WESTAIM

Second Quarter Report to Shareholders
for the quarter ended June 30, 2014

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"Westaim" or the "Company" in this Management's Discussion and Analysis ("MD&A") refers to The Westaim Corporation on a consolidated basis. This MD&A, which has been approved by the Westaim Board of Directors, should be read in conjunction with Westaim's unaudited consolidated financial statements including notes for the three and six months ended June 30, 2014 and 2013 as set out on pages 16 to 27 of this quarterly report. Financial data in this MD&A has been derived from the unaudited consolidated financial statements for the three and six months ended June 30, 2014 and 2013 and is intended to enable the reader to assess Westaim's results of operations for the three and six months ended June 30, 2014 and financial condition as at June 30, 2014. The Company reports its consolidated financial statements using accounting policies consistent with International Financial Reporting Standards ("IFRS"). All amounts are in Canadian dollars unless otherwise indicated. The following commentary is current as of August 14, 2014. Additional information relating to Westaim is available on SEDAR at www.sedar.com. Certain totals, subtotals and percentages may not reconcile due to rounding.

Non-GAAP measures
Westaim uses both IFRS and non-generally accepted accounting principles ("non-GAAP") measures to assess performance. The Company cautions readers about non-GAAP measures that do not have a standardized meaning under IFRS and are unlikely to be comparable to similar measures used by other companies. Management believes these measures allow for a more complete understanding of the underlying business. These measures are used to monitor Westaim's results and should not be viewed as a substitute for those determined in accordance with IFRS. Reconciliations of such measures to the most comparable IFRS figures are included herein. Book value per share represents shareholders' equity at the end of the period, determined on an IFRS basis, divided by the total number of common shares outstanding on the same date. The Company believes that this is a useful measurement as the relative increase or decrease from period to period in book value per share should approximate over the long term the relative increase or decrease in the intrinsic value of the business, but is not necessarily equivalent to the net realizable value of the Company's assets per share. Adjusted book value per share represents shareholders' equity at the end of the period, determined on an IFRS basis and adjusted to include or exclude one or more items required by IFRS but which are either unusual or non-recurring, divided by the total number of common shares outstanding on the same date.

Future Oriented Financial Information
This MD&A may contain forward-looking statements that involve risks and uncertainties. The Company's actual results could differ materially from these forward-looking statements as a result of various factors, including those discussed hereinafter. Please refer to the cautionary note in Section 12 of this MD&A.

1. THE COMPANY

Westaim is a publicly traded Canadian-based investment company that invests directly and indirectly through acquisitions, joint ventures and other arrangements, with the objective of providing its shareholders with capital appreciation and real wealth preservation. Westaim's strategy is to pursue investment opportunities to grow shareholder value (as measured by book value per share) over the long term.

On July 31, 2014, the Company, in combination with third party investors, completed the acquisition of a significant interest in Houston International Insurance Group, Ltd. ("HIIG") through Westaim HIIG Limited Partnership (the "Partnership"), an Ontario limited partnership managed by a subsidiary of the Company. HIIG is a U.S. based diversified specialty insurance provider and managing general insurance agent covering risks across the United States and certain niche global markets. See discussion in Section 3, *Investment in HIIG* and Section 4, *Equity Financings* of this MD&A for additional information on the acquisition and related financing transactions.

On October 1, 2013, the Company completed a 50:1 share consolidation of all of its outstanding common shares. All share capital, per share amounts, and share-based awards in the current and comparative periods have been adjusted to reflect this change.

2. OVERVIEW OF PERFORMANCE

Highlights	Three months ended June 30		Six months ended June 30	
(millions except share and per share data)	2014	2013 (1)	2014	2013 (1)
Revenue	$ 0.0	$ 0.1	$ 0.1	$ 0.2
Expenses excluding share-based compensation	(2.9)	(0.8)	(4.5)	(1.5)
Share-based compensation	0.0	-	(0.1)	-
Income tax recovery	-	0.0	-	0.1
Profit or loss and other comprehensive income	$ (2.9)	$ (0.7)	$ (4.5)	$ (1.2)
Earnings per share				
Profit or loss and other comprehensive income – basic and diluted	$ (0.21)	$ (0.05)	$ (0.33)	$ (0.09)
Number of common shares outstanding - at June 30	13,902,937	13,902,937	13,902,937	13,902,937
Book value per share - at June 30	$ 1.62	$ 2.40	$ 1.62	$ 2.40
Adjustment for reimbursement of transaction costs	$ 0.23		$ 0.23	
Adjustment for share issuance costs incurred to June 30, 2014	$ 0.28		$ 0.28	
Adjusted book value per share - at June 30 (2)	$ 2.13		$ 2.13	

(1) Adjusted to reflect a 50:1 share consolidation completed on October 1, 2013.

(2) After giving effect to the reimbursement of $3.1 million of transaction and related costs incurred by the Company in connection with the investment in Houston International Insurance Group, Ltd. (see discussion in Section 3, *Investment in HIIG* of this MD&A) and on behalf of the Partnership, and adjustment of share issuance costs of $3.8 million incurred by the Company in connection with related equity financing transactions (see discussion in Section 4, *Equity Financings* of this MD&A).

For the three and six months ended June 30, 2014, the Company reported a loss of $2.9 million and $4.5 million (2013 - $0.7 million and $1.2 million).

3. INVESTMENT IN HIIG

On July 31, 2014, the Partnership completed its previously announced acquisition (the "Acquisition") of approximately 70.8% of the issued and outstanding shares of common stock of HIIG, an international specialty insurance company headquartered in Houston, for an aggregate purchase price of approximately US$138.7 million.

The Acquisition involved:

(i) the purchase by the Partnership of an aggregate of 16,588,865 shares of common stock in the capital of HIIG ("HIIG Shares") from certain shareholders of HIIG (the "Sellers") for an aggregate purchase price of US$53.7 million; and

(ii) the purchase by the Partnership from HIIG of an aggregate of 18,702,673 HIIG Shares from treasury for an aggregate purchase price of US$85.0 million.

3. INVESTMENT IN HIIG (continued)

In order to complete the Acquisition and to provide working capital, the Partnership received funding of approximately US$141.1 million. This funding was provided as to (i) US$75.7 million by Westaim, (ii) US$24.3 million and US$22.9 million by affiliates of Everest Re Group, Ltd. and Catlin Group Limited, respectively, (iii) US$10.0 million by Stephen L. Way, Chairman and Chief Executive Officer of HIIG, and/or certain investors affiliated with Mr. Way, and (iv) US$8.2 million by certain other existing shareholders of HIIG and other investors.

The Company was reimbursed $3.1 million in transaction and related costs incurred in connection with the Acquisition and the formation of the Partnership. In addition, the Company was reimbursed US$0.8 million in share issuance costs related to its investment in the Partnership.

See discussion in Section 4, *Equity Financings* of this MD&A regarding equity financing arrangements completed in the three months ended June 30, 2014.

4. EQUITY FINANCINGS

In connection with the Acquisition, on April 23, 2014, Westaim completed the sale of an aggregate of 50,995,385 subscription receipts (the “Subscription Receipts”) at a purchase price of $2.65 per Subscription Receipt for aggregate gross proceeds of approximately $135.1 million (the “Subscription Receipt Offering”). On July 29, 2014, net proceeds of approximately $128.2 million from the Subscription Receipt Offering were released from escrow to Westaim and an aggregate of 50,995,385 additional common shares of Westaim (“Westaim Shares”) were issued upon the conversion of the Subscription Receipts. An additional 5,399,020 Westaim Shares were issued on July 31, 2014 to certain funds and co-investors (collectively, the “Investors”) pursuant to subscription agreements entered into by the Investors on April 23, 2014 (the “Additional Private Placement”). In connection with the Additional Private Placement, Westaim received additional gross proceeds of approximately $14.3 million.

On July 31, 2014, the Company used US$75.7 million of the proceeds from the Subscription Receipt Offering and the Additional Private Placement (collectively, the “Offerings”) to purchase Class A Limited Partnership Units in the Partnership to enable the Partnership (together with funds committed by other investors in the Partnership) to complete the Acquisition. The Partnership completed the Acquisition and acquired 70.8% of HIIG for US$138.7 million (see discussion in Section 3, *Investment in HIIG* of this MD&A). The remaining net proceeds of the Offerings will be used by the Company for general corporate purposes and to consider and possibly fund potential future acquisitions (including possible additional equity investments in the Partnership).

Immediately following the issuance of the common shares under the Offerings, the Company had 70,297,342 common shares outstanding.

5. ANALYSIS OF FINANCIAL RESULTS

Details of the Company’s operating results are as follows:

	Three months ended June 30		Six months ended June 30	
(millions)	2014	2013	2014	2013
Revenue	$ 0.0	$ 0.1	$ 0.1	$ 0.2
Expenses				
Salaries and benefits	0.2	0.4	0.4	0.7
Office expenses	0.3	0.2	0.5	0.5
Professional fees	0.8	0.2	2.1	0.3
Site restoration provision expense	0.8	0.0	0.8	0.0
Share-based compensation	0.0	-	0.1	-
Foreign exchange loss	0.8	-	0.7	-
Total expenses	2.9	0.8	4.6	1.5
Income tax recovery	-	0.0	-	0.1
Loss	$ (2.9)	$ (0.7)	$ (4.5)	$ (1.2)

Revenue

Revenue for the three and six months ended June 30, 2014 of $0.0 million and $0.1 million (2013 - $0.1 million and $0.2 million) consisted of interest on cash and cash equivalents.

5. ANALYSIS OF FINANCIAL RESULTS (continued)

Expenses

Expenses for the three and six months ended June 30, 2014 were $2.9 million and $4.6 million (2013 - $0.8 million and $1.5 million). The increase in expenses of $2.1 million in the second quarter of 2014 compared to the same period in the prior year and $3.1 million in the six months ended June 30, 2014 compared to the same period in 2013 was mainly due to a site restoration provision expense of $0.8 million, a foreign exchange loss of $0.8 million, as well as transaction and related costs incurred in connection with the investment in HIIG (see discussion in Section 3, *Investment in HIIG* of this MD&A) recorded in the second quarter of 2014. Following the completion of the Acquisition on July 31, 2014, the Company was reimbursed $3.1 million in transaction and related costs previously expensed by the Company.

