



# **Economical Insurance**

A member of The Economical  
Insurance Group

## **NOTICE AND MANAGEMENT PROXY CIRCULAR FOR THE ANNUAL AND SPECIAL MEETING OF MEMBERS OF ECONOMICAL MUTUAL INSURANCE COMPANY TO BE HELD ON MAY 26, 2011**

Your Board of Directors has made significant progress towards demutualizing Economical and has a sound plan for its future. As a Member of Economical, the significant value obtained under a demutualization belongs to you, and your current Board will pass this value on to you.

A group led by an outside party called VC & Co. has brought forward proposals which can do nothing more than delay or derail this process, in part by replacing the Board with VC & Co.'s hand-picked nominees. This is a change with no purpose and if the Board is replaced, VC & Co. will attempt to divert significant value out of Economical, and into its own pockets. **This will cost you money.**

**Please read the accompanying letter and this circular carefully. Then ask yourself "who do you trust" to carry out the demutualization of Economical.**

**Vote for Economical's director nominees.**

**Vote against VC & Co.'s proposal to replace the current Board.**

**This Management Proxy Circular solicits BLUE Proxies in  
favour of Management**

**If you have any questions,  
or require assistance in voting your BLUE Proxy,  
please call:**

**Georgeson**

**TOLL FREE – 1-866-909-6468**

**DATED APRIL 11, 2011**

***YOUR VOTE IS EXTREMELY IMPORTANT. VOTE ONLY THE BLUE PROXY.  
For questions or assistance, please call Georgeson at 1-866-909-6468.***

# MANAGEMENT PROXY CIRCULAR

## QUESTIONS AND ANSWERS

### 1) Why is this Meeting important?

The Annual and Special Meeting on May 26, 2011 will determine the future course of Economical at a critical time in its development. On December 14, 2010, the Board announced its intention to demutualize and since then it has made significant progress towards this goal, as we have been reporting to you. Demutualization will make Economical stronger and more competitive by removing the restrictions the mutual structure imposes with respect to access to capital markets. The Board believes demutualization will allow Economical to realize the significant value built up in it for the mutual policyholders ("Members") in the form of cash, shares or both. (More information on demutualization is provided in this Circular).

At this Meeting, you will choose between Economical's director nominees to the Board, who are leading the demutualization project, and an outside group of director nominees selected by VC & Co. Advisory Limited ("VC & Co."), an affiliate of a Toronto-based law firm and its associated company whose primary business is "shareholder activism".

That choice will determine who will lead the demutualization effort and who you entrust to protect your interests under the demutualization and in supervising the ongoing business of Economical.

As discussed more fully in this Circular, Economical believes that there is a real risk that a new board, hand-picked by VC & Co. and inexperienced in the affairs of Economical, will be swayed by the wishes of VC & Co. to act in the best interests of VC & Co. Additionally, VC & Co. has indicated that if its director nominees are elected, it will request that they cause Economical to pay significant fees and reimburse expenses to VC & Co. – effectively reducing each Member's value in Economical.

## THE QUESTION IS THIS – WHO DO YOU TRUST TO CONDUCT ECONOMICAL'S DEMUTUALIZATION?

### 2) What is a demutualization and what does it mean for mutual policyholders?

Demutualization is a process whereby a mutual insurance company (such as Economical) converts from a company with its mutual policyholders as its sole voting members, to a corporation with share capital and shareholders, and distributes the proceeds of such conversion, in the form of cash or transferable shares, to its Members. The Board expects that, in the case of Economical, significant value will be transferred to Members.

### 3) What am I being asked to vote on?

You are being asked to vote on the usual business of the annual meeting: the election of directors and the appointment of auditors. Management of Economical recommends that you vote for the election of its nominees: David A. MacIntosh, Karen L. Gavan and John H. Bowey and vote for the appointment of Ernst & Young LLP as auditors. However, this year will be different from previous years since you will also be asked to vote on resolutions proposed by Dissident Members led by an activist third party (VC & Co.) who wants to remove the entire Board and replace it with the activist's own nominees. Management of Economical recommends that you vote against these resolutions.

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#### **4) Who are the Dissidents and what is VC & Co. Advisory Limited?**

The Dissidents are a relatively small group of Members who signed irrevocable agreements with VC & Co. giving VC & Co. the power to act on their behalf to seek changes at Economical in return for a substantial share of any proceeds the Dissidents receive from Economical as result of a demutualization or other transaction.

VC & Co. is an affiliate of a Toronto-based law firm and an associated company whose primary business is “shareholder activism”. VC & Co. has pursued the business of shareholder activism with VC & Co.’s activities against Economical.

#### **5) Does VC & Co. have a Conflict of Interest?**

Yes, we believe so. The principals of VC & Co. acted as legal counsel for The Westaim Corporation (“Westaim”) when it made an unsolicited approach to Economical. Westaim sought to acquire control of or assets of Economical, presumably at the lowest price possible. If Westaim were to be successful in acquiring Economical for the lowest price, Members would receive (directly or indirectly) less value as a result of such a transaction than if a more competitive price were obtained for Economical or its assets – which your Board is actively seeking as part of its demutualization process. There seems to be an obvious conflict between VC & Co. recently working with Westaim in the hopes of acquiring an interest in Economical or its assets for the lowest price, and VC & Co.’s current position, which is that it is working with the Dissidents to obtain, one presumes, the greatest value (price) for Economical.

#### **6) What is the Dissident Proposal?**

The Dissident Proposal seeks Member support for one purpose – which your Board opposes: to remove the entire Board and replace it with nominees selected by VC & Co. The Dissident Proposal does not indicate the Dissidents’ or VC & Co.’s intentions for Economical or demutualization.

VC & Co. stands to make millions of dollars in fees whether or not it succeeds in replacing the Board. VC & Co. has stated that, if the Dissident Proposal succeeds, it will seek to have its hand-picked Board direct Economical to pay millions in fees and expenses which many of the Dissidents have personally agreed to pay VC & Co. The fee is a substantial 12.5% of their proceeds from any action taken by Economical over the next six years, except normal course premium refunds and claims payments. If the Dissident Proposal succeeds, this would effectively extend the liabilities of a minority of Members to all mutual policyholders who would have to pay for VC & Co.’s fees and expenses, whether or not they support the Dissident Proposal. We believe this inequity indicates how VC & Co. would expect its Board to approach its responsibilities to Members. At the very least, this will decrease the value of Economical and what will be paid to you upon completion of the demutualization.

#### **7) What is the ultimate goal of the Dissident Proposal?**

The Dissident Proposal is led by VC & Co. and is ultimately designed to give VC & Co. and the Dissidents great influence over a new board.

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**8) Why does Management recommend that you vote against the Dissident Proposal?**

Replacing your Board would be a change with no purpose. Your Board has already made significant progress towards demutualization and changing the Board now, would delay, or possibly derail, demutualization.

Your current Board has specific and proven experience with regard to Economical that a new Board will not have.

VC & Co. is not a policyholder in Economical but stands to obtain large fees if the Board is replaced. It intends to dilute the value of your interest in Economical in pursuit of its fees.

VC & Co. has previously worked closely with parties that continue to be interested in acquiring Economical - for a low price. The value of your interest in Economical would suffer under a cheap sale. If VC & Co.'s hand-picked board controls Economical, there is a risk that the new board will be loyal to VC & Co.'s previous partners, and less so to Economical's Members.

**9) How do I avoid paying any fees to VC & Co.?**

By electing each of Economical's director nominees at the Meeting, you will ensure that neither Economical nor you (indirectly or otherwise) will pay any fees or expenses to parties such as VC & Co. (so long as you have not personally signed an agreement with VC & Co.).

**10) Who are the nominees selected by VC & Co. to replace the Board?**

As of the date of this Circular VC & Co. has not disclosed who its nominees would be. Therefore, we cannot comment on whether they are appropriate, independent, or have the relevant experience to serve as directors of Economical. We do know that they will be selected by VC & Co. on behalf of the Dissidents and that there can be no assurance that they will not be swayed by the wishes of VC & Co., which may not necessarily be in the best interests of all Members or Economical.

**11) What is the Board's recommendation on voting?**

The Board recommends that Members:

VOTE FOR the election of each of Economical's director nominees;

VOTE FOR the appointment of auditors; and

VOTE AGAINST the resolutions of the Dissident Proposal that would replace the Board with the Dissident nominees.

The Board believes that the Dissident Proposal is not in the best interests of Members or Economical and has provided its reasons in this Circular. In summary, changing the Board at this time will only delay or derail a demutualization process that is already underway. Additionally, the day-to-day business operations and profitability of Economical may suffer under a new Board, inexperienced in the affairs of Economical – reducing the value of your interest in Economical.

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## **12) How do I complete and submit the Proxy?**

The Board recommends that you complete the form of proxy by VOTING FOR the election of the directors nominated by the Board, VOTING FOR the appointment of the auditors and VOTING AGAINST the ouster of the current directors of Economical.

**Please indicate these choices with a checkmark in the appropriate box on the enclosed form of proxy and complete the information required thereon.** A completed sample form of proxy has been enclosed with this package showing how your Board recommends you vote. Please refer to the sample proxy to see how your proxy should be completed. In order to be valid, the BLUE form of proxy must be received by Computershare by mail or in person at 100 University Avenue, 9<sup>th</sup> Floor, Toronto, ON, M5J 2Y1, or by fax, at 1-866-249-7775 (toll free in North America), 416-263-9524 (International) no later than 1:00 p.m. (Eastern Time) on May 16, 2011. Your blue proxy may also be deposited at the head office of Economical at 111 Westmount Road, Waterloo, Ontario no later than 1:00 p.m. (Eastern Time) on May 16, 2011. If you wish to return the form of proxy by mail you may use the postage paid envelope included with this Circular, or call Georgeson at 1-866-909-6468 who will arrange to have your completed proxy picked up by courier.

## **13) Why is the Board recommending against the Dissident Proposal?**

The Board believes that it is in the best interests of Economical and its Members for Economical's experienced and proven Board to lead the demutualization and these directors have already made substantial progress towards demutualization. Simply put, demutualization is too important to be placed in the hands of Dissident nominees whose expertise, independence, intentions and commitment to the Company are unknown. Replacing your directors will delay and possibly derail the demutualization, and the payment of demutualization benefits to you.

## **14) Why did you go to court about the Dissident Proposal?**

We sought a court ruling on the legality of the Dissident Proposal under the *Insurance Companies Act*, since Economical has not faced a similar situation in its 140-year history. The Board had real concerns about the legality of the Dissident Proposal, some of which were validated by the court. Seeking legal clarity is part of the Board's responsibility to protect the interests of Economical and the Members. As a result, one of the Dissident Proposals was rejected and need not be considered at the Meeting and is not discussed herein.

## **15) Why are you suing the former Chief Financial Officer?**

We have filed a statement of claim against the former CFO alleging misappropriation of funds and breach of fiduciary duty to Economical. An investigation of his activities revealed he had been secretly dealing with Westaim, a company that owns a competing insurer (sharing confidential information about Economical and plotting to oust Economical's directors), and which had approached Economical about a potential transaction. Westaim was being represented in this activity by the principals of VC & Co. The former CFO had also been secretly communicating with VC & Co. before VC & Co. began, and during, its campaign to solicit Dissident Members.

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**16) Will I be voting on demutualization?**

Not yet. We cannot bring a vote on demutualization to the Members until we have a demutualization proposal approved by our regulators. This will not occur until regulations permitting demutualization are put in place by the federal government. The enactment of these regulations is the purview of the Department of Finance with whom we are working to establish these regulations. As a result of our efforts, in the Budget of March 22, 2011 it was disclosed that the Department of Finance is developing a framework for the demutualization of federally regulated property and casualty mutual insurance companies, which will provide, for companies that choose to demutualize, an orderly and transparent process and ensure that policyholders are treated fairly and equitably. The Budget stated that amendments to the *Insurance Companies Act*, including amendments that would prevent any mutual company from demutualizing indirectly, will be introduced. You will be given more information about the progress towards demutualization at the Annual and Special Meeting, but the Member vote to consider and approve the demutualization will be held at a later date.

At the Meeting, you will be voting on who you want to lead Economical through the demutualization process: the current Board you know and who knows Economical, its business and its regulators; or nominees selected by VC & Co. who have not yet been disclosed. We believe you will choose your current Board and not the VC & Co. nominees.

**17) What happens if Economical does not demutualize?**

Economical has been in business for 140 years and could continue for many more as a mutual company. However our competitiveness would be impacted by our lack of access to capital markets. The Board believes Economical can be financially stronger, more competitive, and more capable of long-term growth if these restrictions are removed through demutualization. The Board has determined that demutualization is the best strategic option for Economical and now is the time to pursue it.

**18) Some say current Members should not be entitled to any proceeds from the value accumulated within mutual insurance companies if such companies demutualize. Does that mean I may get nothing from Economical's demutualization?**

Our view – which we believe is supported by existing government policy and law – is that Members are the owners of Economical. As legitimate owners, you are entitled to all proceeds that may result from demutualization. In the case of Economical, those proceeds will be substantial, although we cannot yet determine exact amounts that would be payable to individual Members. Allocation of value among Members will be determined after the passage of regulations that permit the demutualization.

**19) Who is entitled to vote at the Meeting?**

Only mutual policyholders of Economical as of 5:00 p.m. on May 25, 2011 are entitled to vote at the Meeting.

**20) Can I still vote if I cannot attend the Meeting?**

We urge you to exercise your vote now, by returning the BLUE proxy and following the instructions on it, regardless of whether you intend to attend the Meeting in person. It is a

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simple process and your vote is extremely important. To avoid confusion, vote only the BLUE proxy and discard any materials that you may receive from the Dissidents.

**21) Should I send my proxy now even if I am attending the Meeting?**

Yes. Your vote is extremely important and the easiest way to ensure it gets properly counted is to immediately send your BLUE proxy to Computershare, or deposit it at the head office of Economical, as set out herein.

**22) Can I change my vote after I have sent in my proxy?**

Yes. You may change your vote by executing another proxy bearing a later date and depositing it as instructed herein, or by attending at the Meeting, revoking your proxy, and voting in person.

**23) Where can I get more information about voting my proxy?**

If you have any questions or need assistance in completing or returning the enclosed BLUE proxy, please call Georgeson, our proxy solicitation agent, toll free at 1-866-909-6468 or by e-mail at [askus@georgeson.com](mailto:askus@georgeson.com), or call Karen Gavan, Chair of the Special Committee of the Board of Directors of Economical at 519-570-8500 x 42997.

Further information relating to all of these issues may be obtained from Economical's web site at [www.economicalinsurance.com](http://www.economicalinsurance.com).

**The Board of Directors of Economical  
unanimously recommends that you**

- |                      |   |
|----------------------|---|
| <b>RESOLUTION 1.</b> | <b><u>VOTE FOR</u> Each of Economical's<br/>Director Nominees</b>         |
| <b>RESOLUTION 2.</b> | <b><u>VOTE FOR</u> the Appointment of<br/>the Auditors</b>                |
| <b>RESOLUTION 3.</b> | <b><u>VOTE AGAINST</u> the Ouster of All<br/>of the Current Directors</b> |

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or require assistance in voting your BLUE Proxy,  
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## REASONS TO REJECT THE DISSIDENT PROPOSALS: A SUMMARY

Economical's Board has determined that the Dissident Proposal – Resolution 3 - is not in the best interests of Members. There are compelling reasons for you to vote against the Dissident Proposal. They include:

1. **A change with no purpose.** The Dissidents, at the instigation of VC & Co., who is affiliated with a Toronto-based law firm and its associated company that is in the business of “shareholder activism”, are hoping to replace the Board with nominees selected by VC & Co. Economical is already on course for a demutualization to realize value for you. VC & Co.'s proposed change is unlikely to result in a better outcome for Members and will delay and potentially derail the demutualization and your right to receive demutualization benefits. A hand-picked VC & Co. Board, inexperienced in the affairs of Economical, could very well engage in an improvident sale of the Company: a transaction at less than fair value for Members. Members could receive less value under such a transaction, but VC & Co. would get its significant fees in any case.
2. **Change means delaying the demutualization process.** Your existing Board is already implementing its decision to demutualize Economical and has made significant progress in pushing the process forward, internally, with Economical regulators, and in the marketplace. That progress would inevitably be delayed and could be derailed by a new Board that would have to get up to speed before moving ahead.
3. **Lack of experience with Economical's business.** VC & Co. has not yet disclosed who its nominees would be, but they will not have the existing Board's detailed knowledge of Economical business. Inexperienced oversight of Economical's operations at this critical juncture could reduce the value of your Company as an operating business, and thus what you receive on demutualization (since value received on demutualization depends largely on the overall value of Economical).
4. **Your interest in Economical will be reduced by VC & Co.'s substantial fees.** VC & Co. has no interest in Economical as a policyholder but has a large financial interest in replacing the Board with its own nominees. VC & Co. is not a mutual policyholder, but stands to make millions of dollars in fees if it succeeds in taking over the Board. VC & Co. has stated that, if the Dissident Proposal succeeds, it will seek to have its hand-picked Board direct Economical to pay millions in fees and expenses which many of the Dissidents have personally agreed to pay VC & Co. The fee is a substantial 12.5% of their proceeds from any action taken by Economical over the next six years, except normal course premium refunds and claims payments. If the Dissident Proposal succeeds, this would effectively extend the liabilities of a minority of Dissident Members to all Members should Economical have to pay for VC & Co.'s fees and expenses, whether or not they support the Dissident Proposal. We believe this inequity indicates how VC & Co. would expect its Board to approach its responsibilities to Members. At the very least, this will decrease the value of Economical and what will be paid to you upon completion of the demutualization.
5. **An apparent conflict of interest at VC & Co., the leader of the Dissidents.** VC & Co.'s principals were advising Westaim, the company that proposed a transaction to merge its subsidiary JEVCO Insurance with Economical. VC & Co.'s principals were advising Westaim on how to gain control of Economical at the lowest price. Such price would not be in the best interests of Members as it would not maximize the value of Economical for Members. Yet, within days of purportedly severing ties with Westaim, VC & Co.'s principals were soliciting Members with a promise of maximizing value for the Members. This sudden switch in loyalties should be cause for concern, particularly since Westaim has continued to express an interest in acquiring Economical or its assets (and would be doing so from the VC & Co.-nominated Board if the Dissident Proposal is successful). VC & Co. did not disclose its relationship with Westaim to anyone, most importantly you, the mutual policyholders, until forced to do so in court.
6. **Secret Dealings.** An internal investigation into the activities of former Chief Financial Officer of Economical, Sandeep Uppal, indicates that both Westaim and VC& Co. were dealing with him, well before and after VC & Co. began its Dissident solicitation. These dealings were kept secret from the Board of Directors of Economical and, most importantly, from you, the mutual policyholders. Mr. Uppal has since been dismissed from his employment at Economical. Economical has filed a statement of claim against Mr. Uppal alleging misappropriation of funds, and breach of fiduciary duty to Economical in relation to these activities.

## THE QUESTION IS THIS – WHO DO YOU TRUST TO CONDUCT ECONOMICAL'S DEMUTUALIZATION?

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**For questions or assistance, please call Georgeson at 1-866-909-6468.**



**NOTICE OF ANNUAL AND SPECIAL MEETING OF MEMBERS OF  
ECONOMICAL MUTUAL INSURANCE COMPANY**

Notice is hereby given that the Annual and Special Meeting (the "Meeting") of the Members of Economical Mutual Insurance Company ("Economical") will be held on Thursday, May 26, 2011 at 1:00 p.m. at Bingemans - Marshall Hall, 425 Bingemans Centre Drive, Kitchener, Ontario, Canada, for the following purposes:

- A. to receive the consolidated financial statements for the year ended December 31, 2010 and the auditor's report on those statements;
- B. to appoint the auditor;
- C. to consider a Dissident Proposal from a group of members of Economical. The Dissident Proposal is set out on Appendix "A" to this Notice and a supporting statement related to the Dissident Proposal is set out on Appendix "B" to this Notice;
- D. to elect directors; and
- E. to transact such other business as may properly be brought before the Meeting and any adjournments thereof.

