Committee reviews the adequacy and form of directors' compensation and makes recommendations designed to ensure that directors' compensation adequately reflects the responsibilities of the Board. The Committee also administers the Option Plan and makes recommendations to the Board respecting grants of options thereunder.

## **REGULATORY MATTERS**

We are subject to regulation and supervision by various regulatory authorities in Canada and in the provinces in which we operate. The discussion below is a brief summary of certain regulatory matters applicable to our operations and those of Bank West and Western Life.

### **Our Business**

Our brokers are required to be licensed or to receive regulatory approval in each of the provinces in which they conduct business. In addition to licensing requirements applicable to brokers, all individuals engaged in brokerage and certain insurance services activities in the jurisdictions in which we operate are required to be licensed personally. Licensing laws and regulations vary from jurisdiction to jurisdiction.

### **Bank West and Western Life**

Bank West is subject to regulation and supervision by OSFI. Western Life is also subject to regulation and supervision by OSFI as well as insurance regulatory authorities of the provinces in which it is licensed to conduct business. This regulation and supervision is designed to protect depositors, policyholders and creditors rather than investors. Provincial insurance regulations deal primarily with the form of insurance contracts and the sale and marketing of insurance products, including licensing and supervision of insurance distributors. The following is a brief description of certain regulatory and supervisory matters applicable to these regulated financial institutions.

### **General**

Bank West is incorporated under the Bank Act. Western Life is incorporated under the *Insurance Companies Act* (Canada) (the "ICA") and is licensed under insurance legislation in each of the Canadian provinces and territories in which it conducts business.

The Bank Act requires Bank West to file annual and other reports on its financial condition and other matters and sets out requirements for adequate capital and adequate and appropriate forms of liquidity. The ICA and provincial and territorial insurance legislation require the filing by Western Life of annual and other reports on its financial condition, and set out requirements governing minimum continuing capital and surplus requirements ("MCCSR"), the safekeeping of assets and other matters.

The Bank Act and the ICA are administered by, and the activities of Bank West and Western Life are supervised by, OSFI. The Superintendent of Financial Institutions (Canada) (the "Superintendent") is responsible to the Minister of Finance (the "Minister") for the supervision of banks, federal insurance companies and other federal financial institutions. The Superintendent must, at least once a year, examine the business and financial condition of Bank West and Western Life for the purpose of determining whether they are in sound financial condition, and report its finding to the Minister. Where the Superintendent is concerned about an unsafe course of conduct or an unsound practice in conducting the business of a bank or a federal insurance company, the Superintendent may direct the bank or company to refrain from a course of action or to perform acts necessary to remedy the situation. The Superintendent may, in certain circumstances, take control of the assets of a bank or a company or take entire control of the bank or the company.

### **Networking and Restrictions on Related Party Transactions**

Both Bank West and Western Life may distribute the financial products and services that they provide through other financial institutions and entities in which they would be permitted to hold an investment, subject to certain restrictions, such as the limitation on banks selling certain types of insurance through their branches.

The Bank Act and the ICA prohibit certain transactions, and impose restrictions on other transactions, among related parties. Permitted related party transactions of Bank West and Western Life must be made on market terms and conditions, and in accordance with their governing legislation and each institution's related party policy. We are a related party of Bank West under the Bank Act and of Western Life under the ICA.

### **Investment Powers**

Under the Bank Act and the ICA, the directors of Bank West and Western Life must establish prudent investment and lending policies, standards and procedures. Bank West and Western Life must also maintain a prudent portfolio of investments and loans, subject to overall portfolio limits on the amounts they may invest in certain classes of investments, such as consumer and commercial loans, real property and equities.

The Bank Act and the ICA provide broad powers to invest in securities, but limit the acquisition of control or substantial investments in other entities. A bank or a federal insurance company will have a substantial investment in an entity if it has direct or indirect beneficial ownership of voting shares carrying more than 10% of the voting rights attached to all outstanding voting shares of a body corporate, shares representing more than 25% of the shareholders' equity of a body corporate, or more than 25% of the ownership interests in an unincorporated entity.

Banks and federal life insurance companies may make controlling and, in certain circumstances, non-controlling substantial investments in Canadian banks and their holding companies, trust and loan companies, insurance companies and their holding companies, cooperative credit societies, entities primarily engaged in dealing in securities, and in foreign entities that are primarily engaged outside Canada in a business that if carried on in Canada would be the business of banking, the business of a

cooperative credit society, the business of insurance, the business of providing fiduciary services or the business of dealing in securities. Permitted investments include entities that engage in financial agent activities, mutual fund and mutual fund distribution activities, and entities that provide certain information technology and processing services, and investment counselling and portfolio management services. Insurance companies may invest in entities that engage in real property management and brokerage activities, and banks may invest in entities that provide financial services. In some cases, these investments require regulatory approval.

A federal life insurance company with regulatory capital of \$25 million or less and certain of its subsidiaries may not make commercial loans where the aggregate value of those loans would exceed 5% of the total assets of the company. Where a federal life insurance company has regulatory capital over \$25 million, the company may exceed this limit with the approval of the Superintendent. A bank or a federal insurance company and certain of their subsidiaries may hold real property interests so long as the aggregate value of those interests and improvements to those interests would not exceed a prescribed amount. A bank or a federal insurance company and certain of their subsidiaries may not hold a substantial investment in participating shares in a body corporate or ownership interests in an unincorporated entity, other than a permitted entity, if their aggregate value would exceed a prescribed amount. In addition, on an aggregate basis, a bank or a federal insurance company may not acquire a substantial investment in shares or ownership interests in entities or interests in real property if the aggregate value of those investments would exceed a prescribed amount. The Superintendent has the authority to make a divestment order if a bank or federal insurance company contravenes these investment restrictions.

### **Capital Requirements for Banks**

Canadian banks, like Bank West, must maintain, in relation to their operations, adequate capital and adequate and appropriate forms of liquidity. The Superintendent may direct a bank to increase its capital or to provide additional liquidity. Regulatory capital requirements have been implemented through guidelines issued by the Superintendent and, with respect to banks, are based on standards set by the Bank for International Settlements.

OSFI expects banks to meet an assets to capital multiple test, which is calculated by dividing the bank's total assets, including specified off-balance sheet items, by its total capital. Under this test, total assets should be no greater than 20 times capital, although this multiple can be exceeded with the Superintendent's prior approval to an amount no greater than 23 times, and the Superintendent may prescribe a lower multiple.

Under the risk-based capital adequacy framework, a bank's minimum capital requirement is defined as a ratio of total capital divided by the sum of risk-weighted assets and risk-weighted off-balance sheet items. At present, the framework for calculating risk-weighted amounts covers counter party credit risk and, for qualifying deposit taking institutions, market risk. In the future, the Superintendent may adjust capital requirements so that other risks - interest rate risk, operational risk and concentration risk - may be formally considered.

The Superintendent may prescribe a risk-based capital ratio requirement for each deposit taking institution. Where a higher ratio has not been prescribed specifically, banks are expected to maintain a minimum risk-based tier 1 capital ratio of at least seven per cent and a total capital ratio of at least ten per cent. The Superintendent may order a bank to increase its capital or to provide additional liquidity, but the bank may not disclose any such directives.

## **Capital Requirements for Life Insurance Companies**

Federal life insurance companies, like Western Life, must meet its MCCR based on a guideline issued by OSFI. A federal life insurer's MCCR is determined by applying factors for each of the following five risk components to specific on- and off-balance sheet assets or liabilities and by adding the results: asset default risk, mortality/morbidity/lapse risks, interest margin pricing risk, changes in interest rate environment risk and segregated funds risk. Moreover, if a company has reduced its liability for business ceded to unregistered reinsurers, these liabilities less a credit for unregistered reinsurance must be deducted from the total capital available. Capital requirements may be adjusted in future by the Superintendent as experience with the formula develops, as the risk profiles of life insurers change, and so that other risks such as foreign exchange risk may be formally considered.

The definition of capital comprises two tiers, tier 1 (core capital) and tier 2 (supplementary capital), and involves certain deductions, limits and restrictions. The minimum MCCR ratio for federal life insurers is 120%. The MCCR ratio compares capital available to capital required as calculated by applying factors for specified risks. OSFI believes that each institution should establish a target capital level that provides a cushion above minimum requirements to cope with volatility in markets and economic conditions, innovations in the industry, consolidation trends and international developments. OSFI expects each federal life insurer to establish a target total MCCR ratio, and maintain ongoing capital, at no less than the supervisory target of 150%. Western Life may agree with OSFI to maintain a higher MCCR ratio. The Superintendent may, on a case-by-case basis, establish in consultation with a federal life insurer an alternative supervisory target ratio based upon an individual institution's risk profile. The Superintendent may order a federal life insurer to increase its capital or to provide additional liquidity, but the insurer may not disclose any such directives.

In addition, since tier 1 capital is the primary element of capital that allows institutions to absorb losses during ongoing operations, each institution should also establish a tier 1 target ratio that provides a significant cushion above the minimum net tier 1 ratio of 60% MCCR. OSFI expects each institution to establish a target, and maintain its ongoing net tier 1 ratio, at no less than the supervisory target of 105% MCCR.