6. ANALYSIS OF FINANCIAL POSITION

The Company's assets, liabilities and shareholders' equity consist of the following:

(millions)		June 30, 2014		December 31, 2013
Assets				
Cash and cash equivalents	$	31.1	$	35.4
Other assets		0.1		0.2
	$	31.2	$	35.6
Liabilities				
Accounts payable and accrued liabilities	$	5.6	$	2.5
Site restoration provision		3.0		2.2
		8.6		4.7
Shareholders' equity		22.6		30.9
Total liabilities and shareholders' equity	$	31.2	$	35.6

6.1 Cash and Cash Equivalents

At June 30, 2014, the Company had cash and cash equivalents of $31.1 million compared to $35.4 million at December 31, 2013. Included in cash and cash equivalents at June 30, 2014 was restricted cash of $0.6 million related to certain proceeds of the Subscription Receipt Offering held in escrow by the Company pending completion of the Acquisition. See also discussion in Section 8, *Liquidity and Capital Resources* of this MD&A.

6.2 Accounts Payable and Accrued Liabilities

Accounts payable and accrued liabilities were $5.6 million at June 30, 2014 and $2.5 million at December 31, 2013. The increase over the period was primarily related to the accrual of $3.8 million of share issuance costs related to the equity financing incurred during the quarter ended June 30, 2014. See discussion in Section 4, *Equity Financings* of this MD&A regarding equity financing arrangements completed in the three months ended June 30, 2014.

6.3 Site Restoration Provision

The site restoration provision of $3.0 million at June 30, 2014 and $2.2 million at December 31, 2013 relates to costs associated with soil and groundwater reclamation and remediation costs. The increase during the three and six months ending June 30, 2014 was related to a change in the long-term inflation rate assumption from 1.30% at December 31, 2013 to 1.58% at June 30, 2014 and a change in the discount rate due to a flattening of the yield curve during the second quarter. The Company conducts periodic reviews of the underlying assumptions supporting the provision, including remediation costs and regulatory requirements. Reimbursements of costs resulting from indemnifications provided by previous owners of the industrial sites have not been recognized in these consolidated financial statements. Future reimbursements will be recorded when received.

6. ANALYSIS OF FINANCIAL POSITION (continued)

6.4 Shareholders' Equity

The details of shareholders' equity are as follows:

(millions)		June 30, 2014		December 31, 2013
Common shares	$	199.8	$	203.6
Contributed surplus		12.9		12.9
Deficit		(190.1)		(185.6)
Shareholders' equity	$	22.6	$	30.9

Share issuance costs of $3.8 million incurred in connection with the Offerings were deducted from common shares at June 30, 2014. The increase in deficit of $4.5 million from December 31, 2013 to June 30, 2014 is due to the loss for the six months ended June 30, 2014.

7. OUTLOOK

The Company's investment in HIIG through the Partnership, which was completed after the end of the second quarter, is consistent with Westaim's strategy to deploy capital at above average risk-adjusted returns. Westaim has partnered with third party investors and an experienced management team with a proven track record in the attractive global specialty P&C insurance market.

Westaim plans to use the remaining cash raised as a result of the closing of the equity financing (see discussion in Section 4, *Equity Financings* of this MD&A) for general corporate purposes and to consider and possibly fund potential future acquisitions (including possible additional equity investments in the Partnership) consistent with its strategy.

The Company continues to seek additional investment opportunities to create meaningful shareholder value through partnering with aligned and capable management teams to build profitable businesses that generate attractive returns over the long term.

8. LIQUIDITY AND CAPITAL RESOURCES

Capital Management Objectives

The Company's guiding principles for capital management are to maintain the stability and safety of the Company for its stakeholders through optimal capital mix and an adequate level of capital, maintain a strong balance sheet, ensure the return on capital meets the Board of Directors' expectations relative to the risk taken, and minimize the after-tax cost of capital.

Towards achieving these objectives, the Company employs a strong and efficient capital base and manages capital in accordance with policies established by the Board of Directors. These policies relate to capital strength and capital mix. The Company has a capital management process in place to measure, deploy and monitor its available capital to assess its adequacy on a continuous basis. Management develops the capital strategy and oversees the capital management processes of the Company. The Company's capital consists of its shareholders' equity.

Share Capital

The Company's authorized share capital consists of an unlimited number of common shares, Class A preferred shares and Class B preferred shares. On October 1, 2013, the Company completed a 50:1 share consolidation of all of its outstanding common shares. All share capital, per share amounts, and share-based awards in the comparative period have been adjusted to reflect this change. At June 30, 2014 and December 31, 2013, the Company had 13,902,937 common shares outstanding. The Company had 5,000 stock options outstanding at June 30, 2014 and 6,000 options outstanding at December 31, 2013. At those dates, there were no Class A or Class B preferred shares outstanding.

Dividends

No dividends were paid in the six months ended June 30, 2014 and 2013.

8. LIQUIDITY AND CAPITAL RESOURCES (continued)

Share-based Compensation Plans

At the annual and special meeting (the "Meeting") of the shareholders of the Company held on June 19, 2014, the Company's shareholders approved an amendment to the Company's comprehensive long-term equity incentive plan (the "Incentive Plan") to adopt substantially the form of long-term incentive plan of the Company in place prior to the Company's shares being listed on the TSX-V, with certain exceptions. The amendments included (a) providing for grants of restricted share units, stock appreciation rights and other share-based awards in addition to DSUs, (b) providing the Board of Directors with the option of establishing a share purchase program; and (c) removing the ability of the Company to grant stock options under the Incentive Plan. Also at the Meeting, the shareholders of the Company approved the adoption of a stand-alone incentive stock option plan (the "Option Plan") in accordance with the policies of the TSX-V.

Unless increased in accordance with the terms of the plan and the rules of the TSX-V or any other applicable stock exchange, the maximum number of common shares which may be issued under the Incentive Plan is fixed at 7,042,150. The Option Plan is a "rolling plan" which provides that the aggregate number of common shares which may be reserved for issuance under the Option Plan is limited to not more than 10% of the aggregate number of common shares outstanding. However, each of the Incentive Plan and the Option Plan provide that under no circumstances shall there be common shares issuable under such plan, together with all other security-based compensation arrangements of the Company, which exceed 10% of the aggregate number of common shares outstanding. At June 30, 2014, the Company could have outstanding at any one time share-based awards exercisable for 1,390,293 common shares of the Company. Following the completion of the Acquisition and the Offerings (see discussion in Section 4, *Equity Financings* of this MD&A), the Company could have outstanding at any one time share-based awards exercisable for 7,029,734 common shares of the Company.

The Company had 5,000 stock options outstanding at June 30, 2014 and 6,000 stock options outstanding at December 31, 2013. At June 30, 2014 and December 31, 2013, the company had 113,200 DSUs outstanding, issued to non-executive directors of the Company. The DSUs were issued at the market value of the Company's common shares at the date of grant. Vested DSUs are paid out in cash when the participant ceases to be a director, officer or employee. An amount of $0.4 million related to outstanding DSUs was included in accounts payable and accrued liabilities as at June 30, 2014.

Market for Securities

On January 9, 2013, Westaim's common shares commenced trading on the TSX-V under the symbol "WED". Until January 8, 2013, the common shares of Westaim were listed on the Toronto Stock Exchange (the "TSX") under the symbol "WED". The Westaim Board of Directors determined that a listing with the TSX-V better suits the needs of the Company while providing continued trading liquidity for the Company's shareholders. The Company received approval of its listing on the TSX-V prior to voluntarily de-listing from the TSX.

Cash Flow Objectives

The Company manages its liquidity with a view to ensuring that there is sufficient cash to meet all financial commitments and obligations as they fall due. The Company believes its liquidity requirements for the next year will be met with the cash and cash equivalents on hand. The Company has sufficient funds to meet its financial obligations and pursue other opportunities. As part of pursuing one or more new opportunities, the Company may from time to time issue shares from treasury.

The following tables illustrate the duration of the financial assets of the Company compared to its financial obligations:

June 30, 2014 (millions)	One year or less	No specific date	Total
Financial assets:			
Cash and cash equivalents	$ 31.1	$ -	$ 31.1
Other assets	0.1	-	0.1
Total financial assets	31.2	-	31.2
Financial obligations:			
Accounts payable and accrued liabilities	5.6	-	5.6
Site restoration provision	-	3.0	3.0
Total financial obligations	5.6	3.0	8.6
Financial assets net of financial obligations	$ 25.6	$ (3.0)	$ 22.6

8. LIQUIDITY AND CAPITAL RESOURCES (continued)

December 31, 2013 (millions)	One year or less	No specific date	Total
Financial assets:			
Cash and cash equivalents	$ 35.4	$ -	$ 35.4
Other assets	0.2	-	0.2
Total financial assets	35.6	-	35.6
Financial obligations:			
Accounts payable and accrued liabilities	2.5	-	2.5
Site restoration provision	-	2.2	2.2
Total financial obligations	2.5	2.2	4.7
Financial assets net of financial obligations	$ 33.1	$ (2.2)	$ 30.9

The Company's investment guidelines stress preservation of capital and market liquidity to support payment of liabilities. The matching of the duration of financial assets and liabilities is monitored to ensure that all obligations will be met.

9. RELATED PARTY TRANSACTIONS

Transactions with key management personnel

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company, directly or indirectly, including directors of the Company.

Compensation expenses related to key management personnel, including non-executive directors, are as follows:

	Three months ended June 30		Six months ended June 30	
(millions)	2014	2013	2014	2013
Salaries and benefits	$ 0.2	$ 0.4	$ 0.4	$ 0.7

On April 23, 2014, an aggregate of 3,400,000 Subscription Receipts were purchased by certain directors and officers of the Company for aggregate gross proceeds of $9.0 million pursuant to the Subscription Receipt Offering. See discussion in Section 4, *Equity Financings* of this MD&A.

10. QUARTERLY FINANCIAL INFORMATION

(millions)	Q2 2014	Q1 2014	Q4 2013	Q3 2013	Q2 2013	Q1 2013	Q4 2012	Q3 2012
Revenue of continuing operations	$ 0.0	$ 0.1	$ 0.1	$ 0.1	$ 0.1	$ 0.1	$ 0.1	$ 0.1
Expenses of continuing operations	2.9	1.7	2.1	0.6	0.8	0.6	1.1	16.5
Gain on sale of discontinued operations	-	-	-	-	-	-	-	108.1
Profit from discontinued operations	-	-	-	-	-	-	-	3.7
Profit or loss and other comprehensive income	(2.9)	(1.6)	(2.0)	(0.5)	(0.7)	(0.5)	(1.0)	95.4

Quarterly revenue comprises investment income. Expenses can vary from quarter to quarter due to the share-based compensation expense which varies according to the market price of Westaim's common shares. The Company's expenses included transaction and related costs incurred in connection with the investment in HIIG of $0.5 million in the second quarter of 2014, $1.2 million in the first quarter of 2014 and $2.0 million in the fourth quarter of 2013. In the three months ended June 30, 2014, the Company also recorded a site restoration provision expense of $0.8 million and a foreign exchange loss of $0.8 million. In the fourth quarter of 2013, the Company recorded a site restoration provision recovery of $0.4 million.