Each Member is entitled to cast one (1) vote on each matter to be brought before the Meeting.

By order of the Board of Directors,



Katherine A. Mabe  
Chief Executive Officer  
April 11, 2011

Members of Economical, whether or not you attend the Meeting, are urged to complete, date and sign the enclosed form of BLUE proxy (and ONLY the BLUE form of proxy), and return it by mail in the postage-paid envelope provided, or by hand at 100 University Avenue, 9<sup>th</sup> Floor, Toronto, ON M5J 2Y1, or fax it to Computershare Investor Services Inc. at 1-866-249-7775 (toll free in North America), 416-263-9524 (International). Blue proxies may also be returned, by hand, at the head office of Economical at 111 Westmount Road, Waterloo, Ontario. You may also call Georgeson at 1-866-909-6468 who will arrange to have your completed proxy picked up by courier. In order to be valid, the form of proxy must reach Computershare Investor Services Inc., by mail, by fax or by personal delivery at its Toronto office, or must reach Economical by personal delivery, no later than 1:00 p.m. (Eastern Time) on May 16, 2011, or if the Meeting is adjourned or postponed, 10 days before any adjournment or postponement thereof.

For any questions regarding the Management Proxy Circular, the form of BLUE proxy, or the exercise of voting rights, please call Georgeson at 1-866-909-6468, or call Karen Gavan, Chair of the Special Committee of the Board of Directors of Economical at 519-570-8500 x 42997.

## **APPENDIX “A” TO THE NOTICE**

### **DISSIDENT PROPOSAL**

1. To approve a resolution removing from office, effective immediately, all directors of Economical Mutual Insurance Company (the “Company”) whose term in office would otherwise continue following completion of the meeting of policyholders (the “Meeting”).
2. To nominate for election as directors of the Company at the Meeting, to hold office until the next annual meeting of the Company or until their successors are elected or appointed, that number of individuals as are to be directors of the Company immediately following the close of the Meeting, including to fill all vacancies arising from the resolutions above and as successors to the directors previously in office.

## **APPENDIX “B” TO THE NOTICE**

### **STATEMENT OF DISSIDENTS RELATING TO THE DISSIDENT PROPOSAL**

Economical Mutual Insurance Company has great potential, including dedicated management, employees and brokers and important roots in Kitchener-Waterloo. However, the Company continues to be overseen by a board of directors that has collectively shown little regard for the Company's mutual policyholders, the key stakeholder group that ultimately controls the Company and is the financial beneficiary of its business and affairs. As a mutual company, the Company also increasingly struggles under a structure that requires mounting amounts of regulatory capital while affording poor access to the capital necessary to fund growth in a competitive and consolidating industry, a growing challenge that the existing board has failed to address.

THE MORE THAN 100 MUTUAL POLICYHOLDERS THAT SUBMITTED THE POLICYHOLDER PROPOSALS (THE “CONCERNED POLICYHOLDERS”) BELIEVE THAT A NEW BOARD IS REQUIRED NOW TO PROTECT THE SIGNIFICANT ECONOMIC VALUE THAT RESIDES IN OUR POLICIES AND TO ENSURE THE FUTURE SUCCESS OF OUR COMPANY THROUGH A STRONG FOUNDATION THAT PROTECTS ALL POLICYHOLDER LIABILITIES.

At the Meeting, you will be asked to choose between continuing the status quo by re-electing the existing board or electing a new highly experienced and policyholder-focussed board that will bring fresh perspectives and improved board oversight to the Company. That new board will, if elected, immediately commence a strategic process to examine alternatives to responsibly address the Company's structural issues and enhance value for all mutual policyholders in a manner that is in the best interests of the Company and all stakeholders.

**YOUR VOTE IS CRITICALLY IMPORTANT TO THE FUTURE OF ECONOMICAL AND YOUR INTERESTS AS A MUTUAL POLICYHOLDER.** YOU ARE URGED TO IMMEDIATELY CONTACT THE CONCERNED POLICYHOLDERS AT 416-864-2274 OR VISIT [www.concernedeconomical.com](http://www.concernedeconomical.com) INCLUDING TO OBTAIN A COPY OF OUR DISSIDENT PROXY CIRCULAR WHICH CONTAINS IMPORTANT INFORMATION REGARDING THESE INITIATIVES AND HOW TO VOTE IN FAVOUR OF THE DIRECTOR NOMINEES OF THE CONCERNED POLICYHOLDERS AT THE MEETING. **PLEASE CONTACT US NOW TO LEARN MORE.**

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## **ADDENDA**

### **SCHEDULE “A” – GOVERNANCE MANDATES**

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## **1. GENERAL PROXY INFORMATION**

### **SOLICITATION OF PROXIES**

This Management Proxy Circular (the “Circular”) and the accompanying **BLUE** form of proxy are provided in connection with the solicitation of proxies by management (“Management”) of Economical Mutual Insurance Company (“Economical” or the “Company”) to be used at the Annual and Special Meeting (the “Meeting”) of mutual policyholders (“Members”) of Economical for the purposes indicated herein, to be held at 1:00 p.m. (Eastern Time) on Thursday, May 26, 2011, at Bingemans - Marshall Hall, 425 Bingemans Centre Drive, Kitchener, Ontario, Canada, and at any adjournment or postponement thereof.

Only the **BLUE** form of proxy is used by the board of directors (the “Board”) to solicit proxies and the Board recommends that it is the only form of proxy to be returned by you.

### **WHO IS SOLICITING THE PROXY**

Employees, officers, directors and agents of Economical, including Georgeson Shareholder Communications Canada, Inc. (“Georgeson”), a solicitation agent of Economical, will solicit proxies on behalf of Management of Economical. The solicitation of proxies will be done by mail, telephone, fax or in person. The costs of solicitation will be borne by Economical. Economical has retained the services of Georgeson as its proxy solicitation firm to assist with the solicitation of proxies on behalf of Management, and to provide other services relating to the Meeting. The total cost of all these services is estimated to be \$75,000.

### **CURRENCY**

Unless indicated otherwise, all amounts are in Canadian dollars and “\$” or “dollars” refer to Canadian dollars.

### **DATE OF INFORMATION**

The information contained in the Circular is given as at the date of this Circular, except where otherwise noted.

### **FORWARD-LOOKING STATEMENTS**

This Circular contains forward-looking statements concerning the business, operations and financial performance and conditions of Economical.

When used in this Circular, the words “believe”, “anticipate”, “intend”, “estimate”, “expect”, “project” and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain such words. These forward-looking statements are based on Economical’s current expectations and are naturally subject to uncertainty and changes in circumstances that may cause actual results to differ materially from those expressed or implied by such forward-looking statements. Factors that may cause such differences include but are not limited to economic, business, technological, competitive and regulatory factors. Economical is under no obligation to update or alter its forward-looking statements, whether as a result of new information, future events or otherwise, except as may be required by law.

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## **2. BACKGROUND TO THE MEETING**

This Circular is sent to you in relation to the Meeting at which the main item of business is to elect directors. To allow you to better understand the greater issues underlying the events leading up to the Meeting, this Circular also sets out the progress made towards demutualization, following the decision of the Board of Economical to pursue this process. The Circular also provides the unanimous recommendation of your Board to vote against a resolution in the proposal (the “Dissident Proposal”) of a group of dissident Members of Economical (the “Dissidents”), organized by VC & Co. Advisory Limited (“VC & Co.”), an affiliate of a Toronto-based law firm and its affiliated financial company, whose primary business is “shareholder activism”, to replace your Board.

### ***The Decision to Demutualize***

On December 14, 2010, the Board announced its intention to demutualize Economical. Since that time, the Board has made significant progress towards demutualization. Demutualization is a process whereby a mutual insurance company converts from a company with its mutual policyholders as its sole voting members to a corporation with share capital and shareholders, and distributes the proceeds of the conversion to the Members in the form of cash or transferable shares. The Board expects that significant value will be transferred to Members. The specific allocation of value among Members will be determined in accordance with regulations that are being developed by the Department of Finance as announced in the Federal Budget of March 22, 2010. Economical has been pursuing demutualization on two alternative tracks: *conversion*, through an initial public offering into a corporation with shares traded on a stock exchange of which Members would receive such amount that reflects the value of their respective interest in Economical; or *sponsored demutualization* or an asset transaction, which would involve a transaction with a strategically aligned company that would invest in Economical to acquire a significant ownership position in Economical or acquire substantially all of its assets and liabilities. Members could receive shares in the purchaser (or sponsor), or cash, or a combination of both, such compensation reflecting the value of their respective interest in Economical.

### ***Historical Context***

Economical is a “mutual” property and casualty (“P&C”) insurance company. It was founded in Berlin (Kitchener) in 1871. Economical has provided insurance to millions of persons since 1871. It has survived through difficult times (including recessions and depressions) and has weathered changing regulatory and business environments for the insurance industry. It has grown beyond its Waterloo county origins to become a national entity – the eighth largest P&C insurer in Canada - with over 2,600 employees.

P&C insurance companies in Canada typically have one of two forms of corporate organization. One common form is the traditional share corporation (in the industry these are sometimes referred to as “stock companies”). The other common form is a “mutual company”, sometimes simply referred to as “mutuals”. Mutuals in Ontario mainly trace back to companies formed in the mid to late 1800s, often on a town by town or township by township basis in predominantly rural areas. They arose as a means of fire insurance protection in those communities, as associations of people with common interests in forming a vehicle for providing property insurance not otherwise available to individual members of the group.

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As a “mutual”, Economical has no shareholders in the way a typical business corporation does. Instead, its Members elect its directors and appoint its auditors. This structure has existed for 140 years.

Economical has been a financial success over the long term with a significant accumulation of value occurring within the last 15 to 20 years. Its mutual structure (which has seen profits retained in the company) has allowed it financial stability in times of stress. Importantly, given its mutual roots and structure and the philosophy behind its creation, Economical has over the decades provided a quality insurance product at a reasonable cost to its millions of policyholders. It has been an important contributor to the community, Kitchener-Waterloo, in which it has remained headquartered.

As your Board continued the stewardship of Economical under the mutual structure, it periodically reviewed alternatives that would protect Economical and enhance its business prospects in light of longer-term industry developments. The recent global financial crisis that Economical has just weathered has demonstrated certain limitations of the mutual model. Mutual companies do not have access to capital markets to issue capital instruments (such as shares) to repair damage done by adverse market factors or to obtain capital for growth. With the financial risk issues experienced in the capital markets during the recent financial crisis, commercial insureds are relying more on risk ratings from rating agencies in determining the ability of insurers to pay on insurance claims and with whom to insure. To provide a useful rating, rating agencies require mutuals to maintain higher levels of regulatory capital because of mutuals’ lack of access to capital markets. Its mutual structure is thus impairing Economical’s ability to maintain and grow its book of commercial property and casualty insurance. The Board is also aware that a demutualization would result in the transfer of significant value to Members. Given these considerations, your Board has determined that it is appropriate and prudent to move forward with a plan of demutualization.

In the mid-1990’s the *Insurance Companies Act* was amended to allow life insurance companies (“Lifecos”) and P&C companies to demutualize. Subsequently, in the late 1990s, regulations were established that set out the process by which a Lifeco could demutualize. However, no regulations have ever been implemented that provide a framework for demutualizing P&C mutual insurers such as Economical. It is our view that the Lifeco demutualization regulations that underwent extensive review require relatively few amendments to make them applicable to P&C company demutualization situations. At this time, the Department of Finance is developing a framework for the demutualization of federally regulated property and casualty mutual insurance companies, which will provide, for companies that choose to demutualize, an orderly and transparent process and ensure that policyholders are treated fairly and equitably. The Department of Finance will be in a position to review applications to demutualize once regulations are in place. Amendments to the *Insurance Companies Act*, including amendments that would prevent any mutual company from demutualizing indirectly, will be introduced. The directors and officers of Economical have been instrumental in advancing this initiative by the Department of Finance, and the work on this project was confirmed in the March 2011 Federal Budget, which states that,

The Government is developing a framework for the demutualization of federally regulated property and casualty mutual insurance companies, which will provide, for companies that choose to demutualize, an orderly and transparent process and ensure that policyholders are treated fairly and equitably. The Government will be in a position to review applications to demutualize once regulations are in place. Amendments to the *Insurance Companies Act*, including amendments

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that would prevent any mutual company from demutualizing indirectly, will be introduced.

In the summer of 2010, the Westaim Corporation (“Westaim”), a public corporation managed by Goodwood Management Inc. (“Goodwood”), a Toronto-based activist hedge fund manager, requested a meeting with Economical and, in mid-October, 2010, Westaim proposed to the Chair of the Board of Economical the possibility of Westaim and Economical “aligning” and the possibility of a demutualization of Economical. Westaim’s principal asset is JEVCO Insurance Company which Westaim wishes to merge with Economical. JEVCO is a relatively small P&C insurer (direct written premium in 2009 was approximately \$185 million as compared with Economical’s 2009 direct written premium of approximately \$1.8 billion).

Westaim suggested that if Economical worked with Westaim to demutualize there was an opportunity for Economical’s existing directors to remain in place. Westaim also suggested that if Economical did not agree to a transaction with Westaim, Westaim understood the process involved around Economical’s meetings, electing directors and the important role of our voting policyholders. The Board believes this statement meant that if it did not cooperate with Westaim, Westaim would directly approach Members in an attempt to influence them to vote to demutualize Economical, starting with the removal of the directors of Economical. The Chair of the Board brought consideration of Westaim’s proposal to the next scheduled Board meeting on November 4, 2010.

At the November 4, 2010 meeting, the Board considered Westaim’s offer and determined to retain legal advice with respect to the Westaim approach, which led to the establishment of a special committee (the “Special Committee”). The Special Committee was formally constituted, after receipt of legal advice on its formation, on November 15, 2010. At the same time, the Board placed a moratorium on accepting applications for new Mutual Policies as part of its commitment to protect the interests of existing Members. The Special Committee determined that it was in the best interests of Economical and its Members to consider all strategic alternatives, including the Westaim proposal. This was communicated in a letter to Westaim dated November 19, 2010.

The Special Committee was given the responsibility for the review of potential proposals from third parties regarding transactions involving Economical, and to provide recommendations thereon to the Board. It was also given the mandate to consider methods of maximizing value in Economical for its Members – including reconsidering a demutualization process. The Special Committee is composed of directors Karen L. Gavan (Chair), Mary N. Bales, David A. MacIntosh, and Charles M.W. Ormston. Miller Thomson LLP was retained as legal counsel, and Blair Franklin Capital Partners was retained as financial advisor to the Special Committee. Since its inception, the Special Committee, together with Economical’s Management and its financial and legal advisors, has been working to evaluate a range of strategic alternatives.

In December 2010, the Special Committee determined that demutualization holds the greatest potential benefits for Economical.

The Special Committee recommended to the Board, and the Board unanimously agreed to proceed with, two alternatives:

1. conversion through an initial public offering of shares in the capital of Economical, from a mutual company to a public corporation with shares traded on a stock exchange and the distribution of such shares to the Members; and

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2. a sponsored demutualization, or an asset transaction, which would involve a transaction with a strategically aligned company that would invest to acquire a significant ownership position in Economical or acquire substantially all of its assets and liabilities in which case, the Member would, at some point, receive shares in the purchaser (or sponsor), or cash, or a combination of the two, such consideration representing the respective value of each Member's interest in Economical.

This was announced publicly on December 14, 2010.

### ***Significant Progress Towards Demutualization***

This dual track approach allows the Board to focus on maximizing long-term value for Members and is currently well underway. This process is subject to regulatory approval and significant progress has been made as follows:

- Economical's Chief Executive Officer Kathy Mabe announced a corporate reorganization on January 24, 2011, designed to create a model that will meet the current needs of the demutualization process and, more importantly, Economical's future requirements when the process is completed. The new structure draws on Ms. Mabe's extensive insurance industry experience and is designed to promote efficiency and enhance our ability to seize the new opportunities we expect to be created through the demutualization. It also maintains our strong commitment to our broker partners which will always be a critical part of our focus.
- Our internal team, along with the financial and legal advisors, have developed the non-disclosure agreements and a confidential information memorandum that has been provided to qualified third parties who are interested in pursuing a sponsored demutualization, or asset transaction. Non-disclosure agreements have been signed by a number of qualified parties, following which such parties were given access to confidential financial information to allow them to make a "qualifying offer". An offer process memo has also been provided to these interested parties setting out the steps for submission of proposals.
- In preparation for the possible initial public offering, our internal financial team led by interim Chief Financial Officer Phil Mather, and the accounting firm Deloitte LLP, have continued to align Economical's financial reporting and disclosure with best practices for public companies. The Special Committee has also prepared a request for proposals for selection of a lead underwriting manager.
- We have met regularly with officials of the Department of Finance, which is responsible for developing the regulations to guide the demutualization of property and casualty insurance companies. As part of this process, we have developed and provided detailed information and analysis on policy issues and proposed issue resolution to the Department of Finance. As a direct result of these initiatives, the March 2011 Federal Budget provided that, "the Government is developing a framework for the demutualization of federally regulated property and casualty mutual insurance companies, which will provide, for companies that choose to demutualize, an orderly and transparent process and ensure that policyholders are treated fairly and equitably. The Government will be in a position to review applications to demutualize once regulations are in place. Amendments to the *Insurance Companies Act*, including amendments that would prevent any mutual company from demutualizing indirectly, will be introduced."

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- Our Chief Actuary has been working with actuarial consultants and financial advisors on the process of determining the allocation of demutualization benefits and developing specific methods to distribute such benefits. We have also initiated consultation with the Office of the Superintendent of Financial Institutions (“OSFI”) as it will need to approve the demutualization proposal before it is voted on by Members. We have also had our internal auditor firm confirm the data integrity of our mutual policyholder database.

Although demutualization is a complex process, we have already made substantial progress and we are confident that with continuity of stewardship, under your current Board, we can create a successful outcome for Members.

### ***The Proposal of the Dissidents***

On November 12, 2010, an entity called VC & Co., which was incorporated on November 15, 2010 and is owned directly or indirectly by the partners of Voorheis & Co. LLP (whose clients have included Westaim and its manager, Goodwood), began publicly soliciting support from the Dissidents for the Dissident Proposal that the Board be replaced with nominees, selected by VC & Co., who have, as of the date of this Circular, not been identified.

The *Insurance Companies Act* permits not less than 100 eligible Members of Economical to submit Member proposals to Economical for inclusion in a management proxy circular for an annual meeting of Members.

Although the Dissident Proposal has been submitted to Management by the Dissidents for inclusion in this Circular, the solicitation of the Dissident Proposal was sponsored by VC & Co. which required that certain, but apparently not all, of the Dissidents enter into agreements with VC & Co. by which VC & Co. would receive significant fees (12.5 % of the amount or value of all distributions (other than under insurance claims and ordinary course dividends) received by the Dissidents from Economical for a period of six years following the Meeting) if a demutualization of Economical or if certain other significant transactions involving Economical occurred.

VC & Co. has indicated that if the Dissident Proposal is successful, VC & Co. will request that its directors nominees cause Economical to pay the fees and reimburse expenses of VC & Co. and assume the liabilities of any Dissident who entered into a fee agreement with VC & Co.

In effect, this would cause each Member to bear the cost of the obligations assumed personally by the Dissident Members who signed fee agreements with VC & Co., whether or not the Members supported the Dissident Proposal. We understand that not all Dissident Members were required to sign a fee agreement with VC & Co., but VC & Co. has not disclosed to Economical, or to you, which Dissident Members have, and have not, done so.