## **Dynamic Capital Adequacy Testing**

In order to ensure it meets its capital requirements as prescribed by OSFI, Western Life periodically examines, as required, its capital adequacy by conducting dynamic capital adequacy testing ("DCAT"), which examines the effect of various plausible adverse scenarios on its forecasted capital adequacy. The purpose of DCAT is to identify and bring to the attention of Western Life's board of directors, plausible threats to satisfactory financial condition, actions which lessen the likelihood of those threats and actions which would mitigate a threat if it materialized. DCAT is defensive in that it addresses threats to financial condition rather than the exploitation of opportunity. DCAT considers the past, present and future financial position of Western Life and the sensitivity of its surplus to changes in various experience factors and management practices. DCAT analysis considers 12 business scenarios projected five years in the future to provide an early warning system for capital management.

## **Restrictions on Dividends and Capital Transactions**

Bank West and Western Life require regulatory approval prior to withdrawal of capital and, in certain circumstances, prior to the payment of dividends. The Bank Act and the ICA prohibit the declaration or payment of any dividend on shares if there are reasonable grounds for believing the bank or company is, or the payment of the dividend would cause the bank or the company to be, in contravention of its requirements to maintain adequate capital, liquidity and assets. The Bank Act and the ICA also prohibits

the declaration or payment of a dividend in any financial year without Superintendent approval if, at the time the dividend is declared, the total of all dividends declared by the bank or the company in that year would exceed the aggregate of the bank's or the company's net income up to that time in that year and its retained net income for the preceding two financial years. A bank or a federal insurance company must notify the Superintendent of the declaration of a dividend at least ten days prior to the date fixed for its payment. Similarly, the legislation prohibits the purchase for cancellation of any shares issued by a bank or a federal insurance company or the redemption of any redeemable shares or other similar capital transactions, if there are reasonable grounds for believing that the bank or the company is, or the payment would cause the bank or the company to be, in contravention of its requirements to maintain adequate capital, liquidity and assets. Share cancellation or redemption would also require the prior approval of the Superintendent.

### **Constraints on the Transfer of Shares or Assets**

The Bank Act and the ICA contain certain restrictions on the purchase or other acquisition, issue, transfer and voting of any shares of a bank or a federal insurance company. No person is permitted to acquire shares of Bank West or Western Life, or to acquire control of an entity that holds such an interest, if the acquisition would cause the person to have a "significant interest" in any class of shares of those entities or acquire control of them, unless the prior written approval of the Minister is obtained. A person has a significant interest in a class of shares of a bank or a federal insurance company where the aggregate of any shares of that class beneficially owned by that person, or an entity controlled by that person and by any person associated or acting jointly or in concert with that person, exceeds 10% of all outstanding shares of that class of shares of the bank or the company. In addition, a bank or a federal insurance company is not permitted to record any transfer or issue of shares to a person if the transfer or issue would cause the person to have or increase a significant interest in the bank or the company unless regulatory approval has been obtained.

If a person contravenes any of these ownership restrictions, the person may not exercise any voting rights attached to the shares of the bank or the federal insurance company owned by the person or any entity controlled by the person. Moreover, the Minister may, by order, direct that person to dispose of all or any portion of those shares.

Under the Bank Act and the ICA, the approval of the Minister is required for a bank or a federal insurance company to transfer all or substantially all of its assets to another person, or, in the case of an insurance company, to transfer or reinsure its policies, other than reinsurance in the ordinary course of its business. Superintendent approval is generally required by a bank or a federal insurance company or their subsidiaries to acquire assets from, or transfer assets to, a person if the total value of the assets and all other assets acquired from or transferred to the person by the bank or the company and its subsidiaries in the twelve months preceding the transfer is greater than 10% of the total value of the assets of the bank or the company.

### **Canada Deposit Insurance Corporation**

Bank West is a member institution of the Canada Deposit Insurance Corporation ("CDIC"). The CDIC insures certain "deposits" (as defined in section 2 to the CDIC Act) held at member institutions. The CDIC has adopted by-laws for its member institutions, including those establishing Standards of Sound Business and Financial Practices. According to these standards, the board of directors of Bank West is expected to establish the business objectives of the institution and to evaluate the institution's operating and financial results against forecast results. The board is expected to have an understanding of the liquidity and funding needs and capital needs of the institution, to establish prudent policies to address those needs and to review those policies annually to ensure that they remain appropriate. Moreover, the

board is expected to obtain reasonable assurance regularly that the institution has an appropriate control environment, and to establish the mandate of and approve the funding and plan for the institution's independent inspection and audit function. The board is expected to have an understanding of the risks inherent in the institution's business, including credit, market, structural, fiduciary and operational risk, and to establish and review at least annually prudent risk management policies for those risks. At times mandated by the standards, senior management and directors must acknowledge their responsibilities under the standards and attest to the institution's ability to meet those standards in its operations. An institution's board of directors must approve a "standards report" that is filed with the CDIC.

The level of deposit insurance premiums and the frequency of filing reports with the CDIC are related to the classification of the member institution under the CDIC Differential Premiums By-law. Under this By-law, each member institution is classified by a premium category that is based on a rating of the quantitative and qualitative factors and criteria assigned to it by a CDIC examiner. A CDIC member institution is not permitted to disclose CDIC premium rate information, including examiner's ratings.

### **Canadian Life and Health Insurance Compensation Corporation**

Western Life is a member institution of the Canadian Life and Health Insurance Compensation Corporation ("CompCorp"). The Canadian life insurance industry created CompCorp to provide Canadian life insurance policyholders with protection, within limits, against the loss of policy benefits in the event of the insolvency of their life insurance company. CompCorp is funded by its member insurance companies, including Western Life. There are two principal forms of assessment: (i) specific assessments to cover funding made in connection with an insolvent member, to a maximum of 0.85% per annum of a company's Canadian premium income from covered policies averaged over the previous five years with certain exclusions, including segregated fund premiums, and (ii) loan assessments, but in no circumstances will loan assessments result in loans outstanding from a member being in excess of 3.0% of that member's five-year average premium income from covered policies.

### **Financial Consumer Agency of Canada**

Under the *Financial Consumer Agency of Canada Act* ("FCAC Act"), the Financial Consumer Agency of Canada (the "FCAC") enforces consumer related provisions in federal statutes that govern financial institutions. Consumer-related provisions include Bank Act and ICA provisions dealing with customer confidentiality, complaint handling procedures and cost of borrowing disclosure.

The Commissioner of the FCAC (the "Commissioner") has the duty to supervise banks and federal insurance companies to determine whether they are in compliance with consumer provisions that apply to them. The Commissioner has the power to issue notices of violation and to compel the disclosure of personal information necessary to ensure compliance. In addition, the Commissioner may carry on any activity in furtherance of consumer awareness of financial institution obligations under applicable consumer provisions.

The Commissioner must report to the Minister on all matters connected with the administration of the FCAC Act and the consumer provisions of federal financial institutions statutes, including the Bank Act and the ICA.

### **Anti-money Laundering and Anti-terrorism Legislation**

In June 2000, the Government of Canada enacted legislation now entitled the Proceeds of Crime (Money Laundering) and Terrorism Financing Act to implement measures to assist in detecting and deterring money laundering and to facilitate the investigation of money laundering offences. That legislation and its

regulations impose reporting, record keeping and "know your client" obligations on certain financial institutions, including banks and life insurance companies. Under that Act's regulations, banks and life insurance companies must report to a federal agency, the Financial Transactions and Reports Analysis Centre of Canada ("FINTRAC") any transaction that they have reason to suspect relates to the commission of a money laundering offence. In addition, banks and life insurance companies have an obligation to report to FINTRAC or other agencies cross border currency and electronic funds transfers as well as large cash transactions over a certain monetary threshold. Banks and life insurance companies are required to verify the identity of their customers in a prescribed manner and to retain certain customer records for prescribed periods.

In addition, in response to the events of September 11, 2001, the Canadian Criminal Code was amended to prohibit financial institutions and other persons from knowingly dealing in property or providing financial services to persons listed in federal regulations known to be involved in terrorist activities. Financial institutions must search their customer records and report to Canadian regulators and law enforcement agencies identified property or accounts of listed persons.

### **Privacy Legislation**

The two most relevant privacy statutes for our business are the federal Personal Information Protection and Electronic Documents Act ("PIPEDA") and the Alberta Personal Information Protection Act ("PIPA"). PIPEDA is a federal statute that deals with the collection, use and disclosure of personal information. As of January 1, 2004 it applies to all private sector organizations in Canada that are not subject to substantially similar provincial privacy legislation. The purpose of PIPEDA is to protect the privacy of individuals while recognizing the need of organizations to collect personal information. Alberta has also passed private sector privacy legislation that came into force on January 1, 2004. Like PIPEDA, PIPA regulates collection, use and disclosure of personal information by private sector organizations.

As of January 1, 2004, we are required to abide by privacy laws in respect of our commercial activities. In light of the introduction of the new privacy legislation, we have taken steps to maintain the physical, procedural and technical security with respect to our offices and information storage facilities to prevent any loss, misuse, unauthorized access, disclosure, or modification of our client's personal information which are in addition to the controls which we had in place prior to the introduction of the new legislation. We also distribute to our customers a brochure outlining our comprehensive privacy policies.