Gain on sale of discontinued operations is the gain from the sale of Jevco Insurance Company ("Jevco"), an insurance company previously owned by the Company. Profit from discontinued operations for the third quarter of 2012 included two months of operating results from the Company's insurance business to the date of sale of Jevco on September 4, 2012.

11. RISKS

Westaim is subject to a number of risks, including the risks described below. The risks and uncertainties described below are those believed to be material, but they may not be the only ones faced by Westaim. If any of these risks, or any other risks and uncertainties that have not yet been identified by Westaim or that Westaim currently considers not to be material, actually occur or become material risks, the business, prospects, financial condition, results of operations and cash flows of Westaim could be materially and adversely affected.

Risks Relating to Westaim

Risks inherent in acquisitions generally

The Company intends to actively pursue the acquisition of companies or businesses in Canada and/or internationally and may seek to acquire securities or other interests in other companies consistent with its investment and growth strategy. Such acquisitions involve inherent risks including but not limited to (a) unanticipated costs; (b) potential loss of key employees of the Company or the business acquired; (c) unanticipated changes in business, industry or general economic conditions that affect the assumptions underlying the acquisition; and (d) decline in the value of the acquired business or assets. Any one or more of these factors could cause the Company to not realize the anticipated benefits of the acquisition in question. In addition, the Company may be required to use available cash, incur debt, issue securities, or a combination of these in order to complete an acquisition. This could affect the Company's future flexibility and ability to raise capital, operate or develop its business and could dilute its existing shareholders' holdings as well as decrease the trading price of its common shares. There is no assurance that when evaluating a possible acquisition, the Company will correctly identify and manage the risks and costs inherent in the business or asset to be acquired.

Volatile stock price

The price of Westaim's common shares is expected to be highly volatile and could be drastically affected by various factors. Westaim cannot predict the timing of future acquisitions or other developments expected to take place in the future which will likely trigger major changes in the trading price of the common shares.

Liquidity and financing risks

Westaim's ability to continue its acquisition efforts will be in part reliant on its continued attractiveness to equity investors. Westaim will incur operating losses as it continues to expend funds to explore and develop future business. There is no guarantee that Westaim will be able to develop a profitable business that it may acquire as general economic conditions, regulatory requirements and other factors affect Westaim's operations and future performance. Many of these factors are beyond Westaim's control. Additionally, should Westaim require additional capital to continue its activities, failure to raise such capital could restrict Westaim's activities or result in the Company going out of business. From time to time, Westaim may enter into transactions to acquire assets or the shares of other corporations. These transactions may be financed wholly or partially with debt, which may temporarily increase Westaim's debt levels above industry standards. Westaim cannot assure investors that it will be able to generate sufficient cash flow to pay the interest on any debt or that future working capital, borrowings or equity financing will be available to pay or refinance such debt.

Income taxes

The calculation of income taxes requires the use of estimates and judgment. The validity and measurement of tax benefits associated with various tax positions taken or expected to be taken in Westaim's tax filings are a matter of tax law and are subject to interpretation. The impact of the final determination of tax audits, appeals of decisions of a taxing authority, or tax litigation may be materially different from that reflected in the Company's financial statements. The assessment of additional taxes, interest and penalties could be materially adverse to Westaim's future results of operations and financial position.

Operational risks

In connection with its operations, the Company may from time to time be named as defendant in actions for damages and costs allegedly sustained by the plaintiffs. While it is not possible to estimate the outcome of the various proceedings at this time, such actions have generally been resolved with minimal expenses in excess of amounts provided for. The Company does not believe that it will incur any significant additional expenses in connection with such actions.

The Company has agreements to indemnify its officers and directors for certain events or occurrences while the officer or director is or was serving at the Company's request in such capacity. The maximum potential amount of future payments is unlimited. However, the Company maintains Director and Officer Liability insurance coverage that enables the Company to recover a portion of any future payments.

11. RISKS (continued)

Environmental risks

The Company has provided indemnifications to third parties with respect to future site restoration costs to be incurred on industrial sites formerly owned by the Company. The site restoration provision is based on periodic independent estimates of costs associated with soil and groundwater reclamation and remediation of these industrial sites. The Company has accounted for estimated future restoration costs in its financial statements (see note 5 to the Company's unaudited consolidated financial statements for the three and six months ended June 30, 2014 and 2013). Although the Company believes, based on consultation with experts and advisors, that such estimates are reasonable based on information currently available to the Company, the ultimate environmental costs are uncertain as they are dependent on the future use of the land and future laws and regulations. In addition, estimates of future expenditures could change as a result of periodic reviews of the underlying assumptions supporting the provision, including remediation costs and regulatory requirements.

Regulatory rules and required approvals might delay or deter a change of control of Westaim

Many state insurance regulatory laws contain provisions that require advance approval by state agencies of any change of control of an insurance company that is domiciled or, in some cases, has substantial business in that state. "Control" is generally presumed to exist through the ownership of 10% or more of the voting securities of a domestic insurance company or of any company that controls a domestic insurance company. As a subsidiary of Westaim is the general partner of the Partnership, which in turn owns greater than 50% of the outstanding common shares of HIIG, Westaim is considered to exercise control over HIIG and its insurance subsidiaries. Accordingly, any purchaser of Westaim Shares representing 10% or more of the voting power of all outstanding Westaim Shares will be presumed to have acquired control of HIIG's domestic insurance subsidiaries unless, following application by that purchaser, the relevant state insurance regulators determine otherwise. Any transaction that would constitute a change in control of any of HIIG's individual insurance subsidiaries would generally require prior approval by the insurance departments of the states in which the insurance subsidiary is domiciled.

Risks Relating to HIIG's Industry

As a property and casualty insurer, HIIG's business may suffer as a result of unforeseen catastrophe losses.

Property and casualty insurers are subject to claims arising from catastrophes. Catastrophes can be caused by various events, including hurricanes, tsunamis, tornados, windstorms, earthquakes, hailstorms, explosions, flooding, severe winter weather and fires and may include man-made events, such as terrorist attacks and systemic risks. The incidence, frequency and severity of catastrophes are inherently unpredictable. Some scientists believe that in recent years, changing climate conditions have added to the unpredictability and frequency of natural disasters. The extent of losses from a catastrophe is a function of both the total amount of insured exposure in the area affected by the event and the severity of the event.

Although HIIG typically purchases reinsurance protection for risks that it believes bear a significant level of catastrophe exposure, the nature or magnitude of losses attributed to a catastrophic event or events may result in losses that exceed HIIG's reinsurance protection. It is therefore possible that a catastrophic event or multiple catastrophic events could have a material adverse effect on HIIG's financial position, results of operations and liquidity.

The insurance and reinsurance business is historically cyclical, and HIIG expects to experience periods with excess underwriting capacity and unfavourable premium rates, which could cause its results to fluctuate.

The insurance and reinsurance business historically has been a cyclical industry characterized by periods of intense price competition due to excessive underwriting capacity, as well as periods when shortages of capacity permitted an increase in pricing and, thus, more favourable premium levels. An increase in premium levels is often, over time, offset by an increasing supply of insurance and reinsurance capacity, either from capital provided by new entrants or by additional capital committed by existing insurers or reinsurers, which may cause prices to decrease. In addition, changes in the frequency and severity of losses suffered by insureds and insurers may affect the cycles of the insurance and reinsurance business significantly. Any of these factors could lead to a significant reduction in premium rates, less favourable policy terms and fewer opportunities to underwrite insurance risks, which could have a material adverse effect on HIIG's results of operations and cash flows.

HIIG's loss reserves are based on an estimate of its future liability, which may prove to be inadequate.

HIIG maintains loss reserves to cover its estimated liability for unpaid losses and loss adjustment expenses, including legal and other fees, for reported and unreported claims incurred at the end of each accounting period. Reserves do not represent an exact calculation of liability. Rather, reserves represent an estimate of what HIIG expects the ultimate settlement and administration of claims will cost. These estimates are based on HIIG's assessment of facts and circumstances then known, as well as estimates of future trends in severity of claims, frequency of claims, judicial theories of liability and other factors. These variables are affected by both internal and external events that could increase HIIG's exposure to losses, including changes in actuarial projections, claims handling procedures, inflation, climate change, economic and judicial trends, and legislative changes.

11. RISKS (continued)

Volatility in the financial markets, economic events, legal/regulatory changes and other external factors may result in an increase in the number of claims and the severity of the claims reported. Many of these items are not directly quantifiable in advance. Additionally, there may be a significant reporting delay between the occurrence of the insured event and the time it is reported to HIIG.

The inherent uncertainties of estimating reserves are greater for certain types of liabilities, particularly those in which the various considerations affecting the type of claim are subject to change and in which long periods of time may elapse before a definitive determination of liability is made. Reserve estimates are continually refined in a regular and ongoing process as experience develops and further claims are reported and settled. Adjustments to HIIG's loss and loss adjustment expenses are reflected in its results of operations in the periods in which such estimates are changed. Because setting reserves is inherently uncertain, there can be no assurance that current reserves will prove adequate in light of subsequent events. If actual claims prove to be greater than HIIG's reserves, HIIG's financial position, results of operations and liquidity may be materially adversely affected.

The effects of emerging claim and coverage issues on HIIG's business are uncertain.

As industry practices and legal, judicial, social and other environmental conditions change, unexpected and unintended liability for claims and coverage may emerge. These changing conditions may adversely affect HIIG's business by either extending coverage beyond its underwriting intent or by increasing the number or size of claims. In some instances, these changes may not become apparent until considerable time after HIIG has issued insurance or reinsurance contracts that are affected by the changes. As a result, the full extent of liability under HIIG's insurance or reinsurance contracts may not be known for many years after a contract is issued, and HIIG's financial position, results of operations and cash flows may be materially adversely affected.