In any event, the Dissident Proposal is to a large degree, moot. VC & Co. is promoting the Dissident Proposal so as to cause Economical to demutualize or enter into an asset transaction (or other similar transaction), however, your directors, acting through the Special Committee, are already taking the exact action that Westaim, VC & Co. and the Dissidents have implicitly suggested: to demutualize Economical. The crucial difference is that the current Board has a significant head start over any new Board, and under the current Board process, VC & Co. will not receive any fees or expense reimbursement from Economical. Voting for the Dissident Proposal will delay and possibly derail the demutualization and will only bring the Company further away from the shared goal of demutualization and value realization, and will cost Members, and Economical, more.

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The current directors have already:

- made significant progress towards demutualization;
- established relationships with advisors and regulators; and
- drawn on their significant experience with Economical to do so.

Additionally, under a demutualization led by the current Board, the Board will not cause Economical to pay any fees or expense reimbursement to VC & Co., or similar entities (which is substantially different from the VC & Co. agreements pursuant to which VC & Co. states that it will ask its director nominees to have Economical pay its fees and reimburse its expenses). These payments will reduce the value of your interest in Economical and thus the amount that you receive on conclusion of the demutualization. If Economical's current directors remain in place, no payment will be made to an entity like VC & Co.

### ***Court Proceedings***

Given its perception of the conflict created by the Dissident Proposal and VC & Co.'s activities, and the significant effect that a successful Dissident Proposal, followed by a transaction being led by potentially conflicted board of directors inexperienced in the affairs of Economical, could have on Economical and the Members, the Special Committee, with the support of the Board, felt it incumbent to seek clarity on the legality of the Dissident Proposal in court. On January 14, 2011, coincident with Economical's rejection of VC & Co.'s approach, Economical commenced an action in the Ontario Superior Court of Justice (the "Court") seeking clarification as to whether the Dissident Proposal is legally proper and whether it is to be treated as a valid proposal.

Additionally, following an extensive investigation, and as part of the Board's duty to protect the interests of the Company, the Board filed a statement of claim in the Court against Economical's former Chief Financial Officer, Sandeep Uppal and others alleging the misappropriation of \$126,000. The Board is also seeking a declaration that Economical had cause to dismiss Mr. Uppal for that misappropriation and for breach of fiduciary duty related to his secret support of, and participation in, the unsolicited approach by Westaim, regarding its proposed demutualization, as well as the related activities of VC & Co. that followed the Westaim approach.

On April 6, 2011, a judgment was handed down by the Court on Economical's application regarding the Dissident Proposal. The Court ruled that two of three initial proposals from the Dissidents may be considered at the Company's Annual Meeting (to remove the current Board and to replace it with a new Board). However, the Court ruled that the Dissident proposal to amend the Company's By-law providing for the staggered election of directors would violate the *Insurance Companies Act* and cannot be considered. Therefore it will not be considered at the Meeting.

The Court also rejected, in whole, a cross-application from the Dissidents which sought changes to the procedures used for the Meeting, including requiring the Company to provide personal information about all mutual policyholders to the Dissidents, which the Court found would violate the privacy rights of those individuals.

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### **3. WHY YOUR BOARD RECOMMENDS THAT YOU VOTE AGAINST THE DISSIDENT PROPOSAL**

Your Board has been actively engaged on your behalf in the demutualization of Economical and has made significant progress to maximize value for our Members. In working towards demutualization, your Board is applying its extensive experience, its independence and a wealth of important relationships with its Members, advisors, regulators, the community, our broker network and other stakeholders. We believe that the Dissident Proposal does not create any advantage for Members, and that the Members could be significantly disadvantaged by the Dissident Proposal. We also believe Members will realize the most value under a demutualization overseen by your current Board. Only it can maintain the current progress it has already made and offer the necessary continuity and experience to complete the process. Changing directors will only delay, and possibly derail, the demutualization. This may be in the financial interest of VC & Co. but it is not in the interest of the Members.

It was only as a result of the Court application that VC & Co. finally admitted that its principals had been acting as advisers to Westaim, through the law firm of Voorheis & Co. LLP, - a law firm that regularly acts for Goodwood, the hedge fund that manages Westaim, in its hostile proxy battles. VC & Co. had never previously disclosed this relationship to Economical and had stated to Economical and the policyholders that it had no conflicts and it was wrong for Economical to suggest otherwise. More importantly, VC & Co. did not disclose this relationship to you, the mutual policyholders.

Also as a result of the Court application, evidence was produced that showed that Westaim had been communicating with Mr. Sandeep Uppal, the then Chief Financial Officer of Economical, and Westaim obtained from him confidential information concerning Economical. In particular, Mr. Uppal and Westaim discussed in some detail the possibility of ousting the current directors of Economical and demutualizing Economical. Mr. Uppal had also been meeting with and communicating with the principals of VC & Co. on numerous occasions. Mr. Uppal has been dismissed from his employment with Economical, and litigation has been commenced against Mr. Uppal for alleged misappropriation of funds and for breach of fiduciary duty to Economical in relation to his activities. VC & Co. had refrained from disclosing to Economical the communications among Mr. Uppal on the one hand, and Westaim and VC & Co. on the other, and the involvement of Mr. Uppal in the activities of Westaim and VC & Co. More importantly, VC & Co. did not disclose this activity to you, the mutual policyholders. A chart setting out the relationship between these parties is included at the end of this section.

Despite VC & Co.'s failure to disclose the nature of discussions between it and Westaim, it is clear that on multiple occasions, Mr. Uppal and Westaim discussed ousting the current Board of Economical by making a policyholder proposal at the next annual meeting of Economical. They also discussed the longer-term plan of demutualization. Confidential information about Economical was given to Westaim by Mr. Uppal at these meetings.

These discussions are known to have taken place at a time when principals of VC & Co. were acting as Westaim's lawyers. There would almost certainly have been discussion between Westaim and its lawyers of the legal implications of ousting the Board, the proposal process and eventual demutualization. It is likely that Westaim would have shared the confidential information obtained from Mr. Uppal with the principals of VC & Co. Westaim and VC & Co. would have been working hand in hand to further Westaim's goal of acquiring control of Economical. Therefore, it is difficult to believe that a mere few days after purportedly severing

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ties on this matter with Westaim (who remains interested in acquiring Economical), VC & Co. could change allegiances so quickly and work to promote the interests of the Dissidents – whose interests, from a monetary point of view, are opposite to those of Westaim (who wants to acquire Economical as cheaply as possible).

The Board believes that the Dissident Proposal is designed to hand control of Economical to a small group of Dissidents, led by VC & Co., and their director nominees. The Board believes that VC & Co. may be conflicted in its duty to act in the best interest of the mutual policyholders. Its principals acted for Westaim in relation to its overtures to convince Economical to demutualize for the benefit of the shareholders of Westaim. In acting for Westaim, the principals of VC & Co. were involved in a process that would require them to attempt to have Westaim pay the lowest possible price for Economical, to the detriment of the Members. On changing positions only days thereafter and purporting to act for the Dissident Members, VC & Co. now claims not to be acting in Westaim's interests. While VC & Co. has purported to act for the Dissidents, Westaim has continued to express an interest in acquiring Economical or its business. The Board is concerned that VC & Co. is conflicted in these two retainers, or at the very least, there is a serious perception of conflict. VC & Co. had not disclosed this conflict to Economical until required to do so in the recent Court application. More importantly, it did not disclose this conflict to you, the mutual policyholders.

VC & Co. has already indicated to the Dissidents that it will ask the Dissident director nominees (parties who will presumably have certain loyalty to VC & Co. through their nomination as directors) to cause Economical to assume the Dissident policyholders' obligation to pay significant fees and all expenses to VC & Co. This will be paid out of all Members' shares in the value of Economical, whether or not the Member supports the Dissident Proposal. This will reduce any value that could be passed on to you as a Member.

The structure of VC & Co.'s fee arrangements ensures that it will have strong incentive to cause a transaction to be concluded for Economical whether it is in the best interests of Members or not. Your Board believes that there is significant risk of an improvident transaction being approved by a new group of directors, inexperienced in the affairs of Economical. These new directors will, of necessity, owe loyalties of nomination to VC & Co. which may be expected to have an interest in doing a transaction which is beneficial to an entity like Westaim, with whom the principals of VC & Co. have previously been acting, and to whom Mr. Uppal had been rendering assistance in breach of his fiduciary duties. Your Board has no such conflicts and you can be confident that it will act in your best interests no matter with whom it deals.

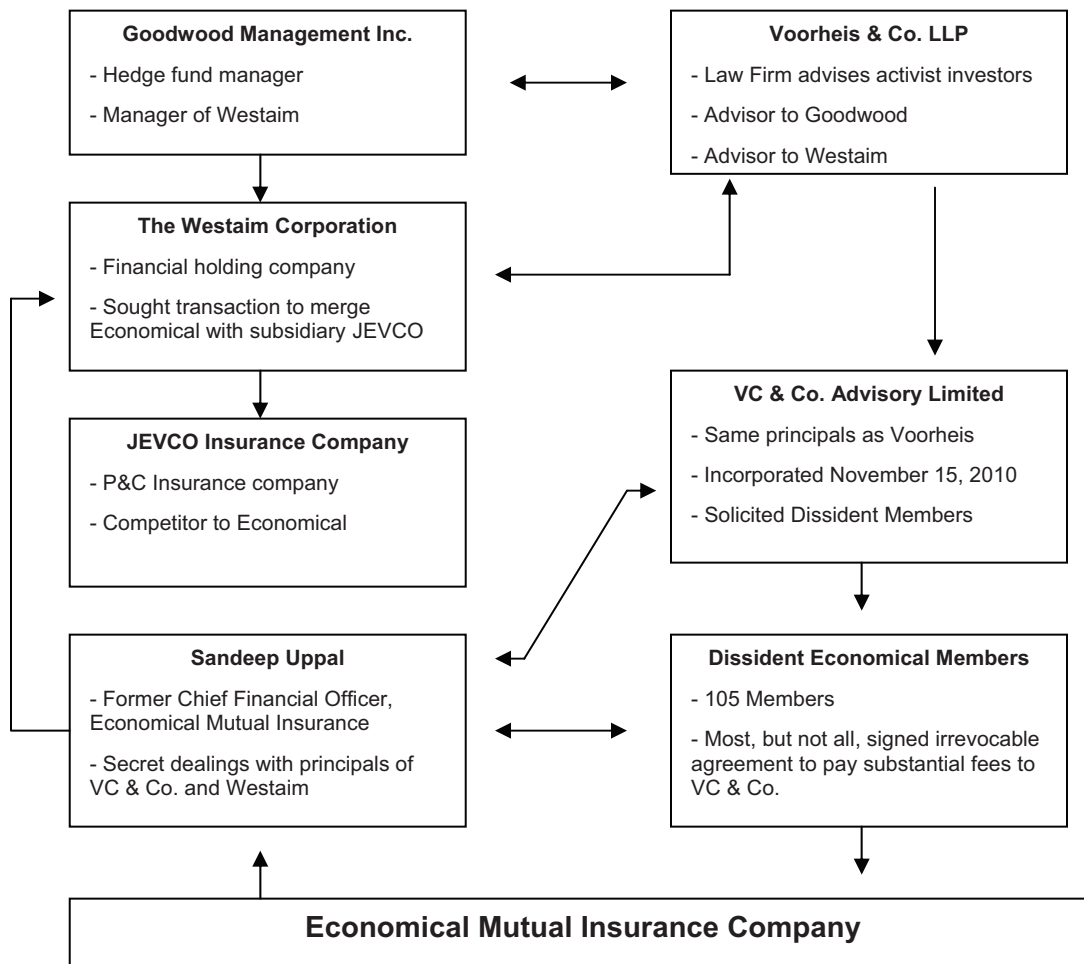
A board hand-picked by VC & Co. may be very sympathetic to transactions suggested by Westaim – VC & Co.'s old partner and confidante. This clear conflict of interest is unacceptable, and Members should not hand control of Economical to a board that is supported by a collaborator of Westaim who continues to want to obtain Economical (presumably as cheaply as possible) – which would also ensure that VC & Co. would be paid its large fees.

Your Board believes that a significant corporate transaction under the direction of a new board of directors in such circumstances cannot be in the best interest of Economical and its Members and carries significant risk for all involved, other than VC & Co. and its associates who will stand to make substantial fees if this occurs.

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**THE QUESTION IS THIS: WHO DO YOU TRUST TO COMPLETE YOUR DEMUTUALIZATION?**

**CHART OF RELATIONSHIPS BETWEEN VC & CO. AND OTHERS**



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***Your Board's Recommendations regarding the Dissident Proposal to End Each Director's Term Effective as of the Meeting Date, to Oust all of the Current Directors and to Replace them with a Slate of Dissident Nominees***

Your Board urges you to **VOTE FOR** its slate of nominees and **VOTE AGAINST** the ouster of the current directors and replacement of them with Dissident nominees for the following reasons.

- **Changing the Board now will delay demutualization and will not maximize value for Members**

The Board is already taking the action that VC & Co. and the Dissidents have suggested: to demutualize Economical or cause it to enter into an asset sale transaction. There is no benefit to replacing the Board as it will just delay, and may derail, the process.

- **Your current Board is experienced and has a wealth of necessary and important relationships with Members, regulators, brokers, employees, the community and other stakeholders**

The current Board has deep knowledge of Economical and the industry and environment in which it operates. The current directors have also spent significant time on the demutualization process, have built strong relationships with regulators and have expertise in this complex area. This experience, and these relationships, will be crucial as Economical reinvents itself to provide better value to its Members and to better serve its stakeholders. Economical has grown significantly under the guidance of the current Board and the election and maintenance of an experienced and stable Board is of utmost importance at this time of change.

- **VC & Co.'s expected influence over its hand-picked director nominees may cause conflicts of interest for the Dissidents' directors**

Since VC & Co. is selecting the Dissident directors, it is likely that these Dissident director nominees will feel pressure to act in the best interest of VC & Co., even if doing so is not necessarily in the best interests of Economical, or may not maximize value for its Members. In addition, as set out above, your Board is concerned that there is a significant risk of conflict because of VC & Co.'s acknowledged relationship with a competitor (Westaim) that had expressed, and continues to express after VC & Co. commenced its solicitation of Dissidents, a strong interest in acquiring Economical.

The current stable, and experienced Board is independent and has no conflict of interest with the demutualization process, or otherwise.

- **Maintaining your Board is the best way to maximize value to Members**

An overturning of the Board, with its attendant changes in the oversight of management, can damage relationships with regulators, customers, employees and other important stakeholders such as brokers. It is essential that continuity be maintained to ensure that Members, brokers and employees are retained throughout this process. Loss of this continuity could result in a decrease in value of Economical, and a loss of value of your interest in Economical which you will receive on completion of the demutualization.

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- **Avoid reducing the value of your interest in Economical: Do not pay fees to VC & Co.**

Your Board is actively pursuing a demutualization process and is ensuring the careful management of costs associated with demutualization. Under a demutualization led by the current Board, no Member will be asked to pay any additional fees to entities like VC & Co. to realize gains under the demutualization process.

VC & Co. has stated that, if the Dissident Proposal succeeds, it will seek to have its hand-picked Board direct Economical to pay millions in fees and expenses which many of the Dissidents have personally agreed to pay VC & Co. The fee is a substantial 12.5% of their proceeds from any action taken by Economical over the next six years, except normal course premium refunds and claims payments. If the Dissident Proposal succeeds, this would effectively extend the liabilities of a minority of Dissident Members to all Members should the Company have to pay for VC & Co.'s fees and expenses, whether or not they support the Dissident Proposal. We believe this inequity indicates how VC & Co. would expect its Board to approach its responsibilities to Members. At the very least, this will decrease the value of Economical and what will be paid to you upon completion of the demutualization.

**The Board of Directors of Economical  
unanimously recommends that you**

- |                      |   |
|----------------------|---|
| <b>RESOLUTION 1.</b> | <b><u>VOTE FOR</u> Each of Economical's<br/>Director Nominees</b>         |
| <b>RESOLUTION 2.</b> | <b><u>VOTE FOR</u> the Appointment of<br/>the Auditors</b>                |
| <b>RESOLUTION 3.</b> | <b><u>VOTE AGAINST</u> the Ouster of All<br/>of the Current Directors</b> |

**YOUR VOTE IS EXTREMELY IMPORTANT. VOTE ONLY THE BLUE PROXY.**  
**For questions or assistance, please call Georgeson at 1-866-909-6468.**

## **4. VOTING INFORMATION**

### **MUTUAL POLICIES**

Economical is the parent company of The Economical Insurance Group (“TEIG”) - federally regulated financial institutions governed by the *Insurance Companies Act* and regulated by OSFI. Economical is a mutual property and casualty insurance company dating back approximately 140 years. “Mutual companies” do not have a share structure or shareholders. Mutual companies have members who are persons who insure their property by way of a mutual insurance policy (each a “Mutual Policy”). Each holder of a Mutual Policy has the right to vote at meetings of members. Each member ceases to become a member when his, her or its mutual policy terminates. Each member has only one vote regardless of how many mutual policies such member holds. Economical also issues a large number of non-mutual insurance policies. Such policies do not give the insured any voting rights.

### **WHO MAY VOTE**

Each holder of a Mutual Policy of record of Economical (a “Member”) at 5:00 p.m. (Eastern Time) on May 25, 2011, is entitled to cast one (1) vote per Member on all matters proposed to come before the Meeting.

Economical’s By-laws provide that if any policy shall be issued in the joint names of two or more persons, any one of them present at the Meeting or represented by proxy duly appointed may vote in the absence of the other or others, but in the case more than one of them be present at any Meeting, either in person or by proxy duly appointed, only the person whose name first appears on such policy, or the proxy duly appointed, as the case may be, shall be entitled to vote in respect thereof.

### **HOW TO VOTE**

Members may vote either:

- by using the BLUE form of proxy; or
- if necessary, in person at the Meeting.

To vote by proxy, Members may complete, sign and return the enclosed form of BLUE proxy by mail in the postage-paid envelope provided, by hand at 100 University Avenue, 9<sup>th</sup> Floor, Toronto, ON, M5J 2Y1, or fax it to Computershare Investor Services Inc. (“Computershare”) at 1-866-249-7775 (toll free in North America), 416-263-9524 (International) as soon as possible but at the latest by 1:00 p.m. (Eastern Time) on May 16, 2011. Blue proxies may also be deposited at the head office of Economical at 111 Westmount Road, Waterloo, Ontario at the latest by 1:00 p.m. (Eastern Time) on May 16, 2011. You may also call Georgeson at 1-866-909-6468 and they will arrange to have a courier pick up your completed BLUE proxy. The form of proxy authorizes a proxyholder to represent and to vote on behalf of the Member at the Meeting.

***YOUR VOTE IS EXTREMELY IMPORTANT. VOTE ONLY THE BLUE PROXY.  
For questions or assistance, please call Georgeson at 1-866-909-6468.***



## VOTING BY PROXY

### *Voting Instructions*

All properly executed proxies are to be voted for, against or withheld from voting by the proxyholder designated in the enclosed BLUE form of proxy as instructed by the Member. **If no instructions are given in the proxy, the voting rights attached to the Mutual Policy in question will be exercised by any designated proxyholder who is a director and/or officer of the Company by voting as follows:**

Resolution 1. FOR the election of each of the proposed directors nominated by Management of Economical;

Resolution 2. FOR the appointment of the auditor; and

Resolution 3. AGAINST the ouster of the current directors of Economical.

The enclosed BLUE form of proxy confers on the proxyholder designated therein discretionary authority with respect to any proposed amendments or variations to the matters set out therein and any other business which may properly come before the Meeting. In the event that the Dissident Proposal results in a requirement to elect nine directors at the Meeting, Management of the Company will put forward a slate of nine directors for election, or re-election as the case may be. This slate will be John H. Bowey, A. Scott Carson, Karen L. Gavan, Mary N. Bales, Gerald A. Hooper, Katherine A. Mabe, David A. MacIntosh, Charles M.W. Ormston, and Michael P. Stramaglia or substitute nominees in the discretion of the proxyholders. At the date of this Circular, Management is not aware of any amendment or other matter which may properly come before the Meeting other than the Dissident Proposal.