## **CAPITAL STRUCTURE**

The following is a summary of the material attributes and characteristics of our securities. We are authorized to issue an unlimited number of Common Shares without nominal or par value, of which 44,174,940 are issued and outstanding as fully paid and non-assessable as at the date hereof. We are also authorized to issue an unlimited number of First Preferred Shares and an unlimited number of Second Preferred Shares. As at the date hereof, 100 First Preferred Shares, Series One and 148,347 First Preferred Shares, Series Two were issued and outstanding and no Second Preferred Shares had been issued. We have also issued debentures and notes as described below.

### **Common Shares**

The holders of Common Shares are entitled, subject to the rights of holders of First Preferred Shares (as defined herein) and any other class of shares ranking senior to the Common Shares, to dividends as and when declared by our board of directors, to one vote per share at meetings of shareholders and, upon liquidation, subject to the rights of holders of First Preferred Shares and any other class of shares ranking

senior to the Common Shares, to receive those of our assets as are distributable to the holders of the Common Shares.

### **First Preferred Shares**

The First Preferred Shares may be issued from time to time in one or more series ("First Preferred Shares"), each series consisting of a number of First Preferred Shares as determined by the board of directors who may also fix the designations, rights, privileges, restrictions and conditions attaching to the shares of each series of First Preferred Shares. The First Preferred Shares of each series shall, with respect to payment of dividends and distributions of assets in the event of our liquidation, dissolution or winding-up, whether voluntary or involuntary, or any other distribution of our assets among our shareholders for the purpose of winding-up our affairs, rank on a parity with the First Preferred Shares of every other series and shall be entitled to preference over the Common Shares and the shares of any other class ranking junior to the First Preferred Shares. The First Preferred Shares of any series shall also be entitled to such other preferences, not inconsistent with our articles of incorporation, over the Second Preferred Shares, the Common Shares and the shares of any other class ranking junior to the First Preferred Shares or as may be fixed by our board of directors from time to time.

### **First Preferred Shares, Series One**

The holders of First Preferred Shares, Series One are entitled to fixed cumulative annual dividends in the amount of 4.0% of the redemption value of \$1,000 per share (the "Redemption Value") as and when declared by our board of directors. To date, 100 First Preferred Shares, Series One are issued and outstanding. The holders of such shares are not entitled to receive notice of, to attend or to vote at any meeting of our shareholders other than meetings of holders of the First Preferred Shares, Series One. We may redeem the First Preferred Shares, Series One at any time, in whole or in part, at a price per share equal to the Redemption Value plus accrued and unpaid dividends thereon. After December 31, 2005, holders of these shares have the right to require us to redeem up to 66 2/3% of such holders' shares in any given calendar year at the Redemption Value plus any accrued and unpaid interest. In the event of our liquidation, dissolution or winding up, the holders of these shares are entitled to receive the Redemption Value per share, together with any accrued and unpaid dividends thereon, in priority to holders of Common Shares, holders of Second Preferred Shares, or holders of any series or other shares ranking junior to the First Preferred Shares, Series One with respect to returns of capital. No distribution shall be made to the holders of any other class of shares, if such distribution would result in us having insufficient net assets to redeem the First Preferred Shares, Series One.

### **First Preferred Shares Series Two**

The First Preferred Shares, Series Two were issued on June 29, 2006 at an issue price of \$100.00 per share (the "Redemption Amount"). The holders of First Preferred Shares, Series Two are entitled to a fixed dividend of 6.75% per annum, payable semi-annually as declared by our board of directors. To date, 148,347 First Preferred Shares, Series One are issued and outstanding. The holders of such shares are not entitled to receive notice of, to attend or to vote at any meeting of our shareholders other than meetings of holders of the First Preferred Shares, Series Two. The First Preferred Shares, Series Two are convertible into Common Shares at any time at the holder's option at a price of \$3.60 per Common Share. The First Preferred Shares, Series Two will be redeemable by us only after the third anniversary of the date of issuance. Payment on redemption of the First Preferred Shares, Series Two will be made by issuing Common Shares at 95% of the prior average 20-day weighted average trading price prior to redemption. Redemption from the third anniversary to and including the fifth anniversary will only occur where the Common Shares are trading at a price of not less than 135% of the \$3.60 conversion price. After the fifth anniversary of the date of issuance, the First Preferred Shares, Series Two will be redeemable at our

option by issuing Common Shares at 95% of the prior average 20-day weighted average trading price. If the First Preferred Shares, Series Two are not redeemed on the fifth anniversary and each anniversary thereafter, they will pay a dividend per annum, payable semi-annually, as declared by our board of directors, of 3.5% above the five year Canadian bond rate as quoted seven days before the applicable anniversary date. In addition, if the First Preferred Shares, Series Two remain outstanding but are not listed on a recognized Canadian stock exchange, the dividend shall be increased a further 0.50%. In the event of our liquidation, dissolution or winding up, the holders of these shares are entitled to receive the Redemption Amount per share, together with any accrued and unpaid dividends thereon, in priority to holders of Common Shares, holders of Second Preferred Shares, or holders of any series or other shares ranking junior to the First Preferred Shares, Series Two with respect to returns of capital and *pari passu* with the holders of First Preferred Shares, Series One.

### **Second Preferred Shares**

The Second Preferred Shares may be issued from time to time in one or more series, each series consisting of a number of Second Preferred Shares as determined by our board of directors who may also fix the designations, rights, privileges, restrictions and conditions attaching to the shares of each series of Second Preferred Shares. The Second Preferred Shares of each series shall, with respect to payment of dividends and distributions of assets in the event of our liquidation, dissolution or winding-up, whether voluntary or involuntary, or any other distribution of our assets among our shareholders for the purpose of winding-up our affairs, rank subsequent to the First Preferred Shares and on a parity with the Second Preferred Shares of every other series and shall be entitled to preference over the Common Shares and the shares of any other class ranking junior to the Second Preferred Shares. The Second Preferred Shares of any series shall also be entitled to such other preferences, not inconsistent with the provisions of our articles of incorporation, over the Common Shares and the shares of any other class ranking junior to the Second Preferred Shares as may be fixed by our board of directors from time to time.

### **4% Debentures**

Pursuant to the terms of a trust indenture between us and Computershare dated March 31, 1999 we issued \$10,000,000 principal amount of 4% subordinated convertible redeemable debentures (the "4% Debentures"). As of the date hereof, there is \$10,000,000 aggregate principal amount of 4% Debentures issued and outstanding.

The 4% Debentures mature on March 31, 2009. The 4% Debentures bear interest at the rate of 4% per annum payable semi-annually in arrears on June 30 and December 31 in each year. On maturity, we will repay the indebtedness represented by the 4% Debentures by paying Computershare in lawful money of Canada an amount equal to the principal amount of the outstanding 4% Debentures together with accrued and unpaid interest. We may, subject to the satisfaction of certain conditions, elect to satisfy our obligation to pay all or any part of the aggregate principal amount payable to holders of the 4% Debentures on maturity by issuing that number of freely tradeable Common Shares obtained by dividing such aggregate principal amount of 4% Debentures by 95% of the weighted average trading price of the Common Shares on the TSX for the 20 consecutive trading days ending not more than five trading days preceding maturity of the 4% Debentures.

Each 4% Debenture is convertible at the holder's option into fully paid and non-assessable Common Shares at the conversion price of \$3.00 per Common Share, subject to adjustment in certain events.

After March 31, 2001 to and including maturity, we may redeem the 4% Debentures at par plus accrued and unpaid interest to and including the date of redemption provided that the weighted average trading price of the Common Shares on the TSX during the 20 consecutive business days immediately preceding

the date on which the notice of redemption is given was more than 130% of the conversion price. We may also elect, subject to satisfying certain conditions, to satisfy our obligation to repay the principal amount of all or any part of the 4% Debentures on redemption by delivering such number of Common Shares to holders of 4% Debentures obtained by dividing the aggregate principal amount redeemed by the conversion price of the 4% Debentures in effect on the redemption date.

### **The 4% Extendible Debenture**

We issued a \$5,000,000 principal amount 4% subordinated convertible redeemable debenture on January 3, 2000 (the "4% Extendible Debenture") pursuant to a debenture certificate. As at the date hereof, the 4% Extendible Debenture is issued and outstanding.

The 4% Extendible Debenture matures on January 3, 2010 but, subject to the satisfaction of certain financial restrictions, maturity can be extended at our option to January 3, 2015. The 4% Extendible Debenture bears interest at the rate of 4% per annum payable semi-annually in arrears on June 30 and December 31 in each year and, if the 4% Extendible Debenture is extended, will bear interest at prime plus 1%. The interest rate on the 4% Extendible Debenture may decrease upon the occurrence of certain events. On maturity, we will repay the indebtedness represented by the 4% Extendible Debenture to the holder thereof in lawful money of Canada together with accrued and unpaid interest.

Each 4% Extendible Debenture is convertible at the holder's option into fully paid and non-assessable Common Shares at the conversion price of \$3.25 per Common Share, subject to adjustment in certain events.