HIIG is subject to extensive governmental regulation.

HIIG is subject to extensive governmental regulation and supervision and its business depends on compliance with applicable laws and regulations and its ability to maintain valid licenses and approvals for its operations. Most insurance regulations are designed to protect the interests of policyholders rather than shareholders and other investors. In the United States, this regulation is generally administered by departments of insurance in each state in which HIIG does business and includes a comprehensive framework of oversight of its operations and review of its financial position. U.S. Federal legislation may lead to additional federal regulation of the insurance industry in the coming years.

Regulatory authorities have broad discretion to grant, renew or revoke licenses and approvals. Regulatory authorities may deny or revoke licenses for various reasons, including the violation of regulations. In some instances, HIIG follows practices based on its interpretations of regulations, or those it believes to be generally followed by the industry, which ultimately may be different from the requirements or interpretations of regulatory authorities. If HIIG does not have the requisite licenses and approvals and does not comply with applicable regulatory requirements, the insurance regulatory authorities could preclude or temporarily suspend HIIG from carrying on some or all of its activities or otherwise penalize it. That type of action could have a material adverse effect on HIIG's results of operations. Also, changes in the level of regulation of the insurance industry (whether federal, state or foreign), or changes in laws or regulations themselves or interpretations by regulatory authorities, could have a material adverse effect on HIIG's business.

The Dodd-Frank Act expands the U.S. Federal government's presence in insurance oversight, streamlines state-based regulation of reinsurance and non-admitted insurance and establishes a new Federal Insurance Office with powers over most lines of insurance other than health insurance. The Federal Insurance Office is authorized to gather data and information to monitor aspects of the insurance industry, identify issues in the regulation of insurers about insurance matters, and pre-empt state insurance measures under certain circumstances. As the Dodd-Frank Act calls for numerous studies and contemplates further regulation, its future impact on HIIG's results of operations or financial position cannot be determined at this time.

HIIG cannot predict the effect, if any, climate change may have on the risks it insures.

Various scientists, environmentalists, international organizations and regulators believe that global climate change has added, and will continue to add, to the unpredictability, frequency and severity of natural disasters (including, but not limited to, hurricanes, tornados, freezes, other storms and fires) in certain parts of the world. In response to this belief, a number of legal and regulatory measures as well as social initiatives have been introduced in an effort to reduce greenhouse gas and other carbon emissions, which may be chief contributors to global climate change. HIIG cannot predict the impact that changing climate conditions, if any, will have on its results of operations or financial condition. Moreover, HIIG cannot predict how legal, regulatory and social responses to concerns about global climate change will impact its business. To the extent climate change does increase the unpredictability, frequency or severity of natural disasters, HIIG may face increased claims, which could have a material adverse effect on its financial position, results of operations and cash flows.

11. RISKS (continued)

HIIG's reliance on agents and brokers subjects it to risk.

In many cases, HIIG markets its insurance through insurance agents and brokers. Some of these agents and brokers provide a significant portion of HIIG's gross written premium for a particular line of business. As a result, some of these agents and brokers could demand higher payments that could put HIIG at a competitive disadvantage and affect the way it prices its products. The deterioration of HIIG's relationship with, or loss of all or a substantial portion of the business provided by, one or more agents and brokers could have a material adverse effect on HIIG's financial position, results of operations and cash flows. HIIG also relies on these agents and brokers to accurately represent the nature of the policies that HIIG places. HIIG may be responsible for any misstatements, misrepresentations or other inappropriate market conduct by such agents or brokers.

In accordance with industry practice, HIIG generally pays amounts owed on claims under its insurance and reinsurance contracts to agents and brokers, and these agents and brokers, in turn, pay these amounts to the clients that have purchased insurance or reinsurance from HIIG. Although the law is unsettled and depends upon the facts and circumstances of the particular case, in some jurisdictions, if an agent or broker fails to make such a payment, HIIG may remain liable to the insured or ceding insurer for the deficiency. Conversely, in certain jurisdictions, when the insured or ceding insurer pays premiums for these policies to agents and brokers, these premiums might be considered to have been paid and the insured or ceding insurer will no longer be liable to HIIG for those amounts, whether or not HIIG has actually received the premiums from the agent or broker. Consequently, HIIG assumes a degree of credit risk associated with agents and brokers with whom it transacts business. However, due to the unsettled and fact-specific nature of the law, HIIG is unable to quantify its exposure to this risk.

Consolidation in the insurance industry could adversely impact HIIG.

Insurance industry participants may seek to consolidate through mergers and acquisitions. Continued consolidation within the insurance industry will further enhance the already competitive underwriting environment as HIIG would likely experience more robust competition from larger competitors. These consolidated entities may use their enhanced market power and broader capital base to take business from HIIG or to drive down pricing, which could adversely affect the results of HIIG's operations.

Risks Relating to HIIG's Business

Inability to accurately assess underwriting risk could reduce HIIG's net earnings.

HIIG's underwriting success is dependent on its ability to accurately assess the risks associated with the business on which the risk is retained. HIIG relies on the experience of its underwriting staff in assessing these risks. If HIIG fails to accurately assess the risks it retains, HIIG may fail to establish appropriate premium rates and its reserves may be inadequate to cover its losses, which could reduce its net earnings. The underwriting process is further complicated by HIIG's exposure to unpredictable developments, including earthquakes, weather-related events and other natural catastrophes, as well as war and acts of terrorism and those that may result from volatility in the financial markets, the economic downturn and systemic risks.

Retentions in various lines of business expose HIIG to potential losses.

HIIG retains risk for its own account on business underwritten by its insurance companies. The determination to not purchase reinsurance, or to reduce the amount of reinsurance HIIG purchases, for a particular risk or line of business is based on a variety of factors including market conditions, pricing, availability of reinsurance, the level of HIIG's capital and its loss history. Such determinations have the effect of increasing HIIG's financial exposure to losses associated with such risks or in such lines of business and, in the event of significant losses associated with such risks or lines of business, could have a material adverse effect on HIIG's financial position, results of operations and cash flows.

If HIIG is unable to purchase adequate reinsurance protection for some of the risks it has underwritten, HIIG will be exposed to any resulting unreinsured losses.

HIIG purchases reinsurance for a portion of the risks underwritten by its insurance companies, especially volatile and catastrophe-exposed risks. Market conditions beyond HIIG's control determine the availability and cost of the reinsurance protection it purchases. In addition, the historical results of reinsurance programs and the availability of capital also affect the availability of reinsurance. HIIG's reinsurance facilities are generally subject to annual renewal. HIIG cannot assure that it can maintain its current reinsurance facilities or that HIIG can obtain other reinsurance facilities in adequate amounts and at favourable rates. Further, HIIG cannot determine what effect catastrophic losses will have on the reinsurance market and on its ability to obtain adequate reinsurance at favourable rates. If HIIG is unable to renew or to obtain new reinsurance facilities on acceptable terms, either its net exposures would increase or, if HIIG was unwilling to bear such an increase in exposure, HIIG would have to reduce the level of its underwriting commitments, especially in catastrophe-exposed risks. Either of these potential developments could have a material adverse effect on HIIG's financial position, results of operations and cash flows.

11. RISKS (continued)

If the companies that provide HIIG's reinsurance do not pay all of its claims, HIIG could incur severe losses.

HIIG purchases reinsurance by transferring, or ceding, all or part of the risk it has assumed as a direct insurer to a reinsurance company in exchange for all or part of the premium HIIG receives in connection with the risk. Through reinsurance, HIIG has the contractual right to collect the amount reinsured from its reinsurers. Although reinsurance makes the reinsurer liable to HIIG to the extent the risk is transferred or ceded to the reinsurer, it does not relieve HIIG of its full liability to its policyholders. Accordingly, HIIG bears credit risk with respect to its reinsurers.

HIIG cannot assure that its reinsurers will pay all of HIIG's reinsurance claims, or that they will pay HIIG's claims on a timely basis. Additionally, catastrophic losses from multiple direct insurers may accumulate within the more concentrated reinsurance market and result in claims that adversely impact the financial condition of such reinsurers and thus their ability to pay such claims. Further, additional adverse developments in the capital markets could affect HIIG's reinsurers' ability to meet their obligations to HIIG. If HIIG becomes liable for risks it has ceded to reinsurers or if HIIG's reinsurers cease to meet their obligations to HIIG, because they are in a weakened financial position as a result of incurred losses or otherwise, HIIG's financial position, results of operations and cash flows could be materially adversely affected.

HIIG may be unsuccessful in competing against larger or more well-established business rivals.

HIIG faces competition from other specialty insurance companies, standard insurance companies and underwriting agencies, as well as from diversified financial services companies that are larger than HIIG and that have greater financial, marketing and other resources than HIIG does. Some of these competitors also have longer experience and more market recognition than HIIG does in certain lines of business. In addition, it may be difficult or prohibitively expensive for HIIG to implement technology systems and processes that are competitive with the systems and processes of these larger companies. HIIG cannot assure that it will maintain its current competitive position in the markets in which it operates, or that it will be able to expand its operations into new markets. If HIIG fails to do so, its results of operations and cash flows could be materially adversely affected.

HIIG invests a significant amount of its assets in securities that have experienced market fluctuations, which may reduce the value of its investment portfolio, reduce investment income or generate realized investment losses.

At December 31, 2013, a significant amount of HIIG's investment portfolio was invested in fixed maturity securities. The fair value of these fixed maturity securities and the related investment income fluctuate depending on general economic and market conditions, including volatility in the financial markets and the economy as a whole. For HIIG's fixed maturity securities, the fair value generally increases or decreases in an inverse relationship with fluctuations in interest rates and credit spreads, while net investment income realized by HIIG from future investments in fixed maturity securities will generally increase or decrease with interest rates. Mortgage-backed and asset-backed securities may have different net investment income and/or cash flows from those anticipated at the time of investment. These securities have prepayment risk because the timing of cash flows that result from the repayment of principal might occur earlier than anticipated, due to declining interest rates, or extension risk when cash flows may be received later than anticipated because of rising interest rates.

Although the vast majority of HIIG's fixed income portfolio is investment grade, all of HIIG's fixed maturity securities are subject to credit risk. For mortgage-backed securities, credit risk exists if mortgagors default on the underlying mortgages. During an economic downturn, HIIG's state, municipal and non-U.S. sovereign bond portfolios could be subject to a higher risk of default or impairments due to declining tax bases and revenue, notwithstanding the relatively low historical rates of default on these types of obligations. If any of the issuers of HIIG's fixed maturity securities suffer financial setbacks, the ratings on the fixed maturity securities could fall (with a concurrent fall in fair value) and, in a worst case scenario, the issuer could default on its financial obligations. If the issuer defaults, HIIG could realize losses associated with the impairment of the securities.