### *How to Appoint a Proxyholder*

The proxyholders designated in the enclosed BLUE form of proxy are directors and/or officers of the Company. **If a Member wishes to appoint a proxyholder other than one of the persons designated in the form of proxy, such Member may do so by striking out the names appearing thereon and inserting the name of such person in the blank space provided.** If the Member is a legal entity, an estate or trust, the form of proxy must be signed by a duly authorized representative and accompanied by a certified resolution confirming such authorization. A proxyholder is not required to be a Member of the Company.

In order to be valid, the BLUE form of proxy must be registered with Computershare by mail or in person at 100 University Avenue, 9<sup>th</sup> Floor, Toronto, ON, M5J 2Y1, or by fax, at 1-866-249-7775 (toll free in North America), 416-263-9524 (International) no later than 1:00 p.m. (Eastern Time) on May 16, 2011, or, if the Meeting is adjourned or postponed, 10 days before the new date determined by adjournment or postponement of the Meeting. Blue proxies may also be deposited at the head office of Economical at 111 Westmount Road, Waterloo, Ontario at the latest by 1:00 p.m. (Eastern Time) on May 16, 2011. You may also call Georgeson at 1-866-909-6468 and they will arrange to have a courier pick up your completed BLUE proxy. If you wish to return the form of proxy by mail, you may use the postage-paid envelope included with this Circular.

**YOUR VOTE IS EXTREMELY IMPORTANT. VOTE ONLY THE BLUE PROXY.**  
**For questions or assistance, please call Georgeson at 1-866-909-6468.**

### ***How to Revoke a Proxy***

Members may revoke a proxy:

- by delivering a written notice to that effect signed by them or their duly authorized representative(s) to Computershare Investor Services Inc., at 100 University Avenue, 9th Floor, North Tower, Toronto, Ontario, Canada, M5J 2Y1, no later than 5:00 p.m. (Eastern Time) on May 25, 2011, or if the Meeting is adjourned, 24 hours before any continuation thereof after an adjournment;
- by delivering a written notice to that effect signed by them or their duly authorized representative(s) to an agent of Computershare or the Chair of the Meeting, on the day of the Meeting, or any continuation thereof after an adjournment; or
- in any other manner permitted by law.

The notice must be signed by the Member or by an attorney duly authorized in writing to this effect; if the Member is a legal entity, the notice must be signed by an officer or attorney of such legal entity duly authorized in writing by a resolution, a certified copy of which must be attached to the notice.

#### **The Board of Directors of Economical unanimously recommends that you**

**RESOLUTION 1.      VOTE FOR Each of Economical's  
Director Nominees**

**RESOLUTION 2.      VOTE FOR the Appointment of  
the Auditors**

**RESOLUTION 3.      VOTE AGAINST the Ouster of All of  
the Current Directors**

***YOUR VOTE IS EXTREMELY IMPORTANT. VOTE ONLY THE BLUE PROXY.  
For questions or assistance, please call Georgeson at 1-866-909-6468.***

## 5. BUSINESS OF THE MEETING

The Meeting is an annual and special meeting of Members and will address the annual business of Economical along with the special matters set out in the Dissident Proposal received from the Dissidents. The Dissident Proposal is set out in its entirety in Appendix “A” and Appendix “B” to the Notice that is set out on page viii of this Circular.

### ITEM A - FINANCIAL STATEMENTS

A copy of the consolidated financial statements of Economical for the year ended December 31, 2010 together with the auditor’s report thereon and the actuary’s report on the policy liabilities in those statements are included with this package and will be placed before the Members at the Meeting. This Company’s Annual Reports are also available in the “Media Centre” section of the Company’s web site (<http://www.economicalinsurance.com>).

No vote is required at the Meeting in respect of Economical’s 2010 financial statements or reports thereon.

### ITEM B - APPOINTMENT OF AUDITORS

Auditors must be appointed at each annual meeting of Members.

**The Board recommends that you VOTE FOR the appointment of the accounting firm of Ernst & Young LLP (“E&Y”) as auditor of the Company for the financial year commencing January 1, 2011 and ending December 31, 2011 and to hold office until the next annual meeting of the Members at remuneration to be fixed by the Board.**

Fees paid to E&Y for 2009 and 2010 are as follows:

Auditor Fees (\$)	2010	2009
Audit Fees <sup>(1)</sup>	747,337	707,168
Audit-Related Fees <sup>(2)</sup>	7,000	93,140
Tax Fees <sup>(3)</sup>	169,895	181,250
All Other Fees <sup>(4)</sup>	38,500	79,062
<b>Total</b>	<b>962,732</b>	<b>1,060,620</b>

Notes:

- (1) Audit Fees include fees for professional services for the audit of the Company’s financial statements and those of its subsidiaries or other services that are normally provided by external auditors in connection with statutory and regulatory filings or engagements, including internal control audit and reviews.
- (2) Audit-Related Fees are for assurance and related services performed by E&Y. These services include pension fund audits, quarterly reviews, accounting consultations in connection with acquisitions and divestitures and interpretation of financial accounting and reporting standards, including IFRS and other attest services not required by statute or regulation.
- (3) Tax Fees are for assistance with tax compliance, tax planning, and tax advice related to restructurings and tax audits and appeals related thereto.
- (4) Such fees were pre-approved by the Audit Committee.

**YOUR VOTE IS EXTREMELY IMPORTANT. VOTE ONLY THE BLUE PROXY.  
For questions or assistance, please call Georgeson at 1-866-909-6468.**

**ITEM C – CONSIDERATION OF, AND VOTING ON, A DISSIDENT PROPOSAL TO REMOVE FROM OFFICE ALL DIRECTORS EFFECTIVE AS OF THE MEETING DATE**

Pursuant to the By-laws of Economical, directors hold office for rotating three year terms and the directors have been elected on a rotating basis. Only three of nine directors are up for election at the Meeting; the remaining six directors' terms continue beyond the Meeting.

This Dissident Proposal contemplates ending any unfinished director term as of the date of the Meeting and ousting all the existing directors of Economical at that time.

Please see the section entitled "Why Your Board Recommends That You Vote Against The Dissident Proposal" for the Board's reasons for its recommendation.

**The Board recommends that you VOTE AGAINST the Dissident Proposal to remove from office all directors effective as of the Meeting date.**

***YOUR VOTE IS EXTREMELY IMPORTANT. VOTE ONLY THE BLUE PROXY.  
For questions or assistance, please call Georgeson at 1-866-909-6468.***

## ITEM D – ELECTION OF DIRECTORS

The fourth matter of business of the Meeting is the election of directors.

**The Board recommends that you VOTE FOR each of Economical's director nominees.**

Please see the section entitled "Why Your Board Recommends That You Vote Against the Dissident Proposal of the Dissidents" for the Board's reasons for its recommendation.

The By-laws of Economical provide that the Board shall consist of a minimum of seven directors and a maximum of 21 directors. The number of directors to be elected at any annual meeting of Members shall be such a number as is fixed by the Board prior to the annual meeting. Until such time as a number of directors constituting the Board shall be changed by resolution of the directors, there shall be nine directors of the Board. While Economical does have honorary directors, these directors do not vote and are not up for election. They are not considered in this Circular.

The current Board consists of Mary N. Bales, A. Scott Carson, Karen L. Gavan, Gerald A. Hooper, Katherine A. Mabe, David A. MacIntosh, Charles M.W. Ormston, Terrence J. Reidel and Michael P. Stramaglia and their biographies are contained hereafter. Noel G. Walpole was the Chief Executive Officer and a director until stepping down effective December 31, 2010. Katherine A. Mabe replaced him as both Chief Executive Officer and director. She was appointed by the Board to fill the vacancy left by Mr. Walpole's retirement and will hold the position until the end of its term.

Mr. Reidel is retiring from the Board at the end of the Meeting and is not standing for re-election. Ms. Gavan and Mr. MacIntosh's three-year terms expire at the end of the Meeting and are standing for re-election. The Board is proposing, in addition to Ms. Gavan and Mr. MacIntosh, that Mr. Bowey be elected for a three-year term. All of the director's biographies are contained hereafter.

These three nominees proposed for election (or re-election, as the case may be) as directors of Economical will hold office for a three-year term ending at the close of the annual general meeting of Members in 2014 or until their successors are elected or appointed.

Economical's Corporate Governance and Conduct Review Committee reviews the qualifications of persons proposed for election to the Board and submits its recommendations to the current directors for consideration. The CGCR Committee is composed entirely of directors who are independent of Management and the Company. Each of Economical's proposed director nominees has established his or her eligibility and willingness to serve as a director if elected and Economical does not contemplate that any of these nominees will be unable to serve as a director. However, if for any reason any of Economical's proposed director nominees do not stand for election or are unable to serve as such, Economical reserves the right to nominate substitute, or additional, nominees, and proxies in favour of management will be voted for such other nominees in the discretion of such proxyholders.

Without limiting the foregoing, although the Board strongly recommends that you vote against the Dissident Proposal, in the event that the Dissident Proposal results in a need to elect nine directors at the Meeting, Management of Economical will put forward a slate of nine directors for election, or re-election as the case may be. This slate will be made up of John H. Bowey, Karen L. Gavan, David A. MacIntosh, Mary N. Bales, A. Scott Carson, Gerald A. Hooper, Katherine A.

***YOUR VOTE IS EXTREMELY IMPORTANT. VOTE ONLY THE BLUE PROXY.  
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Mabe, Charles M.W. Ormston, and Michael P. Stramaglia, or substitute nominees in the discretion of the proxyholders.

### **ECONOMICAL'S SLATE OF DIRECTOR NOMINEES**

At the Meeting, it is proposed that three directors be elected, to hold office until the next annual meeting or until their successors are elected or appointed. **Unless otherwise directed, it is the intention of Management to vote BLUE proxies in favour of the election of Economical's slate of director nominees.**

In the event that the Dissident Proposal results in a need to elect nine directors at the Meeting, it is the intention of Management to vote **BLUE** proxies in favour of the election of Economical's slate of nine director nominees: John H. Bowey, Karen L. Gavan, David A. MacIntosh, Mary N. Bales, A. Scott Carson, Gerald A. Hooper, Katherine A. Mabe, Charles M.W. Ormston, and Michael P. Stramaglia.

The following sets out the names of all persons proposed by Economical for election as directors; the date on which each such nominee first became a director of Economical; all positions, committees and offices with Economical held by each such nominee; the principal occupation and a brief biography of each nominee; and each respective nominee's place of residence. It also sets out the same information for each incumbent and retiring director.

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For questions or assistance, please call Georgeson at 1-866-909-6468.***



## Nominees for Election as Director



JOHN H. BOWEY,  
FCA  
Conestogo, ON  
Canada  
New director nominee  
Age: 64  
**Independent**

Mr. Bowey obtained a BA in Economics from Colby College in Waterville, Maine in 1971 and his MBA from the Ivey School of Business at the University of Western Ontario in 1973 at which time he joined Deloitte becoming a partner in 1983.

He was elected to the Deloitte Board of Directors in 2002, was appointed Chairman of the Board Governance Committee of Deloitte in 2004 and was elected by the partnership as Chairman of Deloitte in 2006 and served in that capacity until his retirement in May of 2010. In addition to his Canadian responsibilities, Mr. Bowey was a member of the global Board of Deloitte and the global governance Committee and Audit Committee. He is a fellow of the Institute of Chartered Accountants of Ontario for his professional and community achievements.

Mr. Bowey has served on a number of corporate and not-for profit boards including, Princess Margaret Hospital Foundation, University Health Network, Opportunity International, Brick Brewing Co. Limited, Simpson Seeds Inc. and Kennsington Capital Partners.

Year Joined Board and Committees	Attendance
N/A	(Mr. Bowey was not a director in 2010)



KAREN L. GAVAN,  
ICD.D, FCA  
Toronto, ON  
Canada  
Age: 49  
**Independent**

Ms. Gavan is Chair of the Special Committee of the Board. She has over twenty-five years of financial and corporate governance experience. She is a Fellow of the Institute of Chartered Accountants of Ontario and holds the ICD.D designation from the Institute of Corporate Directors. Ms. Gavan also sits on the boards of Mackenzie Financial Corporation, Counsel Group of Funds, Independent Order of Foresters, Green Shield Canada, TBAY Tel Municipal Services and Hope Air. She served for many years on the Board of the Children's Aid Foundation. Ms. Gavan was formerly the Chief Operating Officer and Chief Financial Officer of Transamerica Life and AEGON Fund Management Inc. Prior to that she held senior management positions with Canada Life and Imperial Life Assurance Company. Ms. Gavan also held a senior financial position with Canada Life Assurance Company during the time period in which it demutualized.

Year Joined Board and Committees	Attendance
Board (2008)	14/14 (100%)
Audit Committee (2008)	4/4 (100%)
Special Committee (Chair) (2010)	9/9 (100%)
Pension Committee <sup>1</sup> (2008)	5/5 (100%)

<sup>1</sup> The Pension Committee has been dissolved and its mandate split between the Human Resources and Compensation Committee and the Investment Committee for 2011.

**YOUR VOTE IS EXTREMELY IMPORTANT. VOTE ONLY THE BLUE PROXY.**  
**For questions or assistance, please call Georgeson at 1-866-909-6468.**

## Nominees for Election as Director



DAVID A.  
MACINTOSH,  
M.A.  
Waterloo, ON  
Canada  
Age: 70  
***Independent***

Mr. MacIntosh was employed by Mutual Life of Canada for 36 years in a number of senior positions, and at the time of his retirement in 1999 he was Executive Vice President, Investments with responsibility for overall investment operations. He served as a Director of various Mutual Life subsidiary companies, including The Mutual Group (US), The Mutual Trust Company, and Mu-Cana Investment Counseling Ltd. He was previously a Director of several publicly-traded Canadian financial services companies, including Newcourt Credit Group Inc and Perigee Inc. He is currently a member of the Board of Directors of MCAN Mortgage Corporation in Toronto (2000 – present), where he chairs its Investment Committee. Mr. MacIntosh has also been involved in a number of local community organizations, including as President of Kitchener-Waterloo Federated Appeal, Governor and Chair of Grand River Hospital Foundation, and Director and Chair of the Investment Committee of The Kitchener and Waterloo Community Foundation.

<b>Year Joined Board and Committees</b>	<b>Attendance</b>
Board (2002)	14/14 (100%)
Investment Committee (2002)	4/4 (100%)
Special Committee (2010)	9/9 (100%)
Pension Committee (Chair) (2002)	5/5 (100%)

**YOUR VOTE IS EXTREMELY IMPORTANT. VOTE ONLY THE BLUE PROXY.**  
***For questions or assistance, please call Georgeson at 1-866-909-6468.***

## Incumbent Directors Whose Terms Continue Beyond the Meeting



MARY N. BALES,  
M.A., M. Phil  
Kitchener, ON  
Canada  
Age: 68  
**Independent**

Ms. Bales studied at Purdue University and New Mexico State University before completing two graduate degrees at the University of Waterloo. Ms. Bales has been a leading realtor in the Kitchener-Waterloo area since 1974, presently with Coldwell Banker Peter Benninger Realty. She served as a Governor on the Board of the University of Waterloo for 12 years where she chaired its Building and Properties Committee. Her leadership activities also include Boards of the United Way, the Grand River Hospital, the YWCA and Centre in the Square. In response to the serious need for more affordable housing in our community, Ms. Bales established Heartwood Place in 2001. Her accomplishments have been recognized by the Governor General with a Meritorious Service Medal in 2006 and by the University of Waterloo with an honorary Doctor of Laws degree in 2010.

<b>Year Joined Board and Committees</b>	<b>Attendance</b>
Board (1997)	12/14 (86%)
Corporate Governance and Conduct Review Committee (1997)	11/12 (92%)
Human Resources and Compensation Committee (1997)	5/5 (100%)
Selection Committee (2010)	10/10 (100%)
Special Committee (2010)	7/9 (78%)



A. SCOTT CARSON,  
Ph.D.  
Kingston, ON  
Canada  
Age: 61  
**Independent**

Dr. Carson is a Professor of Strategy and until April 30, 2011 is the Director of the MBA Program at the Queen's School of Business, Queen's University. Prior to that he was Dean at both the School of Business & Economics at Wilfrid Laurier University and the Sobey School of Business at Saint Mary's University, Halifax, Nova Scotia. As well, he was Chair of the Canadian Federation of Business School Deans. While on leave from Wilfrid Laurier, he was Chief Executive Officer of the Ontario Government's Privatization Secretariat. He was also Vice President and Head of Corporate Finance for CIBC. Dr. Carson is a past Chair of the Greater Kitchener Waterloo Chamber of Commerce, and he has been on a number of corporate and not-for-profit boards. Dr. Carson is a graduate of Mount Allison and Dalhousie universities, and holds a PhD from the University of London. He is a frequent author and speaker on business ethics, corporate social responsibility and corporate governance.

<b>Year Joined Board and Committees</b>	<b>Attendance</b>
Board (2000)	14/14 (100%)
Audit Committee (2000)	4/4 (100%)
Corporate Governance and Conduct Review Committee (Chair) (2010)	12/12 (100%)
Selection Committee (2010)	10/10 (100%)

**YOUR VOTE IS EXTREMELY IMPORTANT. VOTE ONLY THE BLUE PROXY.**  
**For questions or assistance, please call Georgeson at 1-866-909-6468.**

## Incumbent Directors Whose Terms Continue Beyond the Meeting



GERALD A.  
HOOPER,  
FCA  
Waterloo, ON  
Canada  
Age: 67  
**Independent**

Mr. Hooper is Chairman of the Board of the Company and is a Director of Wescast Industries Inc. He is a Fellow of the Institute of Chartered Accountants of Ontario. Mr. Hooper was at Schneider Foods for 19 years where he last served as Executive Vice President and Chief Financial Officer as well as a member of the Board. Following the acquisition of Schneider Foods in 2003, Mr. Hooper was Executive Vice President of Maple Leaf Foods until his retirement in 2005. From 1975 to 1986 he was a Partner at what is now KPMG. Mr. Hooper also serves on the Finance and Investment Committee of the University of Waterloo. Mr. Hooper has served on a number of corporate and not-for-profit boards, and has attended programs in effective board leadership at the Directors College of McMaster University's DeGroote School of Business. His directorships have included ATS Automation Tooling Systems Inc. (2005-2007), Schneider Corporation, Brick Brewing Co. Limited and Wescast Industries (2006-present).

Year Joined Board and Committees	Attendance
Board (Chair) (2000)	14/14/ (100%)
Audit Committee	4/4 (100%)
Corporate Governance and Conduct Review Committee (2005)	12/12 (100%)
Human Resources and Compensation Committee (2005)	5/5 (100%)
Investment Committee (2005)	4/4 (100%)
Pension Committee (2000)	5/5 (100%)
Selection Committee	10/10 (100%)



CHARLES M. W.  
ORMSTON,  
MBA  
Waterloo, ON  
Canada  
Age: 59  
**Independent**

Mr. Ormston is the Chair of the Company's Human Resources and Compensation Committee. He is President of CMW Ormston Holdings Inc., a privately held asset management company. He spent 20 years in the distribution of industrial gases and welding supplies, as well as the medical supply business. In that capacity, he served as a past President of the National Welding Supply Association, Canadian zone. He is a past President of the Kitchener and Waterloo Community Foundation, and a past Director of the Walter Bean Grand River Community Trails Corp. and Foundation, the Grand River Conservation Foundation, the Ontario Hunter Jumper Association and the Ontario Equestrian Federation. Mr. Ormston graduated from the Institute of Corporate Directors' Education Program at the Rotman School of Management, University of Toronto, in 2007. He also holds a MBA from McMaster University. Mr. Ormston has been named a Paul Harris Fellow, an Honorary Member of the Canadian Fighter Pilots Association and an Honorary Senior Fellow of Renison College. He is also a past member of the Young Presidents' Organization and the World Presidents' Organization.