We are entitled to repay, in whole or in part, at any time and from time to time, the principal amount of the 4% Extendible Debentures without any bonus or penalty.

### **Notes**

Pursuant to the terms of a trust indenture between us and Computershare dated February 25, 2005, we issued \$1,000,000 principal amount of 12% subordinated notes (the "Notes"). As of the date hereof, there is \$1,000,000 aggregate principal amount of Notes issued and outstanding.

The Notes mature on March 1, 2010. The Notes bear interest at the rate of 12% per annum payable semi-annually in arrears on September 1 and March 1 in each year commencing September 1, 2005. On maturity, we will repay the indebtedness represented by the Notes by paying Computershare in lawful money of Canada an amount equal to the principal amount of the outstanding Notes together with accrued and unpaid interest. The Notes are not redeemable.

## **SHAREHOLDER RIGHTS PLAN**

On March 20, 2006, we adopted a Shareholder Rights Plan (the "Plan"). On May 11, 2006 at our Annual and Special Meeting, our shareholders approved the Plan in accordance with the requirements of the TSX. The Board of Directors adopted the Plan to ensure, to the extent possible, that all of our shareholders are treated equally and fairly in connection with any takeover bid or similar offer for all or a portion of our outstanding Common Shares. The Plan has been implemented by way of a Shareholder Rights Agreement (the "Agreement") dated effective March 20, 2006 between us and Computershare Trust Company of Canada, as rights agent (the "Rights Agent").

## **Purpose of the Plan**

The objectives of the Plan are to ensure, to the extent possible, that all of our shareholders are treated equally and fairly in connection with any takeover bid for us. Takeover bids may be structured to be coercive or may be initiated at a time when the Board of Directors will have a difficult time preparing an adequate response to the offer. Accordingly, such offers do not always result in shareholders receiving equal or fair treatment or full or maximum value for their investment. Under current Canadian securities legislation, a takeover bid is required to remain open for 35 days, a period of time which the Board of Directors believes is insufficient for the directors to: (i) evaluate a takeover bid (particularly if it includes share consideration); (ii) explore, develop and pursue alternatives which are superior to the takeover bid and which could maximize shareholder value; and (iii) make reasoned recommendations to the shareholders.

The Plan discourages discriminatory, coercive or unfair takeovers of us and gives the Board of Directors time if, in the circumstances, the Board of Directors determines it is appropriate to take such time, to pursue alternatives to maximize shareholder value in the event an unsolicited takeover bid is made for all or a portion of our outstanding Common Shares. As set forth in detail below, the Plan discourages coercive hostile takeover bids by creating the potential that any Common Shares which may be acquired or held by such a bidder will be significantly diluted. The potential for significant dilution to the holdings of such a bidder can occur as the Plan provides that all holders of Common Shares who are not related to the bidder will be entitled to exercise rights issued to them under the Plan and to acquire Common Shares at a substantial discount to prevailing market prices. The bidder or the persons related to the bidder will not be entitled to exercise any Rights under the Plan. Accordingly, the Plan will encourage potential bidders to make takeover bids by means of a Permitted Bid (as defined below) or to approach the Board of Directors to negotiate a mutually acceptable transaction. The Permitted Bid provisions of the Plan are designed to ensure that in any takeover bid for our outstanding Common Shares all shareholders are treated equally and are given adequate time to properly assess such takeover bid on a fully-informed basis.

The Board of Directors did not adopt the Plan to prevent a takeover of us, to secure the continuance of management or the directors in their respective offices or to deter fair offers for our Common Shares.

## **Summary of the Plan**

The following summary of terms of the Plan is qualified in its entirety by reference to the text of the Agreement. A shareholder or other interested party may obtain a copy of the Agreement by contacting the Senior Vice President Finance and Administration and Chief Financial Officer, Western Financial Group Inc., 309 -1st Street West, P.O. Box 5519, High River, Alberta, T1V 2A7 or by accessing our publicly filed documents, including the Agreement, on SEDAR at [www.sedar.com](http://www.sedar.com).

## **Term**

The Plan (unless earlier terminated) will remain in effect until termination of the our annual meeting of shareholders in 2009 unless the term of the Agreement is extended beyond such date by resolution of shareholders at a shareholders' meeting.

## **Issue of Rights**

One right (a "Right") has been issued by us pursuant to the Agreement in respect of each of our Common Shares outstanding at the close of business on March 20, 2006 (the "Record Time"). One Right will also

be issued for each additional Common Share issued after the Record Time and prior to the earlier of the Separation Time (as defined below) or the Expiration Time (as defined below).

### **Rights Exercise Privilege**

The Rights will separate from the voting shares to which they are attached and become exercisable at the time (the "Separation Time") which is 10 trading days following the date a person becomes an Acquiring Person or announces an intention to make a takeover bid that is not an acquisition pursuant to a takeover bid permitted by the Plan (a "Permitted Bid").

Any transaction or event in which a person (an "Acquiring Person"), including associates and affiliates and others acting in concert, acquires (other than pursuant to an exemption available under the Plan or a Permitted Bid) Beneficial Ownership (as defined in the Plan) of 20% or more of our voting shares is referred to as a "Flip-in Event". Any Rights held by an Acquiring Person on or after the earlier of the Separation Time or the first date of public announcement by us or an Acquiring Person that an Acquiring Person has become such, will become void and the Rights (other than those held by the Acquiring Person) will permit the holder to purchase Common Shares at a substantial discount to their then prevailing market price.

The issuance of the Rights is not dilutive and will not affect reported earnings or cash flow per share until the Rights separate from the underlying Common Shares and become exercisable or until the exercise of the Rights. The issuance of the Rights will not change the manner in which shareholders currently trade their Common Shares.

### **Permitted Lock-Up Agreement**

A person will not become an Acquiring Person by virtue of having entered into an agreement (a "Permitted Lock-Up Agreement") with a shareholder whereby the shareholder agrees to deposit or tender voting shares to a takeover bid made by such person, provided that the agreement meets certain requirements including:

- (a) the terms of the agreement are publicly disclosed and a copy of the agreement is publicly available;
- (b) the shareholder who has agreed to tender voting shares to the takeover bid (the "Lock-Up Bid") made by the other party to the agreement is permitted to terminate its obligation under the agreement in order to tender voting shares to another takeover bid or transaction where: (i) the offer price or value of the consideration payable under the other takeover bid or transaction is greater than the price or value of the consideration per share at which the shareholder has agreed to deposit or tender voting shares to the Lock-Up Bid or is equal to or greater than a specified minimum which is not more than 7% higher than the offer price under the Lock-Up Bid; and (ii) if the number of voting shares offered to be purchased under the Lock-Up Bid is less than all of the voting shares held by shareholders (excluding shares held by the offeror), the number of voting shares offered to be purchased under the other takeover bid or transaction (at an offer price not lower than in the Lock-Up Bid) is greater than the number of voting shares offered to be purchased under the Lock-Up Bid or is equal to or greater than a specified number which is not more than 7% higher than the number of voting shares offered to be purchased under the Lock-Up Bid; and
- (c) no break-up fees or other penalties that exceed in the aggregate the greater of 2.5% of the price or value of the consideration payable under the Lock-Up Bid and 50% of the increase in

consideration resulting from another takeover bid or transaction shall be payable by the shareholder if the shareholder fails to deposit or tender voting shares to the Lock-Up Bid.

### **Certificates and Transferability**

Prior to the Separation Time, the Rights will be evidenced by a legend imprinted on certificates for Common Shares issued from and after the effective date (the "Effective Date") of the Agreement (being the later of the date of the Agreement and the receipt by us of all regulatory approvals with respect to the Agreement). Rights are also attached to Common Shares outstanding on the Effective Date, although share certificates issued prior to the Effective Date will not bear such a legend. Shareholders are not required to return their certificates in order to have the benefit of the Rights. Prior to the Separation Time, Rights will trade together with the Common Shares and will not be exercisable or transferable separately from the Common Shares. From and after the Separation Time, the Rights will become exercisable, will be evidenced by Rights Certificates and will be transferable separately from the Common Shares.

### **Permitted Bid Requirements**

The requirements of a "Permitted Bid" include the following:

- (a) the takeover bid must be made by means of a takeover bid circular;
- (b) the takeover bid is made to all holders of voting shares as registered on our books, other than the offeror;
- (c) the takeover bid contains, and the take-up and payment for securities tendered or deposited is subject to, an irrevocable and unqualified provision that no voting shares will be taken up or paid for pursuant to the takeover bid prior to the close of business on the date which is not less than 60 days following the date of the takeover bid and only if at such date more than 50% of the voting shares held by independent shareholders shall have been deposited or tendered pursuant to the takeover bid and not withdrawn;
- (d) the takeover bid contains an irrevocable and unqualified provision that unless the takeover bid is withdrawn, voting shares may be deposited pursuant to such takeover bid at any time during the period of time between the date of the takeover bid and the date on which voting shares may be taken up and paid for and that any voting shares deposited pursuant to the takeover bid may be withdrawn until taken up and paid for; and
- (e) the takeover bid contains an irrevocable and unqualified provision that if, on the date on which voting shares may be taken up and paid for, more than 50% of the voting shares held by independent shareholders shall have been deposited pursuant to the takeover bid and not withdrawn, the offeror will make a public announcement of that fact and the takeover bid will remain open for deposits and tenders of voting shares for not less than ten business days from the date of such public announcement.