The impact of fluctuations in the market prices of securities affects HIIG's financial statements. Because all of HIIG's fixed maturity and equity securities are classified as available for sale, changes in the fair value of these securities are reflected in net unrealized investment gain or loss within HIIG's other comprehensive income. Similar treatment is not available for liabilities. Therefore, an increase in market interest rates could cause a decrease in HIIG's shareholders' equity and financial position.

Since 2008, the financial markets and the economy have been severely affected by various events. This has impacted interest rates and has caused large writedowns in other companies' financial instruments either due to the market fluctuations or the impact of the events on the debtors' financial condition. Turmoil in the financial markets and the economy, particularly related to potential future ratings downgrade and/or impairment of debt securities of sovereign issuers, could adversely affect the valuation of HIIG's investments and cause it to have to record other-than-temporary impairment credit losses on its investments, which could have a material adverse effect on HIIG's financial position and results of operations.

11. RISKS (continued)

If rating agencies downgrade HIIG's financial strength ratings, HIIG's business and competitive position in the industry may suffer.

Ratings have become an increasingly important factor in establishing the competitive position of insurance companies. HIIG's insurance companies are rated by A.M. Best Company, Inc. (A.M. Best). The financial strength ratings reflect the rating agencies' opinions of an insurance company's and insurance holding company's financial strength, operating performance, strategic position and ability to meet its obligations to policyholders and are not evaluations directed to investors. In addition, some organizations have internal requirements mandating that they transact only with insurance companies that have a specified rating level or higher. HIIG's ratings are subject to periodic review by A.M. Best, and the continuation of those ratings at current levels cannot be assured. If HIIG's ratings are reduced from their current levels, it could affect HIIG's ability to compete for high quality business and, thus, its financial position and results of operations could be adversely affected.

HIIG may require additional capital or funds for liquidity in the future, which may not be available or may only be available on unfavourable terms.

HIIG's future capital and liquidity requirements depend on many factors, including its ability to write new business successfully, to establish premium rates and reserves at levels sufficient to cover losses, and to maintain its current line of credit. HIIG may need to raise additional funds through financings or curtail its growth and reduce its assets. Any equity or debt financing, if available at all in periods of stress and volatility in the financial markets, may be on terms that are not favourable to HIIG. If HIIG cannot obtain adequate capital or funds for liquidity on favourable terms or at all, HIIG's business, results of operations and liquidity could be adversely affected. HIIG may also be pre-empted from making acquisitions.

A.M. Best rates HIIG's credit strength. If HIIG's credit ratings are reduced, it might significantly impede HIIG's ability to raise capital and borrow money, which could materially affect its business, results of operations and liquidity.

HIIG may be unable to attract and retain qualified employees.

HIIG depends on its ability to attract, retain and provide for the succession of skilled and experienced underwriting talent and other key employees (including its CEO and senior executive officers) who are knowledgeable about HIIG's business. Certain of HIIG's senior underwriters and other key employees have employment agreements that are for definite terms, and there is no assurance HIIG will retain these employees beyond the current terms of their agreements. If the quality of HIIG's underwriting team and other key personnel decreases, HIIG may be unable to maintain its current competitive position in the specialized markets in which it operates and be unable to expand its operations into new markets, which could materially adversely affect HIIG's business.

HIIG's strategy of acquiring other companies and underwriting teams for growth may not succeed.

HIIG's strategy for growth includes growing through acquisitions of insurance industry related companies. This strategy presents risks that could have a material adverse effect on HIIG's business and financial performance, including: i) the diversion of management's attention, ii) HIIG's ability to assimilate the operations and personnel of the acquired companies, iii) the contingent and latent risks associated with the past operations of, and other unanticipated problems arising in, the acquired companies, iv) the need to expand management, administration and operational systems and v) increased competition for suitable acquisition opportunities and qualified employees.

HIIG cannot predict whether it will be able to find suitable acquisition targets, nor can it predict whether it would be able to acquire these additional companies on terms favourable to HIIG or if it will be able to successfully integrate the acquired operations into its business. HIIG does not know if it will realize any anticipated benefits of completed acquisitions or if there will be substantial unanticipated costs associated with new acquisitions. In addition, future acquisitions by HIIG may result in potentially dilutive issuances of its equity securities, the incurrence of additional debt, and/or the recognition of potential impairment of goodwill and other intangible assets. Each of these factors could materially adversely affect HIIG's financial position and results of operations.

More recently, HIIG's growth has come through hiring underwriting teams focused on new lines of business. While more limited, many of the same risks above apply. Most notably, the diversion of management attention, the assimilation of new personnel and the need to expand management, administration and operational systems are present. Also, because these are new lines of business for which HIIG may have limited experience, the results of these new lines could materially adversely affect HIIG's financial position and results of operations.

HIIG may be *exposed to goodwill and intangible asset impairment risk as part of its business acquisition strategy.*

HIIG has recorded goodwill and intangible assets in connection with the majority of its business acquisitions. HIIG is required to perform goodwill and intangible asset impairment tests at least annually and whenever events or circumstances indicate that the carrying value of HIIG's goodwill may not be recoverable from estimated future cash flows. As a result of annual and other periodic evaluations, HIIG may determine that a portion of its goodwill or intangible assets needs to be written down to fair value, which could materially adversely affect HIIG's financial position and results of operations.

11. RISKS (continued)

HIIG is an insurance holding company and, therefore, may not be able to receive dividends in needed amounts from its insurance company subsidiaries.

In the past, HIIG has had sufficient cash flow from its non-insurance company subsidiaries to meet its corporate cash flow requirements for paying principal and interest on outstanding debt obligations, dividends to shareholders and corporate expenses. More recently, HIIG has relied on, and in the future it may rely on, dividends from HIIG's insurance companies to meet these requirements. The payment of dividends by HIIG's insurance companies is subject to regulatory restrictions and will depend on the surplus and future earnings of these subsidiaries, as well as the regulatory restrictions. As a result, should HIIG's other sources of funds prove to be inadequate, HIIG may not be able to receive dividends from its insurance companies at times and in amounts necessary to meet its obligations, which could materially adversely affect HIIG's financial position and liquidity.

HIIG's information technology systems or third-party systems that it utilizes or accesses may fail or suffer a loss of security, which could adversely affect HIIG's business.

HIIG's business is highly dependent upon the successful and uninterrupted functioning of its computer systems. HIIG relies on these systems to perform actuarial and other modeling functions necessary for writing business, to process premiums and policies, to process and make claims payments, to establish loss reserves, and to prepare management and external financial statements and information. The failure of these systems could interrupt HIIG's operations. In addition, in the event of a disaster such as a natural catastrophe, a blackout, a computer virus or hacking incident, a terrorist attack or war, HIIG's systems may be inaccessible for an extended period of time. These systems failures or disruptions could result in a material adverse effect on HIIG's business results. HIIG also utilizes and/or relies on computer systems developed and maintained by outsourcing relationships and key vendors. Their systems could experience the same risks, which could result in a material adverse effect on HIIG's business results.

A security breach of HIIG's computer systems could damage its reputation or result in liability. HIIG retains confidential information regarding its business dealings in its computer systems. HIIG may be required to spend significant capital and other resources to protect against security breaches or to alleviate problems caused by such breaches. Despite the implementation of security measures, the infrastructure supporting HIIG's computer systems may be vulnerable to physical break-ins, computer viruses, programming errors, attacks by third parties or similar disruptive problems. In addition, HIIG could be subject to liability if hackers were able to penetrate its network security or otherwise misappropriate confidential information. Furthermore, certain of HIIG's businesses are subject to compliance with laws and regulations enacted by U.S. federal and state governments, the European Union or other jurisdictions or enacted by various regulatory organizations or exchanges relating to the privacy and security of the information of clients, employees or others. The compromise of personal, confidential or proprietary information could result in remediation costs, legal liability, regulatory action and reputational harm, which could have a material adverse effect on HIIG's results of operations or financial condition.

If HIIG experiences difficulties with outsourcing relationships, its ability to conduct its business might be negatively impacted.

HIIG outsources certain business and administrative functions to third parties and may do so increasingly in the future. If HIIG fails to develop and implement its outsourcing strategies or its third party providers fail to perform as anticipated, HIIG may experience operational difficulties, increased costs and a loss of business that may have a material adverse effect on its results of operations or financial position. In addition, HIIG may be responsible for the actions of such third parties particularly if they violate or are inconsistent with applicable regulatory requirements. By outsourcing certain business and administrative functions to third parties, HIIG may be exposed to enhanced risk of data security breaches. Any breach of data security could damage HIIG's reputation and/or result in monetary damages, which could have a material adverse effect on HIIG's results of operations or financial condition.

12. CAUTIONARY NOTE REGARDING FUTURE ORIENTED FINANCIAL INFORMATION

Certain portions of this MD&A, as well as other public statements by the Company, contain forward-looking statements. In particular, the words "strategy", "may", "will", "continue", "developed", "objective", "potential", "exploring", "could", "expect", "expected", "expects", "tends", "indicates", and words and expressions of similar import, are intended to identify forward-looking statements. Such forward-looking statements include but are not limited to statements concerning: strategies, alternatives and objectives to maximize value for shareholders; expectations and assumptions relating to the Company's business plan; expectations and assumptions relating to HIIG's business and operations; expectations regarding the Company's assets and liabilities; the Company's ability to retain key employees; management's belief that its estimates for determining the valuation of the Company's assets and liabilities are appropriate; the Company's views regarding potential future remediation costs; the effect of changes to interpretations of tax legislation on income tax provisions in future periods; and the Company's determination that the adoption of new accounting standards will not have a material impact on its consolidated financial statements.

12. CAUTIONARY NOTE REGARDING FUTURE ORIENTED FINANCIAL INFORMATION (continued)

These statements are based on current expectations that are subject to risks, uncertainties and assumptions and the Company can give no assurance that these expectations are correct. By their nature, these statements are subject to inherent risks and uncertainties that may be general or specific. A variety of material factors, many of which are beyond the Company's control, may affect the operations, financial position, performance and results of the Company and its business, and could cause actual results to differ materially from the expectations expressed in any of these forward-looking statements.