Year Joined Board and Committees	Attendance
Board (1995)	14/14/ (100%)
Corporate Governance and Conduct Review Committee (1995)	12/12 (100%)
Human Resources and Compensation Committee (Chair) (1995)	5/5 (100%)
Selection Committee (2010)	10/10 (100%)
Special Committee (2010)	9/9 (100%)

**YOUR VOTE IS EXTREMELY IMPORTANT. VOTE ONLY THE BLUE PROXY.**  
**For questions or assistance, please call Georgeson at 1-866-909-6468.**

## Incumbent Directors Whose Terms Continue Beyond the Meeting



MICHAEL P.  
STRAMAGLIA, FSA,  
FCIA, CERA  
Toronto, ON  
Canada  
Age: 51  
**Independent**

Mr. Stramaglia chairs the Company's Investment Committee. He is currently Executive Vice-President and Chief Risk Officer for Sun Life Financial, which he joined in 2002 following its acquisition of Clarica, where Mr. Stramaglia held the position of Executive Vice-President, Reinsurance and Chief Investment Officer. He previously served as President & CEO of Zurich Life Insurance Company of Canada and President & COO of Zurich Financial Services Ltd.'s consolidated Canadian P&C and life insurance operations. He has served on the boards of various financial services companies including Zurich Life Insurance Company of Canada, Sun Life Financial Trust and Perigee Inc.

Mr. Stramaglia is a qualified actuary and Chartered Enterprise Risk Analyst. He holds an Honours Bachelor of Mathematics degree from the University of Waterloo, where he serves on the Advisory Board for the Masters in Actuarial Science program.

Year Joined Board and Committees	Attendance <sup>2</sup>
Board (2010)	11/11 (100%)
Investment Committee (Chair) (2010)	3/3 (100%)
Pension Committee (2010)	4/4 (100%)



KATHERINE A.  
MABE,  
CPCU, CLU, ChFC,  
MBA  
Waterloo, Ontario,  
Canada  
Age: 52  
**Non-Independent**

Ms. Mabe is the President and Chief Executive Officer of The Economical Insurance Group. Kathy has over 32 years of experience in the property and casualty industry. She has held many senior leadership roles in the insurance industry including President of the Specialty Products Division of Nationwide Insurance, President and Chief Executive Officer of Titan Insurance Company and Victoria Insurance Company, and President of Nationwide Insurance Western Operations: divisions of Nationwide, a leading property and casualty insurer in the U.S.

Ms. Mabe earned a Bachelor of Arts degree in Communications and a Master of Business Administration degree and holds several designations including: Chartered Property Casualty Underwriter (CPCU); Chartered Life Underwriter (CLU); Chartered Financial Consultant (ChFC); and Associate in Risk Management (ARM).

Year Joined Board and Committees	Attendance
Board (2011) <sup>3</sup>	N/A
Investment Committee (2011)	N/A

<sup>2</sup> Of meetings held during his 2010 tenure as director.

<sup>3</sup> Ms. Mabe was not a director in 2010.

**YOUR VOTE IS EXTREMELY IMPORTANT. VOTE ONLY THE BLUE PROXY.**  
**For questions or assistance, please call Georgeson at 1-866-909-6468.**

## Directors Who Retired In 2010 Or Who Will Retire As Of The Meeting Date And Who Are Not Up For Election



NOEL G. WALPOLE  
Kitchener, Ontario,  
Canada  
Age: 66  
**Non-Independent**

Mr. Walpole was appointed President and Chief Executive Officer of The Economical Insurance Group in January 1995. He began his career in the insurance industry in 1969 as a Claims Adjuster for SAFECO Insurance Company in Toronto. During his 15 years there, Mr. Walpole was National Claims Manager, National Underwriting Manager and then National Marketing Manager. Other past experience includes: Resident Vice President for the Central Region of Fireman's Fund (which became Wellington Insurance Company), and Partner at Halton-Caird Insurance Brokers. From 1986 until he joined The Economical Insurance Group, Mr. Walpole was President and CEO of AXA Insurance Company. In addition to his membership on the Company's Board of Directors where he is the Chairman of the Investment Committee, Mr. Walpole holds, or has held, directorships for: Facility Association, Insurance Bureau of Canada, Centre for Study of Insurance Operations, Chairman of The Insurance Institute of Canada, Underwriters Adjustment Bureau, Insurers' Advisory Organization and Member of the Dean's Advisory Council, School of Business and Economics for Wilfrid Laurier University.

Year Joined Board and Committees	Attendance
Board (1995)	11/14 (79%)
Investment Committee (Chair) <sup>4</sup> (1995)	4/4 (100%)



TERRENCE J.  
REIDEL,  
FCA  
Kitchener, Ontario,  
Canada  
Age: 67  
**Independent**

Mr. Reidel is the former President of Kuntz Electroplating Inc. and is the Chair of Cowan Holdco. Prior to that he was a Partner of the international accounting firm of Ernst and Young. Mr. Reidel is currently the Chairman of Com Dev International, is a member of the Board of Directors of Linamar Corporation and a former member of the Board of Governors of Wilfrid Laurier University. Mr. Reidel is also the Executive Director of the Frank Cowan Foundation. He was formerly the Executive Director of the Waterloo Region Manufacturing Innovation Network, Treasurer of the Conservative Business Association of Waterloo Region, and was a member of the Executive Committee of the Greater Kitchener Waterloo Chamber of Commerce. In 2005, Mr. Reidel was named Kitchener-Waterloo Citizen of the year.

Year Joined Board and Committees	Attendance
Board (2005)	13/14 (93%)
Audit Committee (2005) (Chair) (2010)	4/4 (100%)
Human Resources and Compensation Committee (2005)	5/5 (100%)
Selection Committee (2010)	10/10 (100%)

<sup>4</sup> Until his resignation in 2010

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## Directors Who Retired In 2010 Or Who Will Retire As Of The Meeting Date And Who Are Not Up For Election



Mr. Ruby is Chairman of Krug Inc., and was President of Krug Inc. for many years. He has served on the boards of a number of companies, including Schneider Foods and was Chair of their Audit Committee. He has also served on the boards of many local charitable organizations, and was Chair of the One Voice One Vision joint hospital campaign for the three hospitals of Waterloo Region. He is currently Chair of the Waterloo Region Hospitals Foundation. In 2003 Mr. Ruby was named Kitchener-Waterloo Citizen of the Year.

BRIAN J. RUBY,  
FCA  
Kitchener, Ontario,  
Canada  
Age: 71  
**Independent**

Year Joined Board and Committees	Attendance <sup>5</sup>
Board (1989)	3/3 (100%)
Audit Committee (Chair) <sup>6</sup> (1989)	1/1 (100%)
Investment Committee (1995)	1/1 (100%)
Pension Committee (2006)	1/1 (100%)

### ***Additional Disclosure Relating to Directors***

To the knowledge of the Company, no proposed director of the Company is or has been, within the last 10 years, (a) subject to a cease trade or similar order or an order that denied the relevant company access to any exemption under securities legislation, for a period of more than 30 consecutive days, that was issued while acting in the capacity of director, chief executive officer or chief financial officer of any company; (b) subject to a cease trade or similar order or an order that denied the relevant company access to any exemption under securities legislation, for a period of more than 30 consecutive days, that was issued after he/she ceased to be a director, chief executive officer or chief financial officer and which resulted from an event that occurred while he/she was acting in that capacity. Moreover, to the knowledge of the Company, no proposed director is or has been, within the last 10 years, (a) bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency, or became subject to or instituted any proceedings, arrangement or compromise with creditors, or had a receiver, receiver manager or trustee appointed to hold his/her assets; or (b) a director or executive officer of any company that, while he/she was acting in that capacity, or within a year of his/her ceasing to act in that capacity, became bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency or was subject to or instituted any proceedings, arrangement or compromise with creditors or had a receiver, receiver manager or trustee appointed to hold its assets. Each of the following current directors holds a Mutual Policy: Dr. Carson, Ms. Gavan, Mr. MacIntosh, Mr. Hooper, Mr. Ormston and Mr. Reidel.

<sup>5</sup> Of meetings held during his 2010 tenure as director.

<sup>6</sup> Until his resignation in 2010.

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### ***Directors' Compensation for 2010***

The director compensation program compensates non-executive directors for the time and effort they must devote to Company matters.

The directors' compensation program is as follows:

- An annual Board retainer of \$30,000;
- An annual retainer of \$125,000 for the Chair of the Board;
- An annual retainer of \$6,250 for Committee Chairs, other than for the Audit Committee Chair who was paid an annual retainer of \$13,500;
- For the last quarter of 2010, a quarterly retainer of \$5,000 for the Special Committee Chair;
- An attendance fee of \$1,500 (\$750 if attendance by phone) per Board meeting (\$2,500 for an all day meeting);
- An attendance fee of \$1,500 (\$750 if attendance by phone) per Committee meeting (\$2,500 for an all day meeting); and
- Reimbursement for transportation, lodging, meals and business expenses in accordance with the Company's policy for reimbursing such expenses for Executives.

Annually, the Human Resources and Compensation Committee reviews the directors' compensation against the Canadian Spencer Stuart Board Index, a leading survey on director compensation. The Spencer Stuart Board Index is usually available for the previous year early in the following year from [www.spencerstuart.com](http://www.spencerstuart.com).

The retainers, meeting fees, and annual compensation for the Chair of the Board, Committee Chairs, and other Board members are compared to the benchmarks in the survey data. This analysis takes into account the number of Board and committee meetings each year.

The directors' compensation for 2010 was below the "cap" on directors' compensation set out in the By-laws of Economical.

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The total remuneration paid to directors during the year ended December 31, 2010, other than directors who also serve as officers of Economical<sup>(1)</sup>, is set out in the table below.<sup>(2)</sup>

Name	Retainer and Attendance Fees Earned (\$)	Other Compensation (\$)	Total Compensation (\$)
Mary N. Bales	\$78,750	Nil	\$78,570
A. Scott Carson	\$87,375	Nil	\$87,375
Karen L. Gavan	\$68,875	Nil	\$68,875
Gerald A. Hooper	\$235,125	Nil	\$235,125
David A. MacIntosh	\$68,875	Nil	\$68,875
Charles M.W. Ormston	\$95,125	Nil	\$95,125
Terrence J. Reidel	\$81,500	Nil	\$81,500
Brian J. Ruby <sup>(3)</sup>	\$41,250	Nil	\$41,250
Michael P. Stramaglia	\$33,500	Nil	\$33,500

Notes:

- (1) Ms. Mabe's and Mr. Walpole's compensation are set out in the section "Compensation Discussion and Analysis". Directors' compensation is not and has not been in the past, paid to directors who serve as officers of Economical or its affiliates.
- (2) Fees earned in the fourth quarter of 2009 were paid in the first quarter of 2010. Such fees are accounted for in this table. Fees earned in the last quarter of 2010 and paid in the first quarter of 2011 are not.
- (3) Mr. Ruby retired from the board during the second quarter of 2010.

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## **6. CORPORATE GOVERNANCE**

The main responsibility of the Board is to manage or supervise the management of the business and affairs of Economical. The Board has delegated to the Chief Executive Officer of Economical (the “CEO”) many of the Board’s powers and much of the Board’s authority to manage the business and affairs of Economical. The Board has assumed the duty to supervise the CEO’s management of the business and affairs of Economical. Schedule “A” sets out Canadian governance best practices as suggested in National Policy 58-201 Corporate Governance Guidelines, and Economical’s compliance therewith.

### **BOARD MANDATE**

The Board reviews and approves the strategic plan and the corporate objectives of Economical, supervises management of Economical and ensures succession planning, identifies risks and assesses their impact on the business and affairs of Economical, and ensures that adequate controls exist in relation to business ethics, compliance and corporate governance issues, including monitoring of conflicts of interest. Schedule “A” sets out the overriding statement of governance principles and the ethical principles of Economical.

The mandate of the Board is provided with this Circular. Under the *Insurance Companies Act*, the directors are required to oversee the management of Economical’s business and affairs, and in doing so to act honestly and in good faith with a view to the best interests of Economical. In addition, each director must exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

The Board annually reviews and approves Economical’s operating plan and budget. The Board monitors Economical’s performance against plan and budget at least quarterly through review and discussion with Management. Through its Audit Committee, the Board oversees the integrity of Economical’s internal financial controls and management information systems.

Management is expected to provide effective leadership in all aspects of Economical’s activities, to maintain Economical’s corporate culture and motivate its employees, and to communicate effectively with employees, brokers, policyholders and other industry participants. The Board also expects Management to provide the directors on a timely basis with information concerning Economical’s business and affairs, including financial and operating information and information concerning industry developments as they occur, all with a view to enabling the Board to discharge its stewardship obligations effectively.

The Chair of the Board is independent. The Board holds regular meetings no less than quarterly. Between these meetings, the Board meets as required, generally by means of telephone conferencing facilities. As part of these meetings, the independent directors also meet separately from Management. Management also communicates informally with members of the Board on a regular basis, and solicits the advice of Board members on matters falling within their special knowledge or experience.

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## Board Committees

In carrying out its mandate, the Board delegates certain of its functions to committees of the Board (“Committees”) and these Committees are responsible for specific aspects of the Board Mandate and reporting their recommendations to the Board. The Board, the Committees and their members may retain independent consultants to advise them.

The Board has five committees at this time: Audit Committee; Corporate Governance and Conduct Review Committee (“CGCR Committee”); Human Resources and Compensation Committee (“HR Committee”); Investment Committee; and Special Committee. The duties of the Pension Committee that was active in 2010 have been split between the Investment Committee and the Human Resources and Compensation Committee and the Pension Committee has been dissolved. The Selection Committee that was required in 2010 to assist in the search for a new CEO has also been dissolved for 2011.

## AUDIT COMMITTEE

The Audit Committee is required to obtain and maintain reasonable assurance that the senior officers of Economical, the Board and Economical meet all financial reporting and disclosure obligations imposed on them by financial reporting rules. The 2011 mandate of the Audit Committee is provided with this Circular. Economical’s Audit Committee is currently composed of four independent directors, Messrs. Reidel (Chair), Carson, Hooper and Ms. Gavan, all of whom meet the financial literacy criteria under section 1.6 of Multilateral Instrument 52-110 – Audit Committees. Mr. Reidel (Chair) will be retiring as of the Meeting date. It is intended that he will be replaced as Chair by Ms. Gavan. It is intended that after the Meeting, Mr. Stramaglia shall be appointed to the Audit Committee. The Audit Committee is responsible for, among other matters:

- (a) annually assessing the quality and sufficiency of the Company’s accounting and financial personnel;
- (b) overseeing and regularly assessing the quality of the work of the external auditor in preparing or issuing an audit or other report in respect of the Company’s financial statements and performing other audit, review or attest services for the Company;
- (c) overseeing and regularly assessing the quality of the work of the internal auditor in preparing or issuing an audit or other report in respect of audit, review or attest services for the Company;
- (d) reviewing the Company’s audited financial statements for the purpose of gaining reasonable assurance as to whether each audited financial statement of the Company (including all returns prescribed by the *Insurance Companies Act* (Canada) and the Office of the Superintendent of Financial Institutions) presents fairly, in all material respects, the financial position of the Company, the results of its operations and its cash flows in accordance with IFRS;
- (e) reviewing financial statements and Management’s Discussion & Analysis (“MD&A”) for the purpose of gaining reasonable assurance that current year comparative financial statements of the Company and related MD&A have been composed as required by the laws, regulations, rules, policies and other requirements relating to financial reporting and disclosure promulgated by

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governments, and other agencies and instrumentalities having jurisdiction over the Company;

- (f) satisfying themselves as to the independence of the external auditor and the internal auditor, recommending the external auditor to the Board and the compensation such would receive;
- (g) ensuring that the Company's unearned premium reserves and claims liabilities are fairly stated and that the present and future solvency of the Company is regularly assessed;
- (h) gaining and maintaining reasonable assurance that the Company is in compliance with its obligations under tax, employment and similar laws and regulations, and obtaining quarterly reports from Management as to such compliance; and
- (i) gaining and maintaining reasonable assurance that each current year comparative financial statements of the Company and related MD&A are filed with all regulators in compliance with financial reporting rules, and obtaining assurance from Management as to such filings.

Economical's Audit Committee met four times during fiscal 2010 and will meet at least four times during fiscal 2011.

#### **CORPORATE GOVERNANCE AND CONDUCT REVIEW COMMITTEE MANDATE**

The 2011 mandate of the CGCR Committee sets out the authority, composition, operating procedures and responsibilities of the CGCR Committee and is included with this Circular. Economical's CGCR Committee is currently composed of 4 independent directors, Messrs. Carson (Chair), Hooper, Ormston and Ms. Bales. Dr. Carson teaches, and is a frequent speaker at international meetings and conferences on, the subjects of corporate social responsibility and corporate governance. His teaching in the Queen's University corporate governance executive programs focuses on strategic risk and controls. The CGCR Committee is responsible for, among other matters:

- (j) developing and recommending to the Board the Company's corporate governance practices and principles;
- (k) upon recommendation from the Human Resources and Compensation Committee, recommending to the Board for approval an appropriate framework for the compensation of directors;
- (l) ensuring an appropriate process for director education and orientation;
- (m) annually reviewing and recommending the Code of Business Conduct policy;
- (n) approving and recommending to the Board the annual Conduct Review Report for delivery to the Office of the Superintendent of Financial Institutions;
- (o) approving and recommending to the Board a Corporate Social Responsibility Policy (the "CSR Policy") for the Company and monitoring adherence to the CSR Policy;

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- (p) designing and maintaining the Company's complaint processes for employees;
- (q) nominating qualified individuals as nominees for election to the Board;
- (r) evaluating the effectiveness and independence of the Board, Committees of the Board and individual directors; and
- (s) monitoring, reviewing annually and recommending to the Board for approval the form and amount of the directors' remuneration for Board and committee service.

Economical's CGCR Committee met twelve times during fiscal 2010 and will meet at least three times during fiscal 2011.

### ***Director Orientation and Education***

The CGCR Committee develops, reviews and evaluates on an annual basis the Board's processes for orientation and education of directors. The CGCR Committee ensures that each new director participates in a comprehensive orientation process in relation to his or her Board responsibilities, the role of the Board and its committees, and the contributions and commitment of time and resources that Economical expects each individual director will make.

Relevant orientation and continuing education is available to all directors to enable the directors to maintain or enhance their skills and capabilities as directors and to maintain the currency of their knowledge and comprehension of Economical's business including the opportunity to attend conferences, seminars, courses or other educational experiences which are intended to expand the director's knowledge and skills.

### ***Ethical Business Conduct***

The CGCR Committee is responsible for annually reviewing and recommending the Code of Business Conduct policy and monitoring compliance with this code.

A description of Economical's expectations regarding its Ethical Code of Conduct is contained on Schedule "A" hereto. A copy of the code can be obtained from the Senior Vice President, Chief Human Resources Officer.

The CGCR Committee establishes the tone of ethical conduct for new directors by including integrity as an essential skill in its board competency matrix and by emphasising to candidates the priority placed on ethical conduct on the Board. The CGCR Committee supervises the Board self-assessment process that is undertaken bi-annually by the Board with the support of an external consulting firm. The review process allows for any board member to identify or raise concerns of an ethical nature. As a part of this process, the Chair of the Board interviews each director individually thus allowing ethical concerns to be raised.

The CGCR Committee has been very active in promoting both and Corporate Social Responsibility strategy and "Whistleblower" policy within Economical. The Whistleblower policy is in place for 2011 and the corporate social responsibility strategy is currently being developed with the assistance of external consultants.