The Plan allows for a competing Permitted Bid (a "Competing Permitted Bid") to be made while a Permitted Bid is in existence. A Competing Permitted Bid must satisfy all of the requirements of a Permitted Bid except that it may expire on the same date as the Permitted Bid, subject to the requirement that it be outstanding for a minimum period of 35 days.

## **Waiver and Redemption**

If a potential offeror does not desire to make a Permitted Bid, it can negotiate with, and obtain the prior approval of, the Board of Directors to make a takeover bid by way of a takeover bid circular sent to all holders of voting shares on terms which the Board of Directors considers fair to all shareholders. In such circumstances, the Board of Directors may waive the application of the Plan thereby allowing such bid to proceed without dilution to the offeror. Any waiver of the application of the Plan in respect of a particular takeover bid shall also constitute a waiver of any other takeover bid which is made by means of a takeover bid circular to all holders of voting shares while the initial takeover bid is outstanding. The Board of Directors may also waive the application of the Plan in respect of a particular Flip-in Event that has occurred through inadvertence, provided that the Acquiring Person that inadvertently triggered such Flip-in Event reduces its beneficial holdings to less than 20% of our outstanding voting shares within 14 days or such earlier or later date as may be specified by the Board. With the prior consent of the holders of voting shares, the Board of Directors may, prior to the occurrence of a Flip-in Event that would occur by reason of an acquisition of voting shares otherwise than pursuant to the foregoing, waive the application of the Plan to such Flip-in Event.

The Board of Directors may, with the prior consent of the holders of voting shares, at any time prior to the occurrence of a Flip-in Event, elect to redeem all but not less than all of the then outstanding Rights at a redemption price of \$0.00001 per Right. Rights are deemed to be redeemed following completion of a Permitted Bid, a Competing Permitted Bid or a takeover bid in respect of which the Board of Directors has waived the application of the Plan.

## **Exemptions for Investment Advisors**

Investment advisors (for client accounts), trust companies (acting in their capacity as trustees or administrators), statutory bodies whose business includes the management of funds (for employee benefit plans, pension plans, or insurance plans of various public bodies) and administrators or trustees of registered pension plans or funds acquiring greater than 20% of the voting shares are exempted from triggering a Flip-in Event, provided they are not making, either alone or jointly or in concert with any other person, a takeover bid.

## **Board of Directors**

The adoption of the Plan will not in any way lessen or affect the duty of the Board of Directors to act honestly and in good faith with a view to our best interests. The Board of Directors, when a takeover bid or similar offer is made, will continue to have the duty and power to take such actions and make such recommendations to shareholders as are considered appropriate.

## **Amendment**

We may, prior to the date of the Meeting, without the approval of the holders of Rights or Common Shares, supplement, amend, vary or delete any of the provisions of the Agreement and may, after the date of the Meeting (provided the Agreement is confirmed by shareholders at such meeting) with the prior approval of shareholders (or the holders of Rights if the Separation Time has occurred), supplement, amend, vary or delete any of the provisions of the Agreement. We may make amendments to the Agreement at any time to correct any clerical or typographical error or, subject to confirmation at the next meeting of shareholders, make amendments which are required to maintain the validity of the Agreement due to changes in any applicable legislation, regulations or rules.

## **Voting Requirements**

The Agreement provides that it must be confirmed by shareholders within six months of the Effective Date. The TSX also requires that such confirmation be obtained as a condition to the listing of the Rights on such stock exchange.

## **CONFLICTS OF INTEREST**

There are potential conflicts of interest which some of our directors will be subject to in connection with our operations. Certain of our directors and officers are engaged in, and will continue to be engaged in, the search for corporations, businesses or assets and such searches may be in competition with our search for such corporations, businesses, or assets. Accordingly, situations may arise where some or all of the directors and officers will be in direct competition with us. Conflicts, if any, will be subject to the procedures and remedies as provided under the *Business Corporations Act* (Alberta).

We own a 35.7% equity interest in Jennings. Robert G. Jennings, one of our directors, is the President of Jennings and one of Jennings' principal shareholders, with an 9.6% equity interest. We have also invested in Jennings through the issuance of an unsecured, non-interest bearing demand note. The largest amount of indebtedness owing under the note during the fiscal year ended December 31, 2006 was \$1.5 million and the amount outstanding as of the date hereof, was \$1.5 million. We also own 500 preferred shares in the capital of Jennings.

In addition, we are party to the unanimous shareholders agreement of Jennings, pursuant to which the transfer of its common shares is restricted. Under the terms of such agreement, we could become obligated to purchase from shareholders of Jennings, some or all of their shares and subordinated loans of Jennings, subject to a purchase limitation of 20% of the outstanding shares and subordinated loans of Jennings annually and the achievement of certain performance thresholds for Jennings. Payments for purchased shares would be made over a period of two years. Furthermore, if any person acquires 20% or more Common Shares, we are obliged to either buy all of the shares and subordinated loans of Jennings or sell all of our interest in Jennings, at our option. This agreement also gives us the right to appoint two nominees to the board of directors of Jennings.

## **RISK FACTORS**

An investment in our securities involves a number of risks. In addition to the other information contained in this AIF, readers should give careful consideration to the following factors, which are qualified in their entirety by reference to, and must be read in conjunction with, the detailed information appearing elsewhere in this AIF. Any of the matters highlighted in these risk factors could have a material adverse effect on our results of operations, business prospects or financial condition.

## **Acquisitions and Growth**

Our growth plans depend in part upon the ongoing acquisition, at reasonable prices, of independent brokers and other businesses. To meet our growth plans, an adequate number of acquisition candidates must be available at prices which will allow us to operate on a profitable basis. We may determine that current market or pricing conditions in the P&C insurance brokerage industry make future acquisitions uneconomic or that the available acquisition opportunities are not sufficiently attractive to us. Moreover, we may not be able to finance such acquisitions as additional capital may not be available or may not be available on commercially acceptable terms.

To manage any future growth effectively, we will need to continue to implement and improve our operational, financial and management information systems and to hire, train, motivate, manage and retain our employees. There can be no assurance that we will be able to manage such growth effectively, that our management, personnel or systems will be adequate to support our operations or that we will be able to achieve the increased levels of revenue commensurate with the increased levels of operating expenses associated with this growth, and failure to do so could have a material adverse effect on our business, financial condition and results of operations.

As part of our growth strategy, we seek to cross-sell multiple lines of business to existing customers. This strategy may not result in achieving our desired growth. Due in part to the decentralized nature of our operations, we may have difficulty in focusing our employees on our sales management program and cross-selling strategy. In addition, we may have difficulty integrating acquired operations and newly hired employees into our sales management program and cross-selling strategy.

We have identified 146 Target Communities (that we estimate have 400 brokers) for future expansion in the next five years. There is no assurance that we can complete acquisitions in any of these communities within the estimated time frame or at all.

Although we conduct due diligence in respect of the business and operations of each of the businesses we acquire, we may not have identified all material facts concerning these businesses. Unanticipated events or liabilities relating to these businesses could have a material adverse effect on our financial condition. Furthermore, once we have integrated an acquired business, it may not achieve levels of revenue, profitability, or productivity comparable to our existing locations, or otherwise perform as expected. Our failure to succeed in our growth strategy or to integrate one or more acquired business so that it achieves our performance goals may have a material adverse effect on our results of operations and financial condition.

### **Contingent Commissions**

Many P&C insurance companies pay us contingent commissions for achieving profitability and premium volume goals set by them and/or based on the loss experience of the insurance we place with them. We generally receive contingent commissions in the first and second quarters of each year in respect of contingent commissions earned in the previous year. However, we have no control over the ability of P&C insurance companies to estimate loss reserves, which is a factor that affects the amount of contingent commissions that we will receive. In addition, because no significant incremental operating costs are incurred when contingent commissions are realized, a significant decrease in contingent commissions can cause a disproportionate decrease in net income and would consequently have a negative impact on our financial results. This could also limit our ability to incur and service debt and comply with financial covenants in our existing credit facility and could have a material adverse effect on our business, financial condition and results of operations.

### **Capital Funding**

We will, from time to time, require additional financing to continue to grow our business. Our ability to arrange such financing in the future will depend in part upon the prevailing capital market conditions as well as our business performance. There can be no assurance that we will be successful in our efforts to arrange additional financing, if needed, on terms satisfactory to us. If additional financing is raised by the issuance of Common Shares from treasury our control may change and our shareholders may suffer additional dilution. From time to time we may enter into transactions or expend funds in a manner which may be financed partially or wholly with debt and may increase our debt levels above industry standards.