The Company's actual results or financial position could differ materially from those anticipated by these forward-looking statements for various reasons generally beyond the Company's control, including, without limitation, the following factors: the Company's ability to implement its strategy or operate its business as management currently expects; the Company and/or HIIG may have undisclosed liabilities; the Company's ability to obtain additional funding to pursue additional acquisitions or other investments; HIIG's ability to accurately assess the risks associated with the insurance policies that it writes and to adequately reserve against future claims; unfavourable capital market developments or other factors which may affect the investments of the Company and/or HIIG; the cyclical nature of the P&C insurance industry; HIIG's ability to accurately predict future claims frequency; government regulations designed to protect policyholders and creditors rather than investors; litigation and regulatory actions; periodic negative publicity regarding the insurance industry; intense competition and/or industry consolidation; HIIG's reliance on brokers and third parties to sell its products to clients; HIIG's ability to successfully pursue its acquisition strategy; HIIG's ability to execute its business strategy; HIIG's ability to achieve synergies arising from successful integration plans relating to acquisitions, as well as management's estimates and expectations in relation to resulting accretion, internal rate of return and debt-to-capital ratio; terrorist attacks and ensuing events; the occurrence of catastrophic events including weather related natural disasters; HIIG's ability to maintain its financial strength and issuer credit ratings; access to debt financing and HIIG's ability to compete for large commercial business; HIIG's ability to alleviate risk through reinsurance; HIIG's ability to successfully manage credit risk (including credit risk related to the financial health of reinsurers); HIIG's reliance on information technology and telecommunications systems; dependence by the Company and HIIG on key employees and certain third party service providers; changes in laws or regulations; general economic, financial and political conditions; HIIG's dependence on the results of operations of its subsidiaries; the volatility of the stock market and other factors affecting the Company's share price; future sales of a substantial number of the Company's common shares; and other risk factors set forth herein or in the Company's annual report or other public filings.

The Company disclaims any intention or obligation to revise forward-looking statements whether as a result of new information, future developments or otherwise except as required by law. All forward-looking statements are expressly qualified in their entirety by this cautionary statement.

The Westaim Corporation
Consolidated Statements of Financial Position
(unaudited)

(thousands of Canadian dollars)		June 30 2014		December 31 2013
ASSETS				
Current				
Cash and cash equivalents (note 7)	$	31,098	$	35,412
Accounts receivable and other assets		101		159
	$	31,199	$	35,571
LIABILITIES				
Current				
Accounts payable and accrued liabilities	$	5,622	$	2,450
Site restoration provision (note 5)		3,036		2,219
		8,658		4,669
Commitments and contingent liabilities (note 6)				
Subsequent event (note 14)				
SHAREHOLDERS' EQUITY				
Share capital (note 7)		199,804		203,640
Contributed surplus (note 2h)		12,890		12,890
Deficit		(190,153)		(185,628)
		22,541		30,902
	$	31,199	$	35,571

The accompanying notes are an integral part of these consolidated financial statements

The Westaim Corporation
Consolidated Statements of Profit or Loss and Other Comprehensive Income
(unaudited)

	Three Months Ended June 30		Six Months Ended June 30	
(thousands of Canadian dollars except share and per share data)	2014	2013	2014	2013
Revenue				
Investment income	$ 29	$ 109	$ 87	$ 214
Expenses				
Salaries and benefits	223	409	469	699
Office expenses	338	227	488	468
Professional fees (note 4)	752	208	2,054	347
Site restoration provision expense (note 5)	808	7	817	14
Share-based compensation (note 8)	39	-	123	-
Foreign exchange loss	768	-	661	-
	2,928	851	4,612	1,528
Loss before income tax	(2,899)	(742)	(4,525)	(1,314)
Income tax recovery	-	4	-	124
Profit or loss and other comprehensive income	$ (2,899)	$ (738)	$ (4,525)	$ (1,190)
Earnings per share (note 11)				
Profit or loss and other comprehensive income - basic and diluted	$ (0.21)	$ (0.05)	$ (0.33)	$ (0.09)
Weighted average number of common shares outstanding (in thousands)				
Basic and diluted	13,903	13,903	13,903	13,903

The accompanying notes are an integral part of these consolidated financial statements

The Westaim Corporation
Consolidated Statements of Changes in Equity
(unaudited)

Six months ended June 30, 2014

(thousands of Canadian dollars)	Share Capital	Contributed Surplus	Deficit	Total Equity
Balance at January 1, 2014	$ 203,640	$ 12,890	$ (185,628)	$ 30,902
Share issuance costs (note 7)	(3,836)	-	-	(3,836)
Profit or loss and other comprehensive income	-	-	(4,525)	(4,525)
Balance at June 30, 2014	$ 199,804	$ 12,890	$ (190,153)	$ 22,541

Six months ended June 30, 2013

(thousands of Canadian dollars)	Share Capital	Contributed Surplus	Deficit	Total Equity
Balance at January 1, 2013	$ 203,640	$ 12,890	$ (181,918)	$ 34,612
Profit or loss and other comprehensive income	-	-	(1,190)	(1,190)
Balance at June 30, 2013	$ 203,640	$ 12,890	$ (183,108)	$ 33,422

The accompanying notes are an integral part of these consolidated financial statements

The Westaim Corporation
Consolidated Cash Flow Statements
(unaudited)

(thousands of Canadian dollars)	Six Months Ended June 30 2014	2013
Operating activities		
Profit or loss	$ (4,525)	$ (1,190)
Income tax recovery	-	(120)
Income taxes paid	-	(1,410)
Share-based compensation	123	-
Site restoration provision expense	817	14
Net change in other non-cash balances [1]	(689)	154
Cash used in operating activities	(4,274)	(2,552)
Financing activities		
Share issuance costs [1]	(40)	-
Cash used in financing activities	(40)	-
Net decrease in cash and cash equivalents	(4,314)	(2,552)
Cash and cash equivalents, beginning of period	35,412	39,164
Cash and cash equivalents, end of period	$ 31,098	$ 36,612
Cash and cash equivalents is comprised of:		
Cash - unrestricted	30,545	36,612
Cash - restricted	553	-
	$ 31,098	$ 36,612

[1] Non-cash share issuance costs of $3,796 have been excluded.

The accompanying notes are an integral part of these consolidated financial statements

1 Nature of Operations and Basis of Preparation

The Westaim Corporation (the "Company") was incorporated on May 7, 1996 by articles of incorporation under the Business Corporations Act (Alberta). The Company's registered office is located at 201-212 King Street West, Toronto, Ontario, Canada. These financial statements were authorized for issue by the Board of Directors of the Company on August 14, 2014.

On July 31, 2014, the Company completed the acquisition of a significant interest in Houston International Insurance Group, Ltd. ("HIIG") through Westaim HIIG Limited Partnership (the "Partnership"), an Ontario limited partnership managed by a subsidiary of the Company. HIIG is a U.S. based diversified specialty insurance provider and managing general insurance agent covering risks across the United States and certain niche global markets. See notes 4, 7 and 14 for additional information on the acquisition and related financing transactions.

On January 9, 2013, the Company's common shares commenced trading on the TSX Venture Exchange ("TSX-V") under the symbol WED. Until January 8, 2013, the Company's common shares were traded on the Toronto Stock Exchange under the symbol WED. Concurrent with the commencement of trading on the TSX Venture Exchange, the Company's common shares were voluntarily delisted from the Toronto Stock Exchange. On October 1, 2013, the Company completed a 50:1 share consolidation of all of its outstanding common shares. All share capital, per share amounts, and share-based awards in the current and comparative periods have been adjusted to reflect this change.

These financial statements are prepared in compliance with International Financial Reporting Standards ("IFRS"), including International Accounting Standard ("IAS") 34 *"Interim Financial Reporting"*, and include, on a consolidated basis, the accounts of wholly-owned subsidiaries, Westaim Management GP Inc. and Westaim HIIG GP Inc.

All currency amounts are expressed in thousands of Canadian dollars except earnings per share data, unless otherwise noted.

2 Summary of Significant Accounting Policies

The significant accounting policies used to prepare these financial statements are as follows:

(a) Principles of consolidation

The financial statements of entities which are controlled by the Company through voting equity interests, referred to as subsidiaries, are consolidated. The financial results of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. Intercompany balances and transactions are eliminated upon consolidation.

(b) Use of estimates

The preparation of financial statements requires management to make estimates that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates and changes in estimates are recorded in the reporting period in which they are determined. The key estimates used in these financial statements relate to the site restoration provision and are discussed in note 2(g) and note 5.

(c) Judgments made by management

Key areas where management has made difficult, complex or subjective judgments in the process of applying the Company's accounting policies, often as a result of matters that are inherently uncertain, include the site restoration provision and income taxes. For additional information on these judgments, see note 5 for site restoration provision and note 10 for income taxes.

(d) Foreign currency translation

The Canadian dollar is the functional and presentation currency of the Company. Transactions in foreign currencies are translated into Canadian dollars at rates of exchange prevailing at the time of such transactions. Monetary assets and liabilities are translated at current rates of exchange at the end of the period.

(e) Cash and cash equivalents

Cash and cash equivalents consist of cash on deposit and highly liquid short-term investments with original maturities of 90 days or less.

Cash and cash equivalents are classified in the financial instrument category of loans and receivables for purposes of measurement. Cash and cash equivalents are valued at fair value at the issuance date and subsequently at amortized cost using the effective interest method. Carrying value is a reasonable approximation of fair value.

2 Summary of Significant Accounting Policies (continued)

(f) Income taxes

Income tax expense is recognized in the statement of profit or loss and other comprehensive income. Current tax is based on taxable income which differs from profit or loss and other comprehensive income because of items of income or expense that are taxable or deductible in other years and items that are never taxable or deductible.

Deferred tax assets are generally recognized for all deductible temporary income tax differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilized. Deferred tax liabilities are generally recognized for all taxable temporary differences. Deferred tax assets and liabilities are determined based on the enacted or substantively enacted tax laws and rates that are anticipated to apply in the year of realization. The measurement of deferred tax assets and liabilities reflects the tax consequences that would follow from the manner in which the Company expects to recover or settle the carrying amount of the related assets and liabilities. The carrying amount of the deferred tax asset is reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Income tax assets and liabilities are offset when the Company intends to settle on a net basis and there is a legally enforceable right to offset.