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## **Nomination of Directors**

The CGCR Committee in its role of nominating committee recommends qualified individuals as nominees for election to the Board when there are vacancies at a meeting of members of the Company and for appointment by the Board to fill any vacancies in the Board. The CGCR Committee has retained independent Human Resource search firms, such as Spencer Stuart, as consultants to assist the CGCR Committee in identifying appropriate selection criteria for prospective Board members and in conducting an active search for qualified candidates the CGCR Committee recommends the prospective candidates to the Board.

To assist the CGCR Committee, executive search firms such as Spencer Stuart and Odgers Berndtson, have been retained as external consultants. The consultants assist the CGCR Committee both in identifying appropriate selection criteria for prospective Board members and in conducting an active search for qualified candidates. The CGCR Committee recommends the prospective candidates to the Board. Board approved candidates are proposed to the Members for election at each annual general meeting.

As part of the process, the CGCR Committee considers the competencies and skills of the Board, as a whole, and required competencies and skills from new members. Candidates are screened to ensure they have the following attributes: integrity, judgment, financial literacy, excellent communication skills and the ability to act as a team player. They are also screened to determine their independence or to identify conflicts of interest. To help the CGCR Committee in identifying the right Board candidates, a skills matrix is used by the CGCR Committee to prioritize the required talents and skills of potential directors.

The CGCR Committee also determines whether the current directors individually or collectively possess the requisite competencies and skills required of directors, and where the Board determines that it, as a whole, does not possess all of the requisite competencies and skills, the CGCR Committee will either take the appropriate steps to enable one or more of the current directors to develop such competencies and skills or take the appropriate steps to recommend the election or appointment of one or more individuals to the Board who have them.

The CGCR Committee is also responsible for identifying and maintaining a list of candidates qualified to become new directors.

## **Assessments**

Bi-annually, the Board and each committee reviews their own mandates. The mandates and any revisions are approved by the full Board.

Annually, the Board and each committee of the Board assess their performance during the year in relation to requirements of their mandates. Once the Board and committees have approved their own annual mandate assessments, those assessments are sent to the CGCR Committee for final approval and subsequent forwarding to the Board Chair for the purpose of reporting to the Members at each annual general meeting.

Bi-annually, the Board undertakes a self-assessment process. This process is overseen by the CGCR Committee and is executed with the assistance of an external consulting firm such as Deloitte LLP. Through a process of both questionnaires and interviews with external consultants, the Board and committee members assess both the performance of the Board and of each committee on which an individual Board member sits.

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In addition, each Board member assesses his or her individual performance on both the Board and committees on which they sit.

Further, the each Board member evaluates the Board Chair and the committee chairs on which they sit.

Finally, the Board Chair meets with each Board member to discuss his or her own performance. The performance of the Board Chair is reviewed by the Chair of the CGCR Committee and other Committee members as appropriate.

All discussions between the Board Chair and Board members are guided by the principles of frank, open and honest disclosure.

Additionally, the CGCR Committee conducts, not less than bi-annually, an evaluation of whether the Board has appropriate composition and procedures to allow it to function independently from management. It also reviews at least bi-annually the effectiveness of the composition and membership of each such Board Committee, and whether there is a need for cross appointments to promote greater committee effectiveness. Considerations are among other things:

- (i) the directors' position description;
- (ii) the competencies and skills each individual director is expected to bring to the Board, including the financial literacy and expertise of each individual director;
- (iii) each individual director's continuing qualification under the *Insurance Companies Act* and other applicable laws, rules and policies; and
- (iv) the continuing validity of the assumptions underlying the appointment of each individual director;

## **HUMAN RESOURCES AND COMPENSATION COMMITTEE**

Economical's Human Resources and Compensation Committee is required to obtain and maintain reasonable assurance that there exists within Economical effective policies and practices to enable Economical to attract, develop and retain the human resources required by Economical to meet its objectives. The HR Committee currently consists of four independent directors, Messrs. Ormston (Chair), Reidel, Hooper and Ms. Bales. Mr. Reidel will be retiring as of the Meeting date and Mr. Bowey will be taking his place. The 2011 mandate of the HR Committee is included with this Circular. The HR Committee engages independent consultants such as Mercer to assist with its mandate. The HR Committee is responsible for, among other matters:

- (a) reviewing and recommending to the Board the appointment and terms of employment of officers, including the design of short-term, long-term and other incentive plans;
- (b) recommending to the CGCR Committee the form and amount of directors' compensation;
- (c) reviewing and approving profit sharing or other incentive awards to eligible employees;

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- (d) reviewing at least annually the Company's compensation philosophy and the general design and make-up of its broadly applicable benefit programs as to their general adequacy, competitiveness, internal equity and cost effectiveness;
- (e) overseeing the annual appraisal of the CEO's performance;
- (f) ensuring that there are procedures in place to monitor the Pension Plans compliance with the *Pension Benefits Act* (Ontario), the *Quebec Supplemental Pension Plans Act*, the *Income Tax Act* (Canada) and their respective regulations;
- (g) ensuring that periodic reports addressing the health and safety of the Company's employees are prepared and reviewed by the Committee; and
- (h) succession planning related to officers of the Company.

The HR Committee met five times during fiscal 2010 and will meet at least three times during fiscal 2011.

## INVESTMENT COMMITTEE

The Investment Committee is required to gain and maintain reasonable assurance that the strategic, operational, reporting and compliance risks of Economical's investment portfolio are identified in a timely manner and are effectively assessed, monitored and managed. The Economical Investment Committee consists of Ms. Mabe and three independent directors, Messrs. Stramaglia (Chair), MacIntosh and Hooper. The 2011 mandate of the Investment Committee is included with this Circular. The Investment Committee is responsible for, among other matters:

at least annually, reviewing the Statement of Investment Policies and Procedures ("SIP&P") and the Statement of Investment Policies and Procedures for the Company's staff pension plan ("Pension Plan SIP&P"), and upon agreement, recommending the SIP&P and Pension Plan SIP&P to the Board for approval;

in respect of the SIP&P,

- (i) reviewing, approving and monitoring ongoing performance against the annual investment plan;
- (ii) reviewing every quarter, the investment portfolio and asset/liability performance against approved investment benchmarks and objectives;
- (iii) reviewing management's assessment of the economic, capital markets and regulatory environment and the implications of these on the company's investment plans and operations;
- (iv) at least annually, reviewing the investment holdings of the Company's consolidated portfolio;
- (v) reviewing any matters raised within the scope of this mandate in connection with any internal audits or regulatory reviews, including management's responses or recommendations; and

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- (vi) reviewing investment related implications of material transactions, including mergers and acquisitions, that have been recommended to the Board for approval;

in respect of the Pension Plan SIP&P;

- (i) at least annually reviewing and upon agreement approving the sections of the pension Governance Manual dealing with roles, responsibilities and accountability of pension plan investment managers;
- (ii) reviewing every quarter, the asset mix and investment performance of the defined benefit pension plan;
- (iii) reviewing semi-annually, the investment performance and range of investment options relating to the Defined Contribution pension plan; and
- (iv) initiating, terminating or modifying investment manager mandates as required in order to reflect issues relating to long term investment performance or changes in the investment direction and scope as set out in the Pension Plan SIP&P.

The Investment Committee met three times in 2010 and will meet at least four times in 2011.

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## **7. COMPENSATION DISCUSSION AND ANALYSIS**

The following has been prepared to enhance the quality and transparency of Economical's executive compensation disclosure. It provides explanations regarding the objectives and implementation of Economical's executive pay programs.

### **INTRODUCTION**

The Board has mandated the HR Committee (in this section, the "Committee") to supervise and approve or recommend to the Board the human resources practices and policies of Economical that support the Economical's mission, overall strategy, and objectives. The values guiding Economical in achieving its objectives are: customer focus, integrity, achievement, collaboration, and learning. The total rewards philosophy described below supports the Economical's mission as well as its values.

### **TOTAL REWARDS PHILOSOPHY**

Behind each of Economical's products and services are employees who are engaged, talented, and hard-working. An organization with a high performance culture exhibits systems of reward that are fair, equitable, motivating, and subject to regular review to ensure competitiveness and cost-effectiveness. The compensation systems are linked to performance and reward for those who exhibit sustained levels of contribution that exceed the norm. Economical's total rewards philosophy offers employees pay, benefits, work environment, and learning and development programs. The total rewards strategy is a component of the total human resources strategy which supports and changes with the overall corporate direction and strategy. Economical's rewards strategy ensures that compensation is:

- Internally equitable - Provides equal pay for work of equal value by evaluating positions relative to each other;
- Externally competitive - Aligns with the median market rate for employees and a range between market 50<sup>th</sup> and 75<sup>th</sup> percentile rate for Executives and Senior Executives by analyzing compensation data from labour markets in which we participate
- Affordable - Falls within reasonable and financially responsible budgetary parameters approved by the Board.

To be successful, the Company must attract, retain and motivate talented executives and senior executives in a highly competitive business environment. The Committee wants Economical's leaders to focus on sustaining high levels of performance, reinforcing the pay-for-performance philosophy. Senior Executives play a key role in meeting Economical's objectives. The review, assessment and approval of the Senior Executives' compensation is one of the main functions of the Committee. Economical's executive compensation strategy relative to the market is influenced by a number of factors including:

- The nature of Executive and Senior Executive roles (some being insurance-specific roles);
- Economical's business strategies;
- Economical's mutual company status; and

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- The working location of the executive team (Head Office is in Waterloo, Ontario).

Objectives of the Executive compensation package are the following:

1. To attract and retain executive talent - The fundamental role of the senior positions in Economical is to provide leadership. This leadership includes recommending strategic direction and focus, developing business action plans, monitoring plan implementation and delivering successful results. To support the attraction and retention of the people that have the talent to fill senior positions, Economical provides:
  - Competitive base salaries that recognize the organization's size and location;
  - Competitive incentive-based variable compensation that focuses on annual business plans and strategic directions; and
  - Employment benefit, pension, and perquisite arrangements that are comparable within the Canadian property and casualty insurance industry and community.
2. To reward performance that contributes to business success – Economical provides:
  - Rewards for executives based on successful business results and the position levels;
  - Rewards for executives based on individual contributions for the period under review.
3. To recognize internal equity – Economical recognizes that internal equity is an important element in maintaining individual compensation that is perceived as fair. It also recognizes that executive positions have a unique value to Economical and that market trends and status can also contribute toward the compensation elements.

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## SIGNIFICANT CHANGES IN ORGANIZATIONAL STRUCTURE SINCE DECEMBER 31, 2010

The Economical Group's organizational structure has changed significantly since the end of 2010 with the retirement of the former CEO (Noel Walpole) and the leadership of the new CEO (Katherine Mabe). There are significant changes to a number of the Named Executive Officers (each a "NEO" as defined in Form 51-102F6) in this document as outlined in the following table.

Name	Comments
Noel Walpole, President & CEO	Retired December 31, 2010
Katherine Mabe, President & CEO	Hired November 15, 2010
Sandeep Uppal, SVP and Chief Financial Officer	Separated January 6, 2011
Jorge Arruda, SVP, Operations	Change in role to SVP, Strategic Business Units and Delivery Management effective January 24, 2011
Linda Goss, SVP and Chief Actuary	No change
Dean Bulloch, VP, Human Resources	Change in role to SVP and CHRO effective January 24, 2011
David Crozier, SVP, Operations	Appointment to role SVP, Operations, effective January 24, 2011

## COMPONENTS OF THE COMPENSATION OF EXECUTIVES OF ECONOMICAL

The executive compensation package applies to all of the Company's executives (Vice-Presidents, referred to as "Executives" in this Circular, account for approximately 10 positions) and senior executives (Senior Vice-Presidents and above referred to as "Senior Executives" in this Circular, account for approximately 8 positions). It is designed to assist the Company in attracting and retaining the best available personnel for positions of substantial responsibility. Each year the Company reviews its compensation package (the Committee reviews the compensation of Senior Executives and Executives) to ensure alignment with the compensation philosophy. The Committee also reviews the compensation philosophy on a yearly basis. The following components are part of the executive compensation package: base salary, short term incentive plan, long term incentive plan, pension and benefits, and perquisites. These are detailed in the pages that follow.

### 1. **Base Salary**

- Goal: To provide attractive and equitable fixed compensation based on the external market as well as internal equity with respect to the role, scope, responsibilities and accountabilities within Economical, and the experience and performance of the individual in the role.

Compensation Element	Type	Audience	Performance	Payouts based on	Market Positioning
Base Salary	Cash	All Executives	Annual	Adjustments based on individual performance and market trends	Range = Between 50 <sup>th</sup> and 75 <sup>th</sup> Percentile

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- Administration: Salaries are reviewed once a year by the Committee, with an effective date of the first payday in March for employees, Executives, and Senior Executives. While base pay levels are between the 50<sup>th</sup> and the 75<sup>th</sup> percentile of the target market, short term incentive, long term incentive, pension and benefits and perquisite targets are at the market median. Actual total compensation may be above market median for the best performers when expectations in terms of growth, combined ratios (expenses and claims ratios) and return on equity ("ROE") performance are met or exceeded.
- Market Comparators: The market which the Company compares executive compensation varies by the nature of its executive roles. To the extent possible, all executive roles are matched to the Canadian P&C market. The Company also considers the broader financial services market for non-insurance roles, such as:
  - Senior Vice-President and Chief Financial Officer
  - Senior Vice-President and Chief Information Officer
  - Senior Vice-President and Chief Human Resources Officer
  - Vice-President, Information Technology Delivery and Operations
  - Vice-President, Finance and Controller
- To assess the value of compensation for insurance-related Executives and Senior Executives, the Company participates in an annual survey conducted by Towers Watson, which survey provides aggregate benchmarks and trends for the participants in the survey. The participants, consisting of property and casualty insurance companies in the Canadian market, are the following companies:
  1. Allstate Insurance Company of Canada
  2. Aviva Canada
  3. AXA Canada Inc.
  4. Chubb Insurance Company of Canada
  5. Co-operators General Insurance Company
  6. Dominion of Canada General Insurance
  7. Gore Mutual Insurance Company
  8. Intact Financial
  9. Lombard Canada
  10. Mouvement Desjardins (Desjardins General Insurance Group)
  11. RBC Insurance Company
  12. Royal & Sun Alliance Insurance Company of Canada
  13. State Farm Insurance
  14. Wawanesa Mutual Insurance Company
  15. Zurich Canada

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The scope of the comparator group compares to that of Economical as follows:

	2009 Revenues (\$M) <sup>(1)</sup>	2010 Employees
<b>25th Percentile</b>	596	1,325
<b>Median</b>	819	2,000
<b>75th Percentile</b>	1,425	2,979
<b>Economical</b>	1,809	2,655 <sup>(2)</sup>

Notes:

(1) Comparative 2010 Revenues were not available at the time of this writing.

(2) Includes 100 employees of Family Insurance Solutions Inc.

The comparator group is composed of major Canadian P&C companies of comparable size, scope and geographic span.

The 2010 salaries of the NEOs compared to their 2010 market median and market P75 are as follows:

Name	2010 Base Salary	2010 Median	2010 Market P75
Noel Walpole, President & CEO (retired December 31, 2010)	\$650,000	\$518,900	\$753,200
Katherine Mabe, <sup>(1)</sup> President & CEO	\$63,230	\$518,900	\$753,200
Sandeep Uppal, SVP and Chief Financial Officer	\$423,330	\$301,950	\$353,825
Jorge Arruda, SVP, Operations	\$299,200	Insufficient data available	Insufficient data available.
Linda Goss, SVP and Chief Actuary	\$273,980	\$220,800	\$245,000
Dean Bulloch, VP Human Resources	\$237,930	\$213,475	\$241,400

Notes:

(1) Mr. Walpole retired effective December 31, 2010. Ms. Mabe commenced employment on November 15, 2010. Her base salary in 2010 was based on \$600,000 per annum.

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## 2. **Short Term Incentive Plan (“STIP”)**

- **Goal:** To provide incentive compensation based on the achievement of various key performance measurements and personal goals designed to incent achievement of the Company’s strategic goals and reward employees who help the Company achieve its business goals, and attract and retain the talent necessary for the Company’s success.

<b>Compensation Element</b>	<b>Type</b>	<b>Audience</b>	<b>Performance</b>	<b>Payouts Based On</b>	<b>Market Positioning</b>
Short Term Incentive Plan (STIP)	Cash	All Executives	1 year	Achievement of Company’s strategic financial and non-financial objectives, and individual goals.	Target = median

- All regular-status employees, including Executives and Senior Executives, participate in the annual, cash-based STIP. Awards are earned on the achievement of the Company’s strategic financial objectives, as well as (for managerial employees and above) for the personal performance of individual participants.
- For managerial employees and above, at the beginning of each year, a target incentive opportunity is communicated to each participant, based on the job held, the internal value of the position, as well as alignment to the market median of the relevant market. This target incentive opportunity is expressed as a percentage of the participant’s salary, and reflects the bonus practice of other Canadian P&C companies within the P&C comparative group participating in the Towers Watson survey, as well as the broader financial services sector. The target incentive is based on several components, or objectives, and is paid at target for each specific target component, each with its own weight, if met. The target performance criteria are based on a composite of some or all of the following, depending on the particular position: combined operating ratio, direct premiums written growth, return on equity (1-year and 3-year) (the “Financial Performance Measures”), and execution of personal performance goals.
- Non-managerial employees (other than IT employees) participate in a plan designed to pay out between zero to 10% of base salary on a sliding scale, based on achievement of corporate, regional or subsidiary combined operating ratio. Non-managerial IT employees participate in a distinct STIP designated to pay out between zero to 10% of base salary on a sliding scale, based on achievement of Information Technology Services (“ITS”) projects within defined targets for scope, schedule and budget.
- For each component, minimum and maximum levels are also set, allowing a sliding scale to be used from zero at minimum to 150% of the target amount at maximum level.
- For 2010 individual performance objectives represent at target, 30% of the weight of the overall target incentive for Senior Executives and Executives, and 20% of the weight of overall target incentive for managerial positions below Senior Executives and Executives.

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- For 2010 the Company's Vice President Investments has a distinct STIP with a target of 25% and a maximum of 50% of base salary for meeting investment benchmark performance and no individual component. The investment performance component of the plan constitutes 100% of the incentive bonus.
- The Company's Senior Vice President and Chief Information Officer and Vice President, Information Technology Operations have a distinct STIP whereby in 2010 the ITS project performance component constitutes 52.5% of the incentive bonus, corporate performance component of the incentive bonus 17.5%, and individual performance goals 30% of the incentive bonus.
- For Senior Executives and Executives who participate in the Company's Long Term Incentive Plan ("LTIP"), in the event that in any year the aggregate of cash awards incentive awards under the Company's short term incentive plan ("STIP Awards") and the ("Cash Awards") under the LTIP (as described hereafter) exceed 7% of EBIT for such year (the "Incentive Award Limit"), the Cash Awards under the LTIP shall be reduced, pro rata, until the aggregate of the STIP Awards and the Cash Awards are equal to the Incentive Award Limit. If the STIP Awards are also in excess of the Incentive Award Limit, the STIP Awards for those Executives are also reduced until the STIP Awards are equal to the Incentive Award Limit.
- No incentive bonus under the STIP Plans is paid in any year when the Company on a consolidated basis does not have a profit, except for the component relating to the achievement of personal performance goals.

The 2010 STIP payout targets as a percentage of base salary for NEOs are as follows:

Name	STIP Minimum	STIP Target	STIP Maximum
Noel Walpole, President & CEO (retired December 31, 2010)	0%	50%	75%
Katherine Mabe, <sup>(1)</sup> President	N/A	N/A	N/A
Sandeep Uppal, SVP and Chief Financial Officer	0%	40%	60%
Jorge Arruda, SVP, Operations	0%	40%	60%
Linda Goss, SVP and Chief Actuary	0%	35%	52.5%
Dean Bulloch, VP Human Resources	0%	30%	45%

Notes:

(1) Katherine Mabe's eligibility to participate in the STIP commences with fiscal year 2011.