## **Interest Rates**

An increase in interest rates may result in increased costs of borrowing for us on both existing and future debt instruments or credit facilities and such increased costs would negatively affect our operating results. We are also exposed to interest rate risk arising from the difference between the repricing dates of Bank West's assets and liabilities. The differentials, or interest rate gaps, arise as a result of the differences in term preferences of borrowers and depositors. A positive interest rate gap exists when interest sensitive assets exceed interest sensitive liabilities for a specific repricing period. A positive gap would result in decreased interest income when market interest rates fall because assets are repricing earlier than liabilities. Rising market interest rates have the opposite effect. The effect of an interest rate gap and changing market interest rates may have a negative affect on Bank West's results of operation and financial condition.

## **Investment Risk**

Investment risk is the exposure to investment loss from general economic and stock market fluctuations. We have invested a significant amount of our excess working capital in preferred shares of Canadian corporations rated "Pfd-1" and "P1" and "Pfd-2" and "P2" by Dominion Bond Rating Services or Standard & Poor's, a division of The McGraw-Hill Companies Inc., respectively. Bank West has invested in government and corporate bonds and securities. A significant decline in the value or yields of these securities that we own could have a material adverse effect on our business, results of operations and financial condition. Our ability to achieve our investment objectives is affected by general economic conditions that are beyond our control. These investments are subject to the risk, among others, that the financial condition of issuers in which we invest may become impaired or the general condition of the stock market deteriorates. We may experience losses as a result of this risk and any such losses may be significant.

## **Credit Risk**

We are exposed to credit risk with respect to our marketable securities, accounts receivable and mortgages and loans receivable. We only invest in Canadian corporations and institutions with large capitalization to reduce credit risk, however, changing economic conditions or the change in the financial condition of the issuer of the securities can result in increased defaults by the issuer whose securities we own. Credit risk associated with our accounts receivable is minimized by our large and diverse customer base, which covers all consumer and business sectors in Western Canada. However, we cannot ensure that our debtors will pay our accounts receivable on a timely basis or at all which could have a material adverse effect on our results of operations and financial condition. Credit risk associated with Bank West's mortgages and loans is mitigated through conservative underwriting policies, charges against real property and mortgage insurance, however, we cannot ensure that Bank West's debtors will pay these loans or mortgages on a timely basis or at all or that any associated security will be sufficient to cover the amount of any indebtedness. As a result, failure to repay these amounts could have a material adverse effect on our results of operations or financial condition.

## **Regulation**

Our insurance and investments operations depend on our continued good standing under the licenses and approvals pursuant to which we operate. In all jurisdictions, the applicable licensing laws and regulations are subject to amendment or interpretation by regulatory authorities, and generally such authorities are vested with relatively broad and general discretion as to the granting, renewing and revoking of licenses and approvals. There can be no assurance that we will be able to obtain or retain all required licenses or that the cost of complying with these regulations will not increase. Any increase in the cost of complying

with government regulation will have a negative effect on our operating results, as will the loss or inability to obtain any material license required to operate the business.

Changes to laws or regulations, including the adoption of generous consumer protection measures or other initiatives regarding contingent or other commissions or rates charged for automobile insurance or claims-handling procedures, could materially adversely affect our business, results of operations and financial conditions.

Bank West and Western Life could be subject to regulatory actions, sanctions and fines if a regulatory authority believed it had failed to comply with any applicable law or regulation.

Where the Superintendent is concerned about an unsafe course of conduct or an unsound practice in conducting the business of a bank or a federal insurance company, the Superintendent may direct the bank or insurance company to refrain from a course of action or to perform acts necessary to remedy the situation. The Superintendent may, in certain circumstances, take control of the assets of a bank or insurance company or take control of the bank or insurance company.

More restrictive laws, rules or regulations may be adopted in the future that could make compliance more difficult and/or expensive. Specifically, recently adopted legislation addressing privacy issues, among other matters, is expected to lead to additional regulation of the insurance industry in the coming years, which could result in increased expenses or restrictions on our operations.

The revenue we generate from the sale of automobile insurance policies represents a significant portion of our overall revenues. As a result, any action by government authorities to change the nature of the automobile insurance industry in our markets could affect our commission levels and our revenues.

### **Nature of our Business**

Our fixed costs (including costs associated with salaries and employee benefits and bonuses, depreciation and amortization, and interest expense and principal repayments), account for a significant portion of our costs and expenses. As a result, low productivity resulting from lower demand or other factors or a decrease in the premium rates, volume and commission paid in the segments of the P&C insurance industry in which we operate could have a material adverse effect on our business, financial condition and results of operations.

Brokers distribute insurance policies underwritten by P&C insurance companies. Some P&C insurance companies offer their products through dedicated, captive sales organizations. If the number of such P&C insurance companies increases, our revenues may decrease, which decrease could have a material adverse effect on our business, financial condition and results of operations.

### **Insurance Products**

Our operations and success depend in part upon access to products sold by Canadian and international insurance companies. Our existing brokerage contracts with certain insurance companies do not have a set term or expiry date, but may be terminated by either party on between 90-120 days' written notice, depending on the specific contract. To reduce this risk, we have entered into business development agreements with a number of major Canadian insurance companies. Our ability to carry on business is dependent on our continuing ability to attract and maintain relationships with these insurance companies. However, other than pursuant to these agreements, there can be no assurance that we will continue to have access to such insurance products.

An inability to maintain or obtain access to insurance products would have a negative impact on us. Although we can obtain replacement business for departing insurance companies, the loss of such business, particularly of a major current provider, could have a material adverse effect on our business, financial condition and results of operations.

Further, any significant decrease in the premium rates, volume or basic or contingent commissions paid in the segments of the insurance industry in which we operate can adversely impact us.

### **Competition**

We face competition from the estimated 800 independent brokers delivering P&C and life insurance products in rural Western Canada. We also face competition from certain P&C insurance companies, including some owned by Canadian chartered banks, who distribute their products directly to consumers. In addition, Canadian chartered banks pose a potential competitive threat as they are attempting to obtain the legal right to sell insurance at their branches to compete directly with insurance companies and brokers. There are also a number of companies operating in the P&C insurance brokerage industry in Canada that compete with us, including Hub International Limited, Anthony Clark International Insurance Brokers Ltd. and Canada Brokerlink Inc. We also face competition from banks, financial planners and other financial service providers in the sale of non-P&C insurance products. We, in general, also face future competition from financial institutions which deliver or are preparing to deliver financial services and insurance products and services by electronic means, most notably through the Internet.

Competition is intense in all of our business lines and in every insurance market. We believe that most of our competition in P&C insurance is from numerous local and regional brokerage firms that focus primarily on middle-market businesses and, to a lesser extent, from larger national brokerage firms. In addition, insurance companies compete with us by directly soliciting customers without the assistance of an independent broker or agent. Weak economic growth, as well as rising P&C insurance rates may exacerbate those various competitive pressures as some of our customers may choose to cut back or eliminate various types of coverage, or choose to seek competitive quotes from other brokers.

Some of our competitors have greater financial and other resources than we do and therefore no assurance can be given that we will be successful in such a competitive environment.

### **Dependence on Key Personnel**

Our success is largely dependent on the performance of our key employees and senior management. Failure to retain our key employees or to attract and retain additional key employees with necessary skills could have a materially adverse impact on our growth and profitability. There can be no assurance that we will be able to engage the services of such personnel or retain our current personnel.

### **Errors and Omissions Claims**

We have extensive operations and are subject to claims and litigation in the ordinary course of business resulting from alleged errors and omissions in placing insurance and handling claims. The placement of insurance and the handling of claims involve substantial amounts of money. Since errors and omissions claims against us may allege our potential liability for all or part of the amounts in question, claimants may seek large damage awards and these claims can involve significant defence costs. Errors and omissions could include, for example, our employees or sub-agents failing, whether negligently or intentionally, to place coverage or file claims on behalf of customers, to appropriately and adequately disclose insurer fee arrangements to our customers, to provide insurance providers with complete and accurate information relating to the risks being insured or to appropriately apply funds that we hold for

our customers on a fiduciary basis. It is not always possible to prevent or detect errors and omissions, and the precautions we take may not be effective in all cases.

Our business, financial condition and/or results may be negatively affected if in the future our errors and omissions insurance proves to be inadequate or unavailable. In addition, errors and omissions claims may harm our reputation or divert management resources away from operating our business.

### **Unpredictable Catastrophic Events**

Catastrophes can be caused by various natural and unnatural events. Natural catastrophic events include hurricanes, windstorms, earthquakes, hailstorms, explosions, severe winter weather and fires. Unnatural catastrophic events include hostilities, terrorist acts, riots, crashes and derailments. The incidence and severity of catastrophes are inherently unpredictable. Most catastrophes are restricted to small geographic areas; however, hurricanes, windstorms and earthquakes may produce significant damage in large, heavily populated areas. Catastrophes can cause losses in a variety of P&C insurance lines, including business interruption, business personal property and workers' compensation. It is possible that a catastrophic event or multiple catastrophic events could have a material adverse effect upon contingent commissions we would expect to receive from a P&C insurer that experienced significant losses, which could have a material adverse effect on our net income and financial condition.