(g) Site restoration provision

Future site restoration costs relate to industrial sites previously owned by the Company and are estimated taking into consideration the anticipated method and extent of the remediation consistent with regulatory requirements, industry practices, current technology and possible uses of the site. The estimated amount of future restoration costs is reviewed periodically based on available information. The amount of the provision is the present value of the estimated future restoration costs discounted using the rate of interest of a high quality government bond.

Recoveries of costs resulting from indemnifications provided by previous owners of the Company's industrial sites have not been recognized in these financial statements. Future recoveries of site restoration costs will be recorded when received.

(h) Contributed surplus

The cost of stock options is recognized over the period from the issue date to the vesting date and recorded as contributed surplus. When share capital of the Company is repurchased by the Company, the amount by which the average carrying value of the shares exceeds the cost to repurchase the shares is removed from share capital and included in contributed surplus.

(i) Share-based compensation

The Company maintains share-based compensation plans, which are described in note 8. Any consideration paid by stock option holders for the purchase of stock is credited to share capital. The cost of stock options is recognized over the period from the issue date to the vesting date and recorded as a component of equity in contributed surplus.

Obligations related to Deferred Share Units ("DSUs") are accrued as liabilities when issued. When a change in value occurs, it is recognized in compensation expense in the applicable financial period.

(j) Earnings per share

Basic earnings per share is calculated by dividing profit or loss by the total of the weighted average number of common shares outstanding during the reporting period. Profit or loss equals profit or loss and other comprehensive income for the three and six months ended June 30, 2014 and 2013.

Diluted earnings per share is calculated on the basis of the weighted average number of shares outstanding during the reporting period plus an estimate of the additional common shares that would have been outstanding if potentially dilutive common shares had been issued using the "treasury stock" method. No adjustments to profit or loss are required for dividends, interest or other changes in income for purposes of calculating diluted earnings per share.

3 Recently Adopted and Pending Accounting Pronouncements

In December 2011, amendments to IAS 32 "*Financial Instruments: Presentation*" were issued to clarify the existing requirements for offsetting financial assets and financial liabilities. The amendments are effective for annual periods beginning on or after January 1, 2014. The adoption of these amendments did not have an impact on the Company's interim consolidated financial statements.

In May 2013, International Financial Reporting Standards Interpretations Committee Interpretation 21: Levies ("IFRIC 21") was issued. IFRIC 21 addresses various accounting issues relating to levies imposed by a government. This interpretation is effective for annual periods beginning on or after January 1, 2014. The adoption of IFRIC 21 did not have an impact on the Company's interim consolidated financial statements.

In November 2009, the IASB issued IFRS 9 *"Financial Instruments"* ("IFRS 9") as part of its plan to replace IAS 39 *"Financial Instruments: Recognition and Measurement"*. IFRS 9 requires financial assets, including hybrid contracts, to be measured at either fair value or amortized cost. In October 2010, the IASB amended the requirements for classification and measurement of financial assets and liabilities. In November 2013, the IASB introduced a new hedge accounting model and allowed early adoption of the own credit provisions of IFRS 9. In July 2014, the IASB issued the final version of IFRS 9 incorporating a new expected loss impairment model and introducing limited amendments to the classification and measurement requirements for financial assets. This version supersedes all previous versions and is mandatorily effective for periods beginning on or after January 1, 2018 with early adoption permitted.

4 Investments

On March 12, 2014, the Company announced that the Partnership had agreed to acquire an approximate 42.5% equity ownership interest in HIIG for aggregate consideration of approximately US$75,000 (the "Initial Acquisition") through (i) the purchase of shares from certain existing shareholders of HIIG (the "Sellers") for approximately US$15,000 and (ii) the subscription for stock from HIIG's treasury for approximately US$60,000, subject to closing adjustments. The Company had agreed to provide a US$20,000 capital commitment to the Partnership to fund, in part, the Initial Acquisition.

Under a stock purchase agreement entered into in connection with, and as a condition to, the completion of the Initial Acquisition, the Partnership also had the right and obligation to purchase the remaining shares of HIIG owned by the Sellers (24.6% with the completion of the Acquisition) for an aggregate purchase price of approximately US$38,700, subject to closing adjustments (the "Second Acquisition", and together with the Initial Acquisition, the "Acquisition"). Completion of the Second Acquisition was conditional on the Partnership raising the funds necessary to complete such purchase on terms reasonably satisfactory to the Partnership. See note 7 regarding equity financing arrangements completed in the three months ended June 30, 2014.

On April 30, 2014, the Board of Directors of the Company approved an additional equity investment in the Partnership of up to US$25,000 to fund (subject to the pre-emptive rights of other Partnership investors) the Partnership's subscription for additional stock from HIIG's treasury contingent on the closing of the Acquisition (the "Supplemental Treasury Purchase"). Based on commitments received from certain of the Partnership's other investors, the contribution of the Company was approximately US$16,800.

The Acquisition was subject to the receipt of all requisite regulatory approvals, including TSX Venture Exchange approval, and other regulatory approvals required under applicable U.S. competition and insurance laws, including approval of the Departments of Insurance of the States of Texas and Oklahoma.

The Acquisition and the Supplemental Treasury Purchase were completed on July 31, 2014, and the Partnership acquired 70.8% of HIIG for US$138,683. See note 14 *Subsequent Event.* The Company incurred transaction and related costs in connection with the Acquisition and the Supplemental Treasury Purchase of $1,942 in 2013, and $525 and $1,695 in the three and six months ended June 30, 2014, and $3,156 was reimbursed at closing. The Company's investment in the Partnership at closing was US$75,712, representing a 53.3% ownership interest in the Partnership.

(Currency amounts in thousands of Canadian dollars unless otherwise indicated)

5 Site Restoration Provision

The Company has provided indemnifications to third parties with respect to future site restoration costs to be incurred on industrial sites formerly owned by the Company. The site restoration provision is based on periodic independent estimates of costs associated with soil and groundwater reclamation and remediation of these industrial sites. The ultimate environmental costs are uncertain as they are dependent on the future use of the land and future laws and regulations.

Changes to the site restoration provision for the six months ended June 30, 2014 and 2013 are as follows:

	Six months ended June 30	
	2014	2013
Balance at January 1	$ 2,219	$ 2,663
Changes due to:		
Inflation	256	-
Passage of time and discount rates	561	14
Balance at June 30	$ 3,036	$ 2,677

Estimates of future expenditures could change as a result of periodic reviews of the underlying assumptions supporting the provision, including remediation costs and regulatory requirements. The Company does not expect to settle any portion of the site restoration provision within twelve months after June 30, 2014.

Cash flows are estimated to take place over the next 150 years, with the majority to take place later than 50 years after June 30, 2014. To calculate the site restoration provision, the estimated cash flows were adjusted for inflation and discounted to June 30, 2014. For inflation and discounting calculations, all cash flows later than 50 years are treated as if the cash flow would occur at 100 years. Inflation is estimated at 1.58% per annum over the next 100 years. Discount rates are based on risk free rates which range from 1.0% to 2.8% over the next 30 years. The 30-year risk free rate is used for discounting cash flows that are estimated to occur later than 30 years after June 30, 2014.

Reimbursements of future costs resulting from indemnifications provided by previous owners of the industrial sites have not been recognized in these financial statements. Future reimbursements will be recorded when received.

6 Commitments and Contingent Liabilities

(a) To fund the Initial Acquisition, the Partnership obtained signed equity commitment letters from the Company and certain other investors for an aggregate of approximately US$77,175. Pursuant to these equity commitment letters, the Partnership would collectively be funded as to (i) US$20,000 by the Company and (ii) approximately US$57,175 by other investors.

(b) On April 30, 2014, the Board of Directors of the Company approved an additional equity investment in the Partnership of up to US$25,000 to fund (subject to the pre-emptive rights of other Partnership investors) the Partnership's subscription for additional stock from HIIG's treasury contingent on the closing of the Acquisition. Based on commitments received from certain of the Partnership's investors, the contribution of the Company was approximately US$16,800.

(c) In connection with the sale of the operations and assets of WHL in 2009, WHL agreed to indemnify the purchaser against certain liabilities or losses as described in the asset purchase agreement to an aggregate maximum of US$11,000, subject to certain exclusions. The Company also agreed to indemnify the purchaser and the purchaser's directors, officers and employees, for an indefinite period, from certain environmental liabilities and costs relating to the premises formerly leased by WHL in Fort Saskatchewan, Alberta. No claims have been made under, and no amounts have been accrued related to, these indemnities.

(d) The Company has operating leases in Toronto with remaining lease terms of up to 6 years. At June 30, 2014, the Company had a total commitment of $1,591 for future minimum lease payments including payments due not later than one year of $258, payments due later than one year and not later than five years of $1,216, and payments due later than five years of $117.

7 Share Capital

The Company's authorized share capital consists of an unlimited number of common shares with no par value, Class A preferred shares with no par value and Class B preferred shares with no par value.

The Company's share capital consisted of 13,902,937 common shares with stated capital of $199,804 at June 30, 2014 and $203,640 at December 31, 2013. In the year ended December 31, 2013, 3 common shares were cancelled.

7 Share Capital (continued)

On October 1, 2013, the Company completed a 50:1 share consolidation of all of its outstanding common shares. All share capital, per share amounts, and share-based awards in the current and comparative periods have been adjusted to reflect this change.

No shares of the Company are held by the Company, and there were no Class A preferred shares or Class B preferred shares outstanding at June 30, 2014 and December 31, 2013.

On April 23, 2014, the Company completed the sale, on an underwritten private placement basis, of 47,180,380 subscription receipts (the "Subscription Receipts") of the Company at a price of $2.65 per Subscription Receipt (the "Offering Price") for aggregate gross proceeds to the Company of approximately $125,028 (the "Offering"). The Company also completed a concurrent non-brokered private placement of 3,815,005 Subscription Receipts on the same terms as the Offering for aggregate gross proceeds to the Company of approximately $10,110 (the "Concurrent Private Placement"). Investors in the Concurrent Private Placement include primarily members of the Company's Board of Directors and management team.

Under the terms of the Offering and the Concurrent Private Placement, the net proceeds of the Offering and the Concurrent Private Placement were to be held in escrow pending satisfaction of certain escrow release conditions, including the satisfaction of all conditions required to complete the Acquisition (other than payment of the purchase price) and the receipt of all regulatory approvals (the "Escrow Release Conditions"). Upon satisfaction of the Escrow Release Conditions, each Subscription Receipt would entitle the holder to receive, for no additional consideration, one common share of the Company.