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The following table sets forth the 2010 financial performance measures that are applied under the STIP to determine the amount of the corporate component of the award to Senior Executives and Executives. These objectives represent at target, 70% of the weight of the overall target incentive except in the case of the Vice President, Investments, the Senior Vice President and Chief Information Officer, and the Vice President, Information Technology Operations as described in the note above.

<b>Financial Metrics</b>	<b>Weight</b>
ROE – Three Year	15%
ROE – One Year	35%
Increase in Premiums Written	10%
Combined Operating Ratio	10%

Individual performance objectives in 2010 comprised 30% of the weight of the overall target incentive. These objectives are set by the Board for the CEO, by the CEO for the Senior Executives, and by Senior Executives for Executives. They typically are comprised of both business objectives and personal development goals. Assessment of goal achievement is conducted according to the following criteria:

<b>Criteria</b>	<b>% of Bonus for Individual Performance Objectives</b>
Leader, overall, does not meet expectations.	0%
Leader meets expectations for most job accountabilities, goals and objectives. Some may be below expectations. Leader demonstrates some of the leadership competencies some of the time.	1% - 30%
Leader meets expectations for most job accountabilities, goals and objectives. Some may exceed expectations. Leader demonstrates most of the leadership competencies most of the time.	31% - 70%
Leader exceeds expectations for most job accountabilities, goals and objectives. Some may meet expectations. Leader demonstrates all of the leadership competencies all of the time.	71% - 100%

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The following table presents the payout for each NEO based on 2010 results and will be paid in the second quarter of 2011:

Name	2010 STIP Targets	2010 STIP Financial Results (amount out of 70%)	2010 STIP Individual Results (amount out of 30%)	2010 STIP Total Results (amount out of 100%)	2010 Total STIP
Noel Walpole, President & CEO (retired December 31, 2010)	\$325,000	52.65%	10.00%	62.65%	\$203,620
Katherine Mabe, President & CEO	N/A	N/A	N/A	N/A	N/A
Sandeep Uppal, SVP and Chief Financial Officer	\$169,332	Not eligible	Not eligible	Not eligible	Not eligible
Jorge Arruda, SVP, Operations	\$119,680	52.65%	30.00%	82.65%	\$98,918
Linda Goss, SVP and Chief Actuary	\$95,893	52.65%	30.00%	82.65%	\$79,258
Dean Bulloch, VP Human Resources	\$71,379	52.65%	34.50%	87.15%	\$62,208

**3. Long Term Incentive Plan-Economical Mutual Insurance Company Value Creation Plan**

- Goal: To provide incentive compensation, based on appreciation in value of the Company (on a consolidated basis), to Senior Executives and Executives, thereby providing additional incentive for their efforts in promoting the continued growth and success of the business of the Company, as well as aiding the Company in attracting and retaining executive management personnel. As a mutual company, share based incentives such as stock options or restricted stock units have not formed part of the Company's executive compensation strategy.

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Compensation Element	Type	Audience	Performance	Payouts Based On	Market Positioning
Long Term Incentive Plan (LTIP)	Value Creation Plan	Senior Executives and Executives	3 years	Growth in value of the Company on a consolidated basis above after tax risk-free rate of return allocated amongst participants	Target = median

- **Administration:** Under the LTIP, participants (“Participants”) are rewarded for long-term success. The LTIP is a cash award based on a value creation plan (“Value Creation Plan”), supported by appreciation in value of the Company as measured by the growth in value between the commencement of a three-year performance period and the end of the performance period (the “Performance Period”). Participants are entitled to a share in the growth in value in excess of the after tax risk free investment rate of return (“RFIRR”), which means the after tax RFIRR using the tax rate applicable to the interest income for the Company.
- Annually, at the commencement of each Performance Period, the Committee is required to determine a percentage value (the “Percentage”) which will be used to establish the size of a pool of funds (the “Sharing Pool”) at the end of the Performance Period; determine the current value of the Company on a consolidated basis (the “Opening Company Value”) based on the audited consolidated financial statements for the fiscal year then ended using the following formula: book value of the Company on a consolidated basis as at December 31 of the fiscal year then ended plus  $(4 \times \text{the average of consolidated earnings before interest expense and taxes determined in accordance with generally accepted accounting principles (“EBIT”) over the last three years (the “Formula”)}))$ ; and establish the RFIRR for the Performance Period.
- At the end of the Performance Period, the Committee is required to determine the current value of the Company on a consolidated basis (the “Closing Company Value”) based on the audited consolidated financial statements for the fiscal year then ended using the Formula; determine the growth in value of the Company (the “Growth in Value”) which shall be an amount equal to the Closing Company Value minus Opening Company Value; determine the amount of growth the Company would have had with the RFIRR as determined by the Committee at the commencement of the Performance Period as follows:  $(\text{Opening Company Value} \times (1 + \text{After-tax RFIRR}))^3 - \text{Opening Company Value}$  (the “Threshold Growth in Value”); determine the size of the Sharing Pool which shall be an amount equal to:  $\text{Percentage} \times (\text{Growth in Value} - \text{Threshold Growth in Value})^7$ ; allocate the Sharing Pool amongst the Participants by allocating units to the Participant based on the Participant’s Executive position, with each Participant being granted a percentage of the Sharing Pool (the “Participant’s Share”); determine the amount to be paid (the “Cash Award”) to each Participant which

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<sup>7</sup> Should the amount be negative, the Sharing Pool will have no value.

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shall be an amount equal to the Participant's Share X the Sharing Pool (subject to the Incentive Award Limit referred to below).

- The number of units allocated to each Participant is determined by multiplying salary by a target allocation, which for any employee who has not been in the Executive position for the full three (3) years, is prorated for the percentage of months of service in the three year period.
- In the event that in any year the aggregate of STIP Awards under the Company's STIP and the Cash Awards under this LTIP exceed 7% of EBIT for such year Incentive Award Limit, the Cash Awards under this LTIP are reduced, *pro rata*, until the aggregate of the STIP Awards and the Cash Awards are equal to the Incentive Award Limit.
- No incentive awards are paid in any year where the Company on a consolidated basis does not have a profit.
- The Committee at the commencement of the Performance Period will estimate what the size of the Sharing Pool would be at the end of the Performance Period if 3-year business plan targets were achieved;
- The Sharing Pool is allocated amongst the Participants based on their executive position. The actual incentive bonus paid to a Participant will depend on the number of Participants who qualify for payment in the year the incentive is paid.
- For the Performance Period ending December 31, 2010, growth in value above the Threshold Growth in Value resulted in a Sharing Pool, however, the Incentive Award Limit reduced the Sharing Pool to 0. For the Performance Period ending December 31, 2010 there were 15 Participants eligible to participate and the NEOs would have been entitled to share in the Sharing Pool if it had not been reduced to 0 by the Incentive Award Limit as follows:

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<b>Name</b>	<b>% of Sharing Pool</b>
Noel Walpole, President & CEO (retired December 31, 2010)	25.75%
Katherine Mabe, <sup>(1)</sup> President	N/A
Sandeep Uppal, SVP and Chief Financial Officer	Nil (Not eligible)
Jorge Arruda, SVP, Operations	9.78%
Linda Goss, SVP and Chief Actuary	6.78%
Dean Bulloch, VP Human Resources	5.89%

Notes:

(1) Katherine Mabe's eligibility to participate in the LTIP commences with fiscal year 2011.

Ms. Mabe's initial target incentive under the LTIP will be 40% of \$600,000 or \$240,000 (subject to the Incentive Award Limit). This allocation vests over a three-year period, with the target incentive compensation commencing at \$80,000 for 2011 (payable in 2012).

As additional incentive to Ms. Mabe, the Company will provide a top-up bonus (outside of the LTIP) in any year that an incentive payment is made under the LTIP to her in an amount equal to the incentive paid (in effect doubling the incentive payment) up to the maximum aggregate incentive payment under the LTIP and this top-up bonus, of 120% of base salary. (The top-up bonus will not be included in calculating the Incentive Award Limit for the purposes of the LTIP.)

No payouts have been awarded under this plan, which was introduced January 1, 2008.

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## LTIP Transitional Period

The LTIP had a transitional period during the first three years of the LTIP to allow for an orderly transition from the former long term incentive plan to the Value Creation Plan by fixing the Opening Company Value Plan as follows:

Performance Period	Opening Company Value	Basis of Closing Company Value	Closing Company Value
January 1, 2006 to December 31, 2008	\$1,750,000,000	December 31, 2008 as follows: Book Value of the Company on a consolidated basis as at December 31, 2008 plus (4 X average EBIT for 2006, 2007 and 2008).	\$1,558,081,000
January 1, 2007 to December 31, 2009 <sup>(1)(2)</sup>	\$1,260,000,000	December 31, 2009 as follows: Book Value of the Company on a consolidated basis as at December 31, 2009 plus (4 X average EBIT of 2007, 2008 and 2009).	\$1,407,375,000
January 1, 2008 to December 31, 2010 <sup>(1)(2)</sup>	\$1,126,000,000	December 31, 2010 as follows: Book Value of the Company on a consolidated basis as at December 31, 2010 plus (4 X average EBIT of 2008, 2009 and 2010).	\$1,209,193,000

Notes:

- (1) Closing Company Value Adjustment - The Closing Company Value for the Performance Periods ending December 31, 2009 and December 31, 2010 are subject to the following adjustment: In fixing the Opening Company Value for these Performance Periods, the Committee took into account the unprecedented stock market collapse of 2008. In determining the Closing Company Value the Committee also took into account any correction to those securities within the investment portfolio and any other matters as it feels would be prudent and may adjust the Closing Company Value accordingly.
- (2) Although the Growth in Value of the Company above the Threshold Growth in value for the Performance Periods ending December 31, 2009 and December 31, 2010 created a Sharing Pool, the Incentive Award Limit reduced the Sharing Pool to 0.

## 4. **Pension & Benefits:**

- **Goal:** To provide each participant with competitive benefits and retirement income, in order to retain the Company's Executives and Senior Executives.
- **Administration:** In 2003, Economical closed the Defined Benefit Pension Plan ("DBPP") to new entrants and introduced a Defined Contribution Pension Plan ("DCPP"). All employees including Executives and Senior Executives were given the opportunity to choose one of three pension options as Economical introduced the new DCP. They could: 1) stay with the DBPP; 2) convert their DB balance and move it to the new DCP; or 3) retain their history in the DBPP and join the DCP for future contributions. As a result, Economical has various pension scenarios that apply to the supplementary plans as well.

### Defined Benefit Supplementary Pension Plan

- For Executive and Senior Executive members of the DBPP Economical maintains The Economical Insurance Group Supplementary Pension Plan ("SPP"). The purpose of the SPP is to provide designated members of the DBPP with supplementary pension income

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in order to compensate for the maximum pension limitations applicable to the pension benefits payable under the DBPP, as prescribed under the *Income Tax Act* (Canada), subject to minimum vesting requirements. The pension benefit under the DBPP is determined at retirement using a formula combining final average earnings and service. Final average earnings means the average of the employee's best five years of earnings while a member of the plan. The SPP serves as a retention tool for Executives and Senior Executives and vests when the Executive and Senior Executive have completed two (2) years of continuous service with the Company. The Company has established a "retirement compensation arrangement", as defined in the *Income Tax Act* (Canada) as a trusteed vehicle to provide for the prefunding of all or a portion of the benefits described herein. Such fund and trust may be collapsed or revoked at any time by the Company as it determines in its absolute discretion. For all participants, pensionable earnings comprise base salary; for Senior Executives, pensionable earnings also include STIP payments up to the target.

### **Defined Contribution Supplementary Pension Plan**

- For Executive and Senior Executive members of the DCPPE, Economical provides a "Notional Account" to offer tax-sheltered opportunities for executive pension benefits that exceed defined contribution pension limits for maximum annual contributions. To maximize the tax-effectiveness of our pension plan, any excess Company contributions are automatically credited to a Notional Account. New credits to the Notional Account are tracked and recorded, and the balance earns an investment return. Similar to an RRSP, the balance in a Notional Account accumulates tax-free. When the executive leaves the Company, retires or dies, the full value of their Notional Account is paid out and is fully taxable at that time. The DCPPE for executives includes the company core contribution (4.5% of base pay) as well as the executive supplementary contributions (increased from 3.0% to 3.5% of base pay effective January 24, 2011). The contributions are split between the SPP and the Notional Account.

### **Benefits**

- In terms of company benefits, Executives and Senior Executives have certain upgrades to the flexible benefit plan provided to employees. These upgrades include: higher additional flex dollars; enhanced orthodontic coverage, life insurance; and long-term disability.

## **5. *Perquisites***

- Goal: to provide Executives and Senior Executives with a group of perquisites commensurate with perquisites provided to Executives and Senior Executives within the group of participants in the Towers Watson survey and the broader financial services sector, which include the lease of a company car, personal fitness training reimbursement, annual executive medical, education assistance, and financial counselling.

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### ***Compensation Consultant Independent Advice***

The Committee receives assessments and recommendations from Management when reviewing and considering compensation for Executives and Senior Executives. The Committee works with Management and its compensation team to review employment and compensation practices in the Canadian market in order to ensure that the Company's employees and Management are competitively compensated. The Committee may also consult directly with independent experts to fulfill its mandate.

In 2009, the Committee undertook a request for proposal from compensation consultants and as a result retained the services of Mercer LLC to act as its independent compensation consultant. Mercer's role mainly consists of reviewing and validating Management's recommendations and advising the Committee on market trends, program structures and designs. The market analysis includes comparisons with peer group companies, which are included in the annual "Executive Compensation Review and Analysis" presented to the Committee in order to make the best informed pay decisions. However, the Committee does not solely rely on market data surveys to determine compensation levels. Individual performance and internal equity are also taken into account. In 2010, fees paid to Mercer for market analysis and other compensation advice totalled \$13,102.

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## 8. SUMMARY COMPENSATION TABLE

Compensation for the three most recently completed financial years is summarized in the *Summary Compensation Table* below for the following individuals:

- The President & CEO — Noel Walpole (retired December 31, 2010)
- The President & CEO – Katherine Mabe
- The Senior Vice-President and Chief Financial Officer – Sandeep Uppal
- The next three (3) most highly compensated executive officers (total compensation) — Jorge Arruda, Linda Goss and Dean Bulloch who, together with the Presidents & CEOs and Chief Financial Officer, make up the “Named Executive Officers” or the “NEOs”.

The annual compensation presented excludes perquisites and other personal benefits because these benefits in the aggregate did not exceed \$50,000 or 10% of the total annual salary and bonus for any of the named executive officers.

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## Summary Compensation Table

Name	Year	Salary (\$)	Annual Incentive Plans <sup>(1)</sup> (\$)	Long Term Incentive Plans <sup>(2)</sup> (\$)	Pension Value <sup>(3)</sup> (\$)	All Other Compensation <sup>(4)</sup> (\$)	Total Compensation (\$)
Noel Walpole, President & CEO (retired December 31, 2010)	2010	650,000	203,620	0	203,200	36,615	1,093,435
	2009	630,000	80,253	0	195,600	51,631	957,484
	2008	630,000	64,575	0	580,600	25,546	1,300,721
Katherine Mabe, President & CEO	2010	63,230	N/A	N/A	11,900	13,208	88,338
	2009	N/A	N/A	N/A	N/A	N/A	N/A
	2008	N/A	N/A	N/A	N/A	N/A	N/A
Sandeep Uppal, SVP and Chief Financial Officer	2010	423,330	0	0	36,567	36,109	496,006
	2009	411,000	66,123	0	35,957	37,438	550,518
	2008	411,000	68,432	0	40,973	35,087	555,492
Jorge Arruda, SVP, Operations	2010	299,200	98,918	0	23,755	38,753	453,207
	2009	272,000	21,720	0	21,910	38,723	354,353
	2008	272,000	20,128	0	27,147	38,853	358,128
Linda Goss, SVP & Chief Actuary	2010	273,980	79,258	0	21,892	35,257	399,064
	2009	266,000	19,136	0	21,746	30,893	337,775
	2008	266,000	23,940	0	25,247	28,514	343,701
Dean Bulloch, VP, Human Resources	2010	237,930	62,208	0	20,025	44,155	364,318
	2009	231,000	30,131	0	19,664	46,692	327,487
	2008	231,000	30,185	0	21,910	38,967	322,062

### Notes:

- (1) Annual incentive plans are comprised of the STIP. The amounts disclosed in this Summary Compensation Table for 2008, 2009 and 2010 are the annual bonuses earned in each respective year. Such amounts were paid out in the first quarter of the following year.
- (2) Long term incentive plans are comprised of the Value Creation Plan. The amounts disclosed in this Summary Compensation Table for 2008, 2009 and 2010 are the long term bonuses earned pursuant to the LTIP in each respective year. As indicated, Economical's Value Creation Plan has not paid out since its inception January 1, 2008.
- (3) The pension value disclosed for each NEO is the compensatory value of registered and non-registered defined benefit or defined contribution plans. The compensatory value includes the service cost, net of employee contributions, if any, plus differences between actual and estimated earnings, and any additional changes that have a retroactive impact.
- (4) All "other compensation" could include items such as: the value of perquisites and post-retirement benefits such as life and health insurance.

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## **9. PENSION PLAN BENEFITS**

### **NARRATIVE DISCUSSION FOR ECONOMICAL DBPP, SPP, DCPD AND NOTIONAL ACCOUNT PLANS**

In 2003 Economical closed the DBPP to new entrants<sup>8</sup> and introduced a DCPD.

#### ***Defined Benefit Registered Pension Plan***

- The DBPP provides a specific retirement income based on a formula that takes into account an employee's age, years of participation and pensionable earnings. An employee's retirement income is defined in advance. Members of the plan are required to contribute 5% of earnings.
- The annual pension payable at the employee's normal retirement date is equal to the following: 2% of Final Average Earnings less 1/35th of such employee's Canada Pension Plan/Quebec Pension Plan benefit for each year of Credited Service. Final Average Earnings means the average of the member's best 5 years of earnings while a member of the plan.
- Credited Service is calculated using complete months of contributory membership in the plan.
- If a member remains employed until age 55 and retires prior to age 62, the reduction will be equal to .5% for each month that retirement precedes age 62. If a member retires between age 62 and 65, there will be no reduction.
- If single at retirement, pension will continue to be paid each month for as long as alive. If the member dies before receiving 120 monthly payments, the pension will continue to be paid to the beneficiary until 120 pension payments have been made in total, or the value of the remaining payments will be paid in a lump sum.
- If with a spouse at retirement, pension will begin on the first day of the month following retirement date and will continue to be paid each month for as long as alive. When the member dies, the pension will reduce to 60% and will be paid to the spouse for the spouse's lifetime. If the spouse does not survive the member, the pension will stop.

#### ***Defined Benefit Supplementary Pension Plan***

- For Executive and Senior Executive members of the DBPP, Economical maintains the SPP. The purpose of the SPP is to provide designated members of the DBPP with supplementary pension income in order to compensate for the maximum pension limitations applicable to the pension benefits payable under the DBPP, as prescribed under the *Income Tax Act* (Canada), subject to minimum vesting requirements. The SPP serves as a retention tool for Executives and Senior Executives and vests when the Executive and Senior Executive have completed two (2) years of continuous service with

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<sup>8</sup> Other than Ms. Mabe who was added thereto as part of the terms of her employment.

the Company. The Company has established a “retirement compensation arrangement” as defined in the *Income Tax Act* (Canada) as a trustee vehicle to provide for the prefunding of all or a portion of the benefits described herein. Such fund and trust may be collapsed or revoked at any time by the Company as it determines in its absolute discretion. For all participants, pensionable earnings comprise base salary; for Senior Executives, pensionable earnings also include STIP payments up to the target.