### **Changes in the Business and Economic Environment**

Our business and results can be significantly affected by changes in the business and economic environment, including: changes in the level of demand for P&C insurance; price competition and variation in other terms and conditions of trade; increases in the supply of P&C insurance as a result of new capital provided by recent or future market entrants or by existing P&C insurers; volatile and unpredictable developments (including catastrophes); fluctuations in interest rates and/or price competition. The P&C insurance industry historically has experienced pricing and profitability cycles related to levels of industry underwriting capacity. As a consequence of fluctuations in pricing and P&C insurer profitability we may suffer declines in both basic and contingent commissions which could have a material adverse effect on our net income and financial condition.

### **Failure of Computer and Data Processing Systems**

Our business is dependent upon the successful and uninterrupted functioning of our computer and data processing systems. The failure of these systems could interrupt our operations or materially impact our ability to rapidly evaluate and commit to new business opportunities. If sustained or repeated, system failures could result in the loss of existing or potential business relationships or could negatively affect our financial results.

### **Industry Growth**

We are subject to, and dependent on, fluctuations within the P&C insurance industry and the P&C insurance brokerage industry. Historically, direct written premiums in the P&C insurance industry in Western Canada have grown faster than in the rest of Canada. There can be no assurance that such growth will continue or if it does, will continue at the same rate.

### **Covenants of the Company**

In connection with our ongoing business activities, we have made and may make commitments to lenders, bondholders and regulatory authorities that may limit our flexibility to make, or influence, certain

business decisions concerning the payment of dividends or the amount of dividends, raising capital, making acquisitions, and incurring additional debt. We believe that these commitments are or would be comparable to those made by similar businesses to our own.

### **Pricing Risk**

Pricing of life and health insurance policies involves estimates and assumptions of such factors as mortality, morbidity, future investment yields, expenses and surrenders. Pricing risk is the risk that the actual experience will not develop as estimated. Management of pricing risk involves careful product design, extensive use of modeling and sensitivity testing as well as monitoring through experience studies. Despite management of these risks, there can be no guarantee that actual experience will not differ from the assumptions made in the pricing of the insurance products of Western Life from time to time. Western Life manages this risk through comprehensive underwriting and claims payment guidelines. In addition, reinsurance is used to mitigate exposure to individual lives or benefits. Western Life's maximum retentions are subject to board approval.

### **Reinsurance Risk**

Western Life focuses on minimizing the credit risk associated with its reinsurance agreements by partnering with reinsurers with strong credit ratings. Western Life regularly evaluates the financial condition of its reinsurers, monitors the concentration of credit risk and, where possible, obtains security to support the reinsurance obligations. Accordingly, Western Life currently purchases approximately 95% of its reinsurance from three highly-rated reinsurance companies, who are rated "A" or higher by A.M. Best. The concentration of Western Life's reinsurance with three partners increases the impact upon Western Life's financial condition and results of operations if one or more of its reinsurers defaults on its reinsurance obligation. Although all of Western Life's reinsurers were rated "A-" or higher by A.M. Best at the time of entering into the reinsurance arrangements, these ratings are subject to change and may be lowered.

Although reinsurance makes the assuming reinsurer liable to Western Life to the extent of the risk ceded, Western Life is not relieved of its primary liability to its policyholders. We cannot ensure that Western Life's reinsurers will pay all reinsurance claims on a timely basis or at all. Western Life evaluates each reinsurance claim based on the facts of the case, historical experience with the reinsurer or similar past claims and existing law and includes any amounts deemed uncollectible in its reserves for uncollectible reinsurance.

The inability to collect amounts due to Western Life under reinsurance arrangements could have a significant adverse effect on its results of operations and financial condition.

### **Regulatory Risk**

The life and health insurance business is subject to extensive levels of regulation on matters such as rate-setting, risk-based capital and solvency standards, restrictions on types of investments, the maintenance of adequate reserves for unearned premiums and unpaid claims, examinations, licensing of insurers and agents and limitations on dividends and transactions with affiliates. Changes in the law or regulations, or in government policies, could materially and adversely affect the business and operations of Western Life. In particular, insurance regulators in Canada have given greater emphasis in recent years to the investigations of improper life insurance pricing and sales practices by life and annuity insurers.

Western Life is required to maintain adequate regulatory capital in relation to its operations. These ratios can be adversely affected by changes in business conditions beyond Western Life's control, such as a decline in the stock market or interest rate spreads.

There have been developments in the life insurance industry over the past year similar to developments in the P&C insurance industry where insurers have been requested to provide detailed information on their compensation practices and their relationships with brokers who sell their products. While we are not able to predict whether these recent developments will result in additional regulatory restrictions, such restrictions, if any, could include increased disclosure obligations or limitations on commission practices. Onerous restrictions could adversely affect Western Life's ability to conduct business and add significantly to the cost of conducting business thereby adversely affecting its results of operations or financial conditions.

### **Interest Rate Risk**

Western Life's financial position may be affected by its exposure to interest rate risk. Interest rate risk is the risk of economic losses or gains arising from the reinvestment of cash flows or sale of assets. If the cash flows from assets supporting the policy liabilities do not match the timing and amount of the policy cash flows, interest rate losses or gains may occur.

### **Credit Risk**

Western Life is exposed to credit risk with respect to its investments. Exposure to credit loss is managed through compliance with investment policy standards for quality ratings, maximum single issuer guidelines, diversification of type and location of properties and, for mortgages and real estate, independent borrower and appraisal reviews. These investments are subject to the risk, among others, that the financial condition of issuers in which Western Life invests may become impaired. Accordingly, while compliance with such policies is measured frequently, Western Life may still experience losses as a result of this risk which could have a material adverse effect on its results of operations or financial condition.

### **Investment Risk**

Investment risk is the exposure to investment loss from general economic and stock market fluctuations. Western Life's ability to achieve its investment objectives is affected by general economic condition that are beyond its control. Western Life's asset mix guidelines identify limits on the amount and quality of equity investments to mitigate this loss. While compliance with this limitation is measured frequently, these investments are subject to the risk, among others, that the financial condition of issuers in which Western Life invests may become impaired or the general condition of the stock market deteriorates. Western Life may still experience losses as a result of this risk and any such losses may be significant.

### **Competition Risk**

The insurance business that Western Life engages in is highly competitive. Western Life's products compete not only with those offered by other insurers, but in many cases also with those offered by mutual funds, banks and other providers. Insurers compete on the basis of pricing and terms, service provided to distribution channels and policyholders and claims paying financial strength ratings. Many of Western Life's competitors are large well-capitalized financial services companies with significantly more resources than Western Life and therefore no assurance can be given that Western Life will be successful in such a competitive environment.

## **Risks with Respect to Financial Strength Ratings**

Ratings with respect to claims-paying ability and financial strength are an important factor in establishing the competitive position of insurance companies. Ratings are influential in maintaining public confidence in Western Life and its ability to market its products. Rating organizations continually review the financial performance and condition of insurers, including Western Life. Downgrades or negative outlooks with respect to the ratings of Western Life could, among other things, increase surrender levels, adversely affect relationships with distributors of Western Life's products and services, negatively impact persistency, adversely affect Western Life's ability to market its products and thereby materially and adversely affect Western Life's liquidity and in some cases its business, financial condition and results of operations.

## **TRANSFER AGENT AND REGISTRAR**

Western's transfer agent and registrar is Computershare for all its securities with offices in Calgary and Toronto.

## **MATERIAL CONTRACTS**

Our material contracts that were entered into during the most recently completed financial year or contracts entered into prior thereto which are still material and in effect, other than contracts entered into in the ordinary course of business is the 2006 Underwriting Agreement.

Pursuant to the terms of the 2006 Underwriting Agreement, we sold an aggregate of 7,590,000 Common Shares to the Underwriters at a purchase price of \$3.50 per Common Shares for total gross proceeds of approximately \$26.6 million. In consideration of the services provided, we paid the Underwriters a fee of \$0.21875 per Subscription Receipt issued for an aggregate fee of \$1,660,313, which was paid in full on completion of the offering. We also agreed that, subject to certain exceptions, we would not offer or sell any of our securities for a period of 90 days subsequent to the closing of the offering of Common Shares without the consent of the Underwriters.

Particulars of each of this contract are disclosed elsewhere in this Annual Information Form. See "Development of the Business - History".

## **INTERESTS OF EXPERTS**

As at the date hereof, the partners and associates of PricewaterhouseCoopers LLP, the auditors of the Corporation, as a group, did not beneficially own any of the outstanding Common Shares or Debentures.

## **DOCUMENTS INCORPORATED BY REFERENCE**

Documents incorporated by reference in the Annual Information Form can be found on SEDAR under our profile at [www.sedar.com](http://www.sedar.com).

## **ADDITIONAL INFORMATION**

Additional information, including directors' and officers' remuneration and indebtedness, principal holders of our securities, options to purchase securities and interests of insiders in material transactions, where applicable, is contained in our Information Circular for our most recent annual meeting of shareholders that involved the election of directors. Also, additional financial information is included in our Consolidated Financial Statements and MD&A for the year ended December 31, 2006, which are

included in our 2006 Annual Report as filed with the applicable Canadian regulatory authorities. These documents are available on SEDAR at [www.sedar.com](http://www.sedar.com) and may also be obtained without charge by writing to our Corporate Secretary at 1010 - 24 Street West, High River, Alberta, T1V 2A7.