Concurrent with the closing of the Offering and the Concurrent Private Placement, the Company also entered into irrevocable subscription agreements with certain funds and co-investors (collectively, the "Investors") for the subscription of 5,399,020 common shares of the Company at a price of $2.65 per share, for aggregate gross proceeds to the Company of $14,307 (the "Additional Subscription"). The Investors were shareholders of HIIG (and members of the Seller group) and they agreed to use the proceeds from the sale of their shares of HIIG to the Partnership pursuant to the Acquisition to fund the Additional Subscription. The conditions to the closing of the Additional Subscription were the same as the Escrow Release Conditions under the Offering and the Concurrent Private Placement.

The Escrow Release Conditions were satisfied on July 29, 2014 and the Company used $75,712 of the proceeds from the Offering and the Concurrent Private Placement to purchase Class A Limited Partnership Units in the Partnership to enable the Partnership (together with funds committed by other investors in the Partnership) to satisfy the cash consideration payable by the Partnership in connection with the Acquisition and the Supplemental Treasury Purchase. See note 4 for additional information on the investment in HIIG and note 14 *Subsequent Event*. The remaining net proceeds of the Offering, the Concurrent Private Placement and the Additional Subscription will be used by the Company for general corporate purposes and to consider and possibly fund potential future acquisitions (including possible additional equity investments in the Partnership).

Included in cash and cash equivalents at June 30, 2014 was restricted cash of $553 related to certain proceeds of the Offering and the Concurrent Private Placement held in escrow by the Company pending satisfaction of the Escrow Release Conditions, with a corresponding credit in current liabilities at June 30, 2014. Costs of $3,836 incurred in connection with the Offering, the Concurrent Private Placement and the Additional Subscription were deducted from share capital at June 30, 2014.

8 Share-based Compensation

At the annual and special meeting (the "Meeting") of the shareholders of the Company held on June 19, 2014, the Company's shareholders approved an amendment to the Company's comprehensive long-term equity incentive plan (the "Incentive Plan") to adopt substantially the form of long-term incentive plan of the Company in place prior to the Company's shares being listed on the TSX-V, with certain exceptions. The amendments included (a) providing for grants of restricted share units, stock appreciation rights and other share-based awards in addition to DSUs, (b) providing the Board of Directors with the option of establishing a share purchase program; and (c) removing the ability of the Company to grant stock options under the Incentive Plan. Also at the Meeting, the shareholders of the Company approved the adoption of a stand-alone incentive stock option plan (the "Option Plan") in accordance with the policies of the TSX-V.

Unless increased in accordance with the terms of the plan and the rules of the TSX-V or any other applicable stock exchange, the maximum number of common shares which may be issued under the Incentive Plan is fixed at 7,042,150. The Option Plan is a "rolling plan" which provides that the aggregate number of common shares which may be reserved for issuance under the Option Plan is limited to not more than 10% of the aggregate number of common shares outstanding. However, each of the Incentive Plan and the Option Plan provide that under no circumstances shall there be common shares issuable under such plan, together with all other security-based compensation arrangements of the Company, which exceed 10% of the aggregate number of common shares outstanding. At June 30, 2014, the Company could have outstanding at any one time share-based awards exercisable for 1,390,293 common shares of the Company.

(Currency amounts in thousands of Canadian dollars unless otherwise indicated)

8 Share-based Compensation (continued)

Stock Options - Changes to the number of stock options for the six months ended June 30, 2014 and 2013 are as follows:

	Six months ended June 30, 2014		Six months ended June 30, 2013 (1)	
Common share stock options	Number	Weighted Average Exercise Price in dollars	Number	Weighted Average Exercise Price in dollars
Outstanding at January 1	6,000	$ 165.25	7,456	$ 153.50
Expired and forfeited	(1,000)	$ 197.50	(1,456)	$ 104.00
Outstanding at June 30	5,000	$ 158.80	6,000	$ 165.25

(1) Adjusted to reflect a 50:1 share consolidation completed on October 1, 2013.

Stock options outstanding are exercisable at prices ranging from $61.50 to $309.00 and at June 30, 2014 had an average remaining contractual life of 1.6 years.

Deferred Share Units - DSUs are granted to non-executive directors of the Company and are issued at the market value of the Company's shares at the date of grant. Vested DSUs are paid out in cash when the participant ceases to be a director, officer or employee.

There were 113,200 DSUs outstanding at June 30, 2014, December 31, 2013 and December 31, 2012. There were no changes to the number of DSUs for the six months ended June 30, 2014 and 2013.

For the three and six months ended June 30, 2014, compensation expense relating to DSUs was $39 and $123 (2013 - $nil and $nil). At June 30, 2014, a liability of $362 (December 31, 2013 - $239) has been accrued with respect to outstanding DSUs.

9 Related Party Transactions

Transactions with key management personnel

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company, directly or indirectly, including directors of the Company.

Compensation expenses related to key management personnel for the three and six months ended June 30, 2014 and 2013 are as follows:

	Three months ended June 30 2014	Three months ended June 30 2013	Six months ended June 30 2014	Six months ended June 30 2013
Salaries and other short-term employee benefits	$ 223	$ 409	$ 469	$ 699

An aggregate of 3,400,000 Subscription Receipts were issued to certain directors and officers of the Company pursuant to the Concurrent Private Placement completed on April 23, 2014, on terms equivalent to the other participants in the Concurrent Private Placement. See note 7 for additional information on the Concurrent Private Placement.

10 Income Taxes

Income taxes are recognized for deferred income taxes attributed to estimated differences between the financial statement carrying values of assets and liabilities and their respective income tax bases.

As the realization of any related tax benefits is not probable, no deferred income tax assets have been recognized for the following:

	June 30, 2014	December 31, 2013
Non-capital loss carry-forwards	$ 50,912	$ 48,234
Capital loss carry-forwards	6,987	6,987
Deductible temporary differences	7,911	6,066
Corporate minimum tax credits	1,406	1,406
Investment tax credits	9,633	9,633

(Currency amounts in thousands of Canadian dollars unless otherwise indicated)

10 Income Taxes (continued)

The unrecognized non-capital losses and investment tax credits will expire at various times to the end of 2034, as follows:

Non-capital losses by year of expiry:		
2026	$	7,883
2027		6,151
2028		9,048
2029		103
2030		610
2031		20,609
2033		3,830
2034		2,678
	$	50,912

Investment tax credits by year of expiry:		
2016	$	961
2017		3,241
2018		888
2019		961
2020		823
2021		643
Beyond 2021		2,116
	$	9,633

The following is a reconciliation of income taxes calculated at the statutory income tax rate to the income tax expense included in the statements of profit or loss and other comprehensive income:

	Three months ended June 30		Six months ended June 30	
	2014	2013	2014	2013
Loss before income tax	$ (2,899)	$ (742)	$ (4,525)	$ (1,314)
Statutory income tax rate	26.5%	26.5%	26.5%	26.5%
Income taxes at statutory income tax rate	(768)	(197)	(1,199)	(349)
Variations due to:				
Unrecognized temporary differences	260	(105)	489	(213)
Unrecognized tax losses	508	302	710	562
Adjustment to prior year provision	-	(4)	-	(124)
Income tax recovery	$ -	$ (4)	$ -	$ (124)

11 Earnings per Share

The Company uses the treasury stock method to calculate diluted earnings per share. Following the treasury stock method, the numerator for the Company's diluted earnings per share calculation remains unchanged from the basic earnings per share calculation, as the assumed exercise of the Company's stock options does not result in an adjustment to profit or loss.

Stock options to purchase 5,000 common shares were outstanding at June 30, 2014 (December 31, 2013 – 6,000). These stock options were excluded in the calculation of diluted earnings per share because the exercise price of the stock options was greater than the weighted average market value of the common shares in the three and six months ended June 30, 2014 and 2013.

12 Capital Management

The Company's capital consists of its shareholders' equity. The Company's objectives when managing capital are to maintain a strong balance sheet and maximize shareholder value. In order to achieve the Company's capital management objectives, it employs a strong and efficient capital base and manages capital in accordance with policies established by the Board of Directors. These policies relate to capital strength, capital mix, dividends and return on capital. The Company has a capital management process in place to measure, deploy and monitor its available capital to assess its adequacy on a continuous basis. Management develops the capital strategy and oversees the capital management processes. Capital is managed using internal metrics. There are no internal or external restrictions on the Company's capital.

13 Risk Management

The Company's statement of financial position at June 30, 2014 consists of short-term financial assets and financial liabilities with maturities of less than one year, other than the site restoration provision discussed in note 5 and the commitments in note 6(c) and 6(d). The most significant identified risks which arise from holding financial instruments include credit risk, market risk and liquidity risk. As at June 30, 2014, the Company's exposure to credit and market risk is nominal as the Company's financial assets consisted of cash and cash equivalents held with a Schedule 1 bank in Canada. Additionally, at June 30, 2014 the Company's financial assets were significantly higher than its financial liabilities resulting in minimal liquidity risk. Overall, the Company has a comprehensive risk management framework to monitor, evaluate and manage the risks assumed in conducting its business.

14 Subsequent Event

On July 29, 2014, the Subscription Receipts were exchanged for 50,995,385 common shares of the Company pursuant to the terms of the Offering and the Concurrent Private Placement when the Escrow Release Conditions were satisfied. Aggregate gross proceeds of the Offering and the Concurrent Private Placement to the Company, before share issuance costs, amounted to $135,138. See note 7 for additional information on the Offering and the Concurrent Private Placement.

On July 31, 2014, the Company completed the Additional Subscription. On closing, the Company issued 5,399,020 common shares of the Company to the Investors at a price of $2.65 per share for aggregate gross proceeds to the Company of $14,307. See note 7 for additional information on the Additional Subscription. The Company was reimbursed US$839 in transaction and related costs incurred in connection with the Additional Subscription.

On July 31, 2014, the Company used a portion of the proceeds from the Offering, the Concurrent Private Placement and the Additional Subscription to purchase Class A Limited Partnership Units in the Partnership and the Partnership (together with funds committed by other investors in the Partnership) completed the Acquisition and the Supplemental Treasury Purchase and acquired 70.8% of HIIG for US$138,683. At closing, the Company was reimbursed $3,156 in transaction and related costs incurred in connection with the Acquisition. The Company's investment in the Partnership at closing was US$75,712, representing a 53.3% ownership interest in the Partnership. See note 4 for additional information on the investment in HIIG.

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