#### ***Defined Contribution Registered Pension Plan***

- Economical makes a basic contribution of 4.5% of an employee’s base salary to the DCPP. Economical make additional matching contributions up to a maximum of 3.5% to the DCPP (for employees with 3 years of service and 3.0% for employees with less than 3 years of service) when an employee elects to make optional payroll contributions to the Savings Plan. There is no company match on employee lump sum contributions to the Savings Plan.
- All contributions from Economical are directed to the DCPP. This plan is governed by pension legislation and an employee cannot withdraw cash from the DCPP until the employee retires.

#### ***Defined Contribution Supplementary Pension Plan***

For Executive and Senior Executive members of the DCPP, Economical provides a “Notional Account” to offer tax-sheltered opportunities for executive pension benefits that exceed defined contribution pension limits for maximum annual contributions. To maximize the tax-effectiveness of this pension plan, any excess Company contributions are automatically credited to a Notional Account. New credits to the Notional Account are tracked and recorded, and the balance earns an investment return. Similar to an RRSP, the balance in a Notional Account accumulates tax-free. When the executive leaves the Company, retires or dies, the full value of his or her Notional Account is paid out and is fully taxable at that time. The DCPP for executives includes the company core contribution (4.5% of base pay) as well as the executive supplementary contributions (increased from 3.0% to 3.5% of base pay effective January 24, 2011). The contributions are split between the RPP and the Notional Account.

The following tables provide information on pension plans as at 2010 in which the NEOs participate.

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**For questions or assistance, please call Georgeson at 1-866-909-6468.**

## Defined Benefit Pension Plan Table

Name	Number of Years Credited Service (#) <sup>(1)</sup>	Annual Benefits Payable		Accrued Obligation at Start of Year (\$) <sup>(3)</sup>	Compensatory Change (\$) <sup>(4)</sup>	Non-Compensatory Change (\$) <sup>(5)</sup>	Accrued Obligation at Year End (\$) <sup>(6)</sup>
		At Year End (\$)	At Age 65 (\$) <sup>(2)</sup>				
Noel Walpole, President & CEO (retired December 31, 2010)	24.00	374,300	374,300	4,595,900	230,200	444,400	5,243,500
Katherine Mabe, President & CEO	0.13	1,500	260,100	0	11,900	1,300	13,200

### Notes:

- (1) For Mr. Walpole, the number of years of credited service under the SERP are 24 (includes 7.42 years transferred from former employer.)
- (2) The information shown in this column was determined based on the final average earnings of each participant as at December 31, 2010 and years of credited service projected up to age 65 (assuming full-time employment).
- (3) The information shown in this column was determined by using the same assumptions and methods used for 2009 financial statement reporting purposes. In particular, the discount rate used, for each individual, is 6.50% per year.
- (4) Includes service cost, net of employee contributions, if any, plus differences between actual and estimated earnings, and any additional changes that have a retroactive impact.
- (5) Includes all items that are not compensatory, such as changes in actuarial assumptions and interest cost.
- (6) The information shown in this column was determined by using the same assumptions and methods used for 2009 financial statement reporting purposes. In particular, the discount rate used, for each individual, is 5.50% per year.

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## Defined Contribution Pension Plan Table

Name	Number of Years Credited Service (#) <sup>(1)</sup>	Accrued Obligation at Start of Year (\$) <sup>(2)</sup>	Compensatory Change (\$) <sup>(3)</sup>	Non-Compensatory Change (\$) <sup>(4)</sup>	Accrued Obligation at Year End (\$) <sup>(5)</sup>
Sandeep Uppal, SVP and Chief Financial Officer	10.17	238,548	36,567	7,183	282,298
Jorge Arruda, SVP, Operations	14.67	232,688	23,755	23,871	280,314
Linda Goss, SVP and Chief Actuary	9.42	169,730	21,892	19,683	211,305
Dean Bulloch, VP Human Resources	14.33	177,383	20,025	19,671	217,079

Notes:

- (1) Is the regular status tenure of the individual.
- (2) Includes the value of the DBPP plus the value of the Notional Account at January 1, 2010.
- (3) Includes the employer contributions to the DCPD and Notional Account made during 2010.
- (4) Includes investment gains and losses on the DCPD, and is net of fees on the DCPD, and also includes the interest on the Notional Account (the average rate on 10 year Government of Canada marketable bonds) through the year 2010.
- (5) Includes the value of the DBPP plus the value of the Notional Account at December 31, 2010.

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## 10. TERMINATION AND CHANGE OF CONTROL

### *Termination and Change of Control Provisions*

Other than as described herein, no NEO is a party to an agreement with the Company that contains change of control provisions. Hiring documents for such NEOs include confirmation of total rewards, as well as a requirement for each Executive to sign the Company's Code of Business Conduct.

The employment agreement (the "Employment Agreement") made between Katherine Mabe and the Company provides for the following payments and benefits following her termination by the Company, other than for cause, death or disability:

- A lump sum payment equal to 18 months of Ms. Mabe's then current base salary and target short-term incentive compensation, less appropriate deductions;
- Continuation of benefit and pension coverage subject to the terms and conditions of the applicable plan/policy and to the extent permitted by the carrier, for a period of eighteen (18) consecutive months;
- With respect to the STIP, Ms. Mabe will be deemed actively employed until the required eligibility date for any plan year that falls within the 18-month severance period, but the amount payable will be prorated to the number of months of severance payment attributable to that plan year; and
- With respect to the LTIP, the Company will, only for the fiscal year in which Ms. Mabe's employment is terminated, pay to her a portion of any LTIP that would be otherwise payable. That is, notwithstanding the express terms of the LTIP, for the purposes of the LTIP, Ms. Mabe will be deemed actively employed until the required eligibility date but the amount payable will be pro-rated to the number of months within the applicable fiscal year up to the date that she receives notice of her termination of employment.

The Employment Agreement provides for the following payments and benefits following a hostile or friendly change of control of the Company:

#### *Hostile Transfer of Control*

- If Ms. Mabe provides notice to the Company of her resignation within 30 days following a Hostile Transfer of Control (as defined in the Employment Agreement), such resignation shall be treated as a termination of employment in the same manner as a termination by the Company, other than for cause, death or disability; and
- If, within 18 months following a Hostile Transfer of Control, there is a significant change in Ms. Mabe's status, position or responsibilities or a reduction in her salary or a material change detrimentally affecting her remuneration, she may, provided 30 days notice following such event is given to the Company, elect to terminate her employment, which such termination shall be treated in the same

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manner as a termination by the Company, other than for cause, death or disability.

#### *Friendly Transfer of Control*

- If, within 18 months following a Friendly Transfer of Control (as defined in the Employment Agreement), there is a significant change in Ms. Mabe's status, position or responsibilities or a reduction in her salary or a material change detrimentally affecting her remuneration, she may, provided 30 days notice following such event is given to the Company, elect to terminate her employment, and such termination shall be treated in the same manner as a termination by the Company, other than for cause, death or disability.

Ms. Mabe has no duty to mitigate any amounts paid under the Employment Agreement and the Company has no right of set-off against Ms. Mabe.

The Company has also entered into agreements ("Change of Control Agreements") with other NEOs and Senior Executives and Executives which provide for the following payments and benefits following a hostile or friendly change of control of the Company:

- In the event of an Involuntary Termination (as defined in the Change of Control Agreements) on the Effective Date (as defined in the Change of Control Agreements) or within 18 months following a Change of Control (as defined in the Change of Control Agreement), the Company shall pay to the Executive an amount equal to the sum of:
  - (i) 18 months for Senior Vice Presidents and 12 months plus one (1) month per year of service up to 18 months for Vice Presidents, of the Executive's Regular Monthly Compensation (as defined in the Change of Control Agreements);
  - (ii) a pro-rata share of the Executive's current year's STIP based on Target Incentive Award pro rated for the number of complete months in the fiscal year in which the Involuntary Termination occurs up to the Termination Date (as defined in the Change of Control Agreements); and
  - (iii) 15% of the amount set out in paragraph (i) above in lieu of contributions by the Company in respect of the Pension Plan (as defined in the Change of Control Agreements) and long term disability coverage, all of which cease on the Termination Date.
- The Executive may elect to either:
  - (i) maintain the Executive's regular employee benefits until the earliest of:
    - (a) the end of the Termination Period (as defined in the Change of Control Agreements);
    - (b) the date the Executive is employed by another employer on a regular fulltime basis and is eligible to participate in a group insurance plan with the new employer that is similar to the Company program;

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- (c) the date the Executive's retirement pension commences; or
  - (i) have the Company pay to the Executive a lump sum amount equal to the aggregate cost to the Company (without discount or present valuation) of the regular employee benefits for the Termination Period.
- The Company shall provide the Executive with professional outplacement services not to exceed the cost of \$10,000.

## **11. INDEBTEDNESS OF DIRECTORS AND EXECUTIVE OFFICERS**

There is no outstanding indebtedness to Economical or to its subsidiaries incurred by directors, executive officers, employees or former directors, executive officers or employees of the Company.

## **12. CORPORATE GOVERNANCE PRACTICE**

Economical considers corporate governance and sound market practices to be essential components of its operations.

Economical's Statement of Corporate Governance Practices is attached as Schedule "A" to this Circular.

## **13. PROPOSALS**

The *Insurance Companies Act* permits not less than 100 eligible Members of Economical to submit Member proposals to Economical for inclusion in a management proxy circular for an annual meeting of Members.

Please see the sections entitled "Background to the Meeting" and "Business of the Meeting" for a discussion of the Dissident Proposal. This is the only proposal of which Management is aware.

The Dissident Proposal is attached as Appendix "A" and Appendix "B" to the Notice of Meeting. The matter to be considered under the Dissident Proposal is the ouster of all of the existing directors. The Dissident Proposal also contemplates the replacement of the existing board entirely with Dissident nominees. However this matter will be dealt with under the normal election procedure once the Dissident Proposal has been voted on.

If these items are put forward at the Meeting, and unless otherwise specified, the proxyholders designated in the BLUE form of proxy intend to vote AGAINST the Dissident Proposal.

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**14. ADDITIONAL INFORMATION AND CONTACTING ECONOMICAL MUTUAL INSURANCE COMPANY**

Further information relating to Economical may be obtained from its web site at [www.economicalinsurance.com](http://www.economicalinsurance.com). Financial information is provided in Economical's comparative financial statements and management's discussion and analysis for the fiscal year ended December 31, 2010 and these documents are also accessible through Economical's website.

To obtain a copy of these documents together with Economical's annual report, when available, at no cost, please contact Economical at 519-570-8589.

**15. APPROVAL OF THE BOARD OF DIRECTORS**

The Board has approved the contents and the sending of this Management Proxy Circular to the Members of Economical.



Katherine A. Mabe  
Chief Executive Officer  
April 11, 2011

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***For questions or assistance, please call Georgeson at 1-866-909-6468.***

## **SCHEDULE “A”**

### **Governance Mandates of the Board of Directors and Committees**

#### **Statement of Corporate Governance Practices**

The Board of Directors (the “Board”) of Economical Mutual Insurance Company and each of its subsidiaries, The Missisquoi Insurance Company, Federation Insurance Company of Canada, Waterloo Insurance Company and Perth Insurance Company (individually each herein referred to as the “Company” and collectively as the “Companies”), believe that sound corporate governance policies and practices are essential to the well being of the Companies.

The corporate governance policies and practices are designed to strengthen the ability of the Board for each Company to supervise management, enhance long-term value and to ensure that each of the Companies operate to the highest standards of integrity. As part of these governance practices the Board for each of the Companies have adopted mandates for the Board and their committees, which set out their responsibilities.

#### **Ethical Business Conduct**

The Board has adopted a written code of business conduct (the “Code”) for the Companies’ directors, officers and employees that sets out the expectations of conduct of such persons in their dealings on behalf of the Companies. There are established reporting procedures for employees, directors and officers to raise concerns regarding matters addressed by the Code on a confidential basis free from discrimination, retaliation or harassment. Employees, officers and directors who violate the Code may face disciplinary action, including dismissal or removal from their post.

It is the responsibility of every director, officer and employee of the Companies to understand the Code. Any such person who becomes aware of a violation of the Code by anyone working for the Companies must report such knowledge to their immediate leader, manager, Senior Vice President, Chief HR Officer, the President & Chief Executive Officer and/or the Chair of the Board, depending on the circumstances.

#### **Ethics Reporting System**

In 2010, Economical partnered with ClearView Strategic Partners Incorporated, a third party vendor, to provide its employees, brokers and claims vendors with a confidential and anonymous means to communicate wrongdoing. The Ethics Reporting Program now includes the Code of Business Conduct and the Whistleblower Policy. This Policy applies to all employees of Economical and includes all of its wholly-owned subsidiaries. The Policy encourages employees to report incidents where identified concerns regarding Economical’s wrongdoing, accounting, internal controls or auditing matters. This Policy ensures that Economical continues to operate with a high degree of integrity and ethical accountability.

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## TABLE OF COMPLIANCE WITH SUGGESTED CORPORATE GOVERNANCE PRACTICES

NP 58-201 Provision	Summary of the Provision	Economical Compliance with Provision
3.1	The board should have a majority of independent directors	Complies
3.2	The chair should be an independent director or an independent director should be appointed to act as “lead director”. Such person should act as the effective leader of the board and ensure that the board’s agenda will enable it to successfully carry out its duties.	Complies
3.3	The independent directors should hold regularly scheduled meetings at which non-independent directors and members of management are not in attendance.	Complies
3.4	<p>The board should adopt a written mandate where it acknowledges responsibility for the stewardship of the Company, including responsibility for: (a) the integrity of executive officers and that such officers create a culture of integrity throughout the organization; (b) a strategic planning process and annual (or more frequent) adoption of plan that takes into account opportunities and risks of the business; (c) the identification and implementation of systems regarding principal risks; (d) succession planning; (e) a communication policy; (f) internal control and management information systems; and (g) corporate governance principles and guidelines.</p> <p>The written mandate of the board should also set out: (i) stakeholder feedback measures; and (ii) expectations and responsibilities of directors, including basic duties, attendance and advance review of meeting materials.</p>	Complies other than development of a communications policy and stakeholder feedback measures that are under development.
3.5	The board should develop clear position descriptions for the chair of the board, the chairs of each board committee and the CEO. The board should also develop or approve the corporate goals and objectives of the CEO.	Under development
3.6	The board should ensure that all new directors receive a comprehensive orientation, and that they understand the role of the board, its committees, the contribution individual directors are expected to make and the nature and operation of the Company’s business.	Complies
3.7	The board should provide continuing education opportunities for all directors.	Complies
3.8	The board should adopt a written code of business conduct and ethics, applicable to directors, officers and employees. The code should constitute written standards that are reasonably designed to promote integrity and to deter wrongdoing.	Complies

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NP 58-201 Provision	Summary of the Provision	Economical Compliance with Provision
	It should address: (a) conflicts of interest; (b) protection and proper use of corporate assets and opportunities; (c) confidentiality of information; (d) fair dealing with the customers, suppliers, competitors and employees; (e) legal and regulatory compliance; and (f) reporting of any illegal or unethical behaviour.	
3.9	The board should be responsible for monitoring compliance with the code. Any waivers from the code that are granted for the benefit of the Company's directors or executive officers should be granted by the board (or a board committee) only.	Complies
3.10	The board should appoint a nominating committee composed entirely of independent directors.	Complies (Nominating Committee = Corporate Governance Committee)
3.11	The nominating committee should have a written charter that clearly establishes the committee's purpose, responsibilities, member qualifications, member appointment and removal, structure and operations (including any authority to delegate to individual members and subcommittees), and manner of reporting to the board. In addition, the nominating committee should be given authority to engage and compensate any outside advisor that it determines to be necessary to permit it to carry out its duties.	Complies
3.12	<p>Prior to nominating or appointing directors, the board should: (a) consider what competencies and skills the board should possess; and (b) assess what competencies and skills each existing director possesses.</p> <p>The board should be considered as a group, with each individual making his or her own contribution.</p> <p>The board should also consider the size of the board, with a view to facilitating effective decision-making.</p> <p>In carrying out each of these functions, the board should consider the advice and input of the nominating committee.</p>	Complies
3.13	The nominating committee should be responsible for identifying and recommending new director nominees	Complies
3.14	In making its recommendations, the nominating committee should consider: (a) the competencies and skills necessary for the board to possess; (b) the competencies and skills that the board considers each existing director to possess; and (c) the competencies and skills each new nominee will bring to the	Complies

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NP 58-201 Provision	Summary of the Provision	Economical Compliance with Provision
	<p>boardroom.</p> <p>The nominating committee should also consider whether nominees can devote sufficient time and resources to his or her duties as a board member.</p>	
3.15	The board should appoint a compensation committee composed entirely of independent directors.	Complies
3.16	The compensation committee should have a written charter that establishes the committee's purpose, responsibilities, member qualifications, member appointment and removal, structure and operations (including any authority to delegate to individual members or subcommittees), and the manner of reporting to the board. In addition, the compensation committee should be given authority to engage and compensate any outside advisor that it determines to be necessary to permit it to carry out its duties.	Complies
3.17	The compensation committee should be responsible for: (a) reviewing, approving and evaluating corporate goals and the CEO's performance in respect of such goals in determining (or making recommendations regarding) compensation; (b) making recommendations to the board with respect to other officers and director compensation, incentive-compensation plans and equity-based plans; and (c) reviewing executive compensation disclosure before the Company publicly discloses this information.	Complies
3.18	The board, its committees and each individual director should be regularly assessed, considering (a) in the case of the board or a board committee, its mandate or charter, and (b) in the case of an individual director, the applicable position description(s), as well as the competencies and skills each individual director is expected to bring to the board.	Complies Assessments are completed bi-annually

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## **CAST YOUR VOTE NOW – HERE'S HOW**

The Board unanimously recommends that shareholders:

VOTE FOR Economical's slate of director nominees;

VOTE FOR the appointment of auditors; and

VOTE AGAINST the ouster of all of the current directors.

If, after reading the proxy materials you agree to support Economical's existing Board, it is crucial that you sign, date and return the enclosed BLUE proxy using any of the methods described on your form of proxy.

Please note that if you have mistakenly voted using the wrong proxy, or have changed your mind, you have every right to change your vote by simply signing, dating and mailing the enclosed BLUE Proxy. This action will cancel all previous votes as it is the later dated proxy received that will count at the Meeting.

### **1. What materials do I need to submit?**

You only need to submit your BLUE Proxy which accompanies this material. The BLUE proxy must be signed, dated and returned using any of the methods described on the form of proxy.

### **2. What is my deadline to vote?**

Your BLUE Proxy must be voted by any one of the methods described on the form no later than 1:00 p.m. (Toronto time) on May 16, 2011. It is particularly important that you return the executed BLUE Proxy

VOTING FOR Economical's slate of director nominees;

VOTING FOR the appointment of auditors; and

VOTING AGAINST the ouster of all of the current directors, as soon as possible to ensure your vote is counted).

DO NOT submit the sample form of proxy printed on white paper. ONLY submit the BLUE form of proxy.

### **3. Who do I call if I have any questions about the Economical proxy or if I need help voting?**

Any questions about the proxy materials you have received or how to complete your BLUE proxy in support of Economical's slate of director nominees can be addressed by calling Karen Gavan, Chair of the Special Committee of the Board of Directors of Economical at 519-570-8500 x 42997 or by calling Georgeson toll free at 1-866-909-6468.

**Please visit our website for regular updates at [www.economicalinsurance.com](http://www.economicalinsurance.com)**

***YOUR VOTE IS EXTREMELY IMPORTANT. VOTE ONLY THE BLUE PROXY.  
For questions or assistance, please call Georgeson at 1-866-909-6468.***

**Please direct all inquiries to:**

**Questions and Further Assistance**

If you have any questions about the information contained in this document or require assistance in completing your **BLUE** proxy form, please contact our proxy solicitation agent at:



North American Toll Free Number: 1-866-909-6468

Email: [askus@georgeson.com](mailto:askus@georgeson.com)

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