## **SCHEDULE "A"**

### **AUDIT COMMITTEE TERMS OF REFERENCE**

The Audit Committee (the "Committee") of the Board of Directors (the "Board") of Western Financial Group Inc. (the "Corporation") shall have the oversight responsibility, authority and specific duties as described below.

#### **Composition**

The Committee will be comprised of three or more directors as determined by the Board, none of whom shall be or shall have been, unless the period prescribed by applicable securities rules or regulations has elapsed since the end of service or employment, an officer or employee of the Corporation or any subsidiary of the Corporation. Each Committee member shall satisfy the independence, financial literacy and experience requirements of applicable securities laws, rules or guidelines, any applicable stock exchange requirements or guidelines and any other applicable regulatory rules. Determinations as to whether a particular director satisfies the requirements for membership on the Committee shall be made by the full Board.

Members of the Committee shall be appointed by the Board. Each member shall serve until his successor is appointed, unless he shall resign or be removed by the Board or he shall otherwise cease to be a director of the Corporation. The Board shall fill any vacancy if the membership of the Committee is less than three directors.

The Chair of the Committee may be designated by the Board or, if it does not do so, the members of the Committee may elect a Chair by vote of a majority of the full Committee membership.

#### **Communication, Authority to Engage Advisors and Expenses**

The Committee shall have access to such officers and employees of the Corporation, the Corporation's external auditor and to such information respecting the Corporation, as it considers to be necessary or advisable in order to perform its duties and responsibilities.

The Committee provides an avenue for communication, particularly for outside directors, with the external auditor and financial and senior management and the Board. The external auditor shall have a direct line of communication to the Committee through its Chair and shall report directly to the Committee. The Committee, through its Chair, may directly contact any employee in the Corporation as it deems necessary, and any employee may bring before the Committee, on a confidential basis, any matter involving the Corporation's financial practices or transactions.

The Committee has the authority to engage independent counsel and other advisors as it determines necessary to carry out its duties and to set the compensation for any such counsel and advisors. Any engagement of independent counsel or other advisors is to be at the Corporation's expense.

The Corporation shall be responsible for all expenses of the Committee that are deemed necessary or appropriate by the Committee in carrying out its duties.

#### **Meetings and Record Keeping**

Meetings of the Committee shall be conducted as follows:

1. the Committee shall meet at least four times annually at such times and at such locations as the Chair of the Committee shall determine, provided that meetings shall be scheduled so as to permit timely review of the quarterly and annual financial statements and reports. The external auditor or any two members of the Committee may also request a meeting of the Committee. The Chair of the Committee shall hold *in camera* sessions of the Committee, without management present, at every meeting;
2. the quorum for meetings shall be a majority of the members of the Committee, present in person or by telephone or by other telecommunication device that permits all persons participating in the meeting to hear each other;
3. if the Chair of the Committee is not present at any meeting of the Committee, one of the other members of the Committee who is present at the meeting shall be chosen by the Committee to preside at the meeting;
4. the Chair shall, in consultation with management and the external auditor, establish the agenda for the meetings and instruct management to ensure that properly prepared agenda materials are circulated to the Committee with sufficient time for study prior to the meeting;
5. every question at a Committee meeting shall be decided by a majority of the votes cast;
6. the President and Chief Executive Officer and the Senior Vice President, Finance and Administration and Chief Financial Officer shall be available to advise the Committee, shall receive notice of meetings and may attend meetings of the Committee at the invitation of the Chair of the Committee. Other management representatives may be invited to attend as necessary; and
7. a Committee member, or any other person selected by the Committee, shall be appointed at each meeting to act as secretary for the purpose of recording the minutes of each meeting.

The Committee shall provide the Board with a summary of all meetings together with a copy of the minutes from such meetings. Where minutes have not yet been prepared, the Chair shall provide the Board with oral reports on the activities of the Committee. All information reviewed and discussed by the Committee at any meeting shall be referred to in the minutes and made available for examination by the Board upon request to the Chair.

### **Responsibilities**

The Committee is part of the Board. Its primary functions are to assist the Board in fulfilling its oversight responsibilities with respect to: (i) the oversight, review and approval of the financial statements and the accounting and financial reporting processes of the Corporation; (ii) the assessment of the system of internal controls that management has established; and (iii) the external audit process. In addition, the Committee shall assist the Board, as requested, in fulfilling its oversight responsibilities with respect to (i) financial policies and strategies; (ii) financial risk management practices; and (iii) transactions or circumstances which could materially affect the financial profile of the Corporation.

The Committee shall be directly responsible, in its capacity as a committee of the Board, for recommending to the Board the appointment of the external auditor and the compensation and retention of the external auditor and overseeing the work of the external auditor and the relationship of the external

auditor with the Corporation (including the resolution of disagreements between management and the external auditor regarding financial reporting).

The Committee should have a clear understanding with the external auditor that they must maintain an open and transparent relationship with the Committee, and that the ultimate accountability of the external auditor is to the shareholders of the Corporation.

### **Specific Duties**

#### **A. Relationship with External Auditor**

The Committee shall:

1. consider and make a recommendation to the Board as to the appointment or re-appointment of the external auditor for the purpose of preparing or issuing an auditor's report or performing other audit, review or attest services, ensuring that such auditor is a participant in good standing pursuant to applicable securities laws;
2. consider and make a recommendation to the Board as to the compensation of the external auditor which is to be paid by the Corporation;
3. oversee the work of the external auditor in performing their audit, review or attest services and oversee the resolution of any disagreements between management of the Corporation and the external auditor regarding financial reporting;
4. review and discuss with the external auditor all significant relationships that the external auditor and its affiliates have with the Corporation and its affiliates in order to determine the external auditor's independence;
5. as may be required by applicable securities laws, rules and guidelines, either:
  - (a) pre-approve all non-audit services to be provided by the external auditor to the Corporation (and its subsidiaries, if any), or, in the case of *de minimus* non-audit services, approve such non-audit services prior to the completion of the audit; or
  - (b) adopt specific policies and procedures for the engagement of the external auditor for the purposes of the provision of non-audit services; and
6. review and approve the hiring policies of the Corporation regarding partners and employees and former partners and employees of the present and former external auditor of the Corporation.

#### **B. Financial Statements and Financial Reporting**

The Committee shall:

1. review with management and the external auditor, and recommend to the Board for approval, the annual financial statements of the Corporation and related annual financial reporting, including management's discussion and analysis and earnings press releases. In particular, the Committee's review of such financial statements should include, but not be limited to:

- (a) reviewing changes in accounting principles, or in their application, which may have a material effect on the current or future years' financial statements;
  - (b) reviewing significant accruals, reserves or other estimates;
  - (c) reviewing the accounting treatment of unusual or non-recurring transactions;
  - (d) the adequacy of the Corporation's asset retirement obligations;
  - (e) reviewing disclosure requirements for commitments and contingencies; and
  - (f) related party transaction reporting and accounting;
2. upon completion of each audit, review with the external auditor the results of such audit. This process should include but not be limited to reviewing:
- (a) the scope and quality of the audit work performed;
  - (b) the capability of the Corporation's financial personnel;
  - (c) the co-operation received from the Corporation's financial personnel during the audit;
  - (d) the internal resources used;
  - (e) significant transactions outside of the normal business of the Corporation; and
  - (f) significant proposed adjustments and recommendations for improving internal accounting controls, accounting principles or management systems;
3. review with management and the external auditor, and recommend to the Board for approval, the interim financial statements of the Corporation and related interim financial reporting, including management's discussion and analysis and earnings press releases;
4. review with management and recommend to the Board for approval, the Corporation's annual information form;
5. consider and be satisfied that adequate policies and procedures are in place for the review of the Corporation's public disclosure of financial information extracted or derived from the Corporation's financial statements (other than public disclosure referred to in clauses B.1 and B.3 above), and periodically assess the adequacy of such procedures;
6. review the proceedings of the audit committee meetings of certain of its subsidiaries; and
7. review accounting, tax, legal and financial aspects of the operations of the Corporation as the Committee considers appropriate.

C. Internal Controls

The Committee shall:

1. review with management and the external auditor, the adequacy and effectiveness of the internal control and management information systems and procedures of the Corporation (with particular attention given to accounting, financial statements and financial reporting matters) and determine whether the Corporation is in compliance with applicable legal and regulatory requirements and with the Corporation's policies;
2. establish procedures for the receipt, retention and treatment of complaints, submissions and concerns regarding accounting, internal controls or auditing matters and the confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters; and
3. review annually expenses submitted for reimbursement by the Chairman of the Board and the President and Chief Executive Officer of the Corporation.

The Chairman of the Audit Committee will attend the Audit Committee meetings of the subsidiaries of the Corporation.

D. Financial Risk Management

The Committee may, if requested by the Board, review the appropriateness and effectiveness of the Corporation's policies and business practices which impact on the financial integrity of the Corporation, including those relating to accounting and management reporting. The Committee may, if requested by the Board, also review the financial risks arising from the Corporation's exposure to such things as interest rates, financial markets, foreign currency exchange rates and credit, the Corporation's insurance program and tax or governmental audits and report the results of such reviews to the Board for the purpose of assisting the Board in identifying principal business risks associated with the businesses of the Corporation.