Grant Thornton

Financial Statements

Grand Forks District Savings Credit Union

December 31, 2012

Contents

Grant Thornton

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Independent auditors' report

To the members of Grand Forks District Savings Credit Union:

We have audited the accompanying financial statements of Grand Forks District Savings Credit Union ("the Credit Union"), which comprise the statement of financial position as at December 31, 2012, and the statement of comprehensive income, statement of changes in members' equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Credit Union's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Credit Union's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Grand Forks District Savings Credit Union as at December 31, 2012, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Grant Thornton LLP

Kelowna, BC
March 7, 2013

Chartered accountants

Grand Forks District Savings Credit Union
Statement of financial position
December 31

	2012	2011
Assets		
Cash resources (Note 5)	**$ 29,899,541**	$ 42,571,304
Investments (Note 6)	**15,633,311**	17,126,881
Receivables and prepaid expenses	**413,009**	134,924
Derivative financial instruments (Note 7)	**428,261**	631,092
Loans (Note 8)	**168,374,404**	149,988,878
Property, equipment and intangible asset (Note 10)	**2,493,501**	2,675,498
Income taxes recoverable	**254,113**	-
Deferred income tax asset (Note 14)	**20,758**	-
Total assets	**$ 217,516,898**	$ 213,128,577
Liabilities		
Deposits (Note 11)	**$ 202,729,126**	$ 198,582,365
Payables and other liabilities (Note 12)	**2,100,743**	2,100,367
Income taxes payable	**-**	208,738
Deferred income tax liability (Note 14)	**-**	21,378
Total liabilities	**204,829,869**	200,912,848
Members' equity		
Retained earnings	**12,431,166**	11,662,956
Accumulated other comprehensive income	**255,863**	552,773
Total members' equity	**12,687,029**	12,215,729
	$ 217,516,898	$ 213,128,577

Commitments (Note 22)

Post reporting date events (Note 23)

On behalf of the Board

M Dhutoff Director Theresa Dergousoff Director

Grand Forks District Savings Credit Union
Statement of comprehensive income

Year ended December 31	2012	2011
Financial income		
Loans	$ 7,397,703	$ 7,716,740
Cash resources and investments	1,424,551	1,581,618
	8,822,254	9,298,358
Financial expense		
Deposits	2,513,916	2,881,078
Provision for credit losses, net of recoveries (Note 9)	175,488	29,984
	2,689,404	2,911,062
Financial margin	6,132,850	6,387,296
Other income (Note 16)	1,144,698	1,203,952
Operating margin	7,277,548	7,591,248
Operating expenses (Note 17)	6,328,753	6,466,299
Earnings before income taxes	948,795	1,124,949
Income taxes (Note 14)	180,585	371,377
Net earnings	768,210	753,572
Other comprehensive (loss) income, (net of tax)		
Realized and unrealized (losses) gains on cash flow hedges	(131,813)	539,648
Reclassification of realized gains on cash flow hedges	(102,697)	(56,992)
Unrealized actuarial losses	(62,400)	-
Total other comprehensive (loss) income for the year	(296,910)	482,656
Total comprehensive income for the year	$ 471,300	$ 1,236,228

Grand Forks District Savings Credit Union
Statement of changes in members' equity
Year ended December 31, 2012

	Accumulated other comprehensive income	Retained earnings	Total members' equity
Balance on December 31, 2011	**$ 552,773**	**$ 11,662,956**	**$ 12,215,729**
Net earnings	-	768,210	768,210
Other comprehensive income			
Unrealized losses on cash flow hedges, net of tax	(131,813)	-	(131,813)
Reclassification of realized gains on cash flow hedges, net of tax	(102,697)	-	(102,697)
Unrealized actuarial losses	(62,400)	-	(62,400)
Balance on December 31, 2012	**$ 255,863**	**$ 12,431,166**	**$ 12,687,029**

Grand Forks District Savings Credit Union
Statement of cash flows

Year ended December 31		2012		2011
Increase (decrease) in cash resources				
Operating activities				
Earnings before income taxes	$	**948,795**	$	1,124,949
Adjustments for non-cash items				
Distributions to members		**629,552**		824,000
Depreciation		**368,675**		347,517
Provision for credit losses, net of recoveries		**175,488**		29,984
Gain on cancellation of derivative contract		**(129,997)**		(72,141)
Loss (gain) on disposal of property, equipment and intangible asset		**295**		(1,950)
Unrealized loss (gains) on derivative instruments		**21,285**		(55,390)
Interest received		**7,243,557**		7,813,986
Interest income		**(7,397,703)**		(7,716,740)
Interest paid		**(2,821,194)**		(3,007,027)
Interest expense		**2,513,916**		2,881,078
Income taxes paid		**(623,234)**		(234,680)
Proceeds from cancellation of derivative contract		**-**		202,138
Changes in non-cash operating working capital				
Receivables and prepaid expenses		**(278,085)**		740
Derivatives		**14,694**		-
Loans, net of repayments		**(18,406,868)**		4,287,726
Deposits, net of withdrawals		**4,453,726**		768,983
Payables and other liabilities		**115,150**		12,825
		(13,171,948)		7,205,998
Financing activities				
Patronage distributions paid		**(806,726)**		(990,968)
Addition to equity shares, net		**314**		926
		(806,412)		(990,042)
Investing activities				
Investments		**1,493,570**		(2,266,158)
Purchase of property, equipment and intangible asset		**(188,768)**		(221,991)
Proceeds from disposal of property, equipment and intangible asset		**1,795**		1,950
		1,306,597		(2,486,199)
Net (decrease) increase in cash resources		**(12,671,763)**		3,729,757
Cash resources, beginning of year		**42,571,304**		38,841,547
Cash resources, end of year	**$**	**29,899,541**	$	42,571,304

1. Governing legislation and nature of operations

Grand Forks District Savings Credit Union ('the Credit Union") is incorporated under the Credit Union Incorporation Act of British Columbia and its operations are subject to the Financial Institutions Act of British Columbia. The Credit Union serves members principally in the Boundary Area of British Columbia. The Credit Union's head office is located at 447 Market Avenue, Grand Forks BC.

These financial statements have been approved and authorized for issue by the Board of Directors on March 7, 2013.

2. Summary of presentation and statement of compliance

Basis of presentation

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

These financial statements were prepared under the historical cost convention, as modified by the revaluation of available-for-sale financial assets and derivative financial instruments measured at fair value.

The Credit Union's functional and presentation currency is the Canadian dollar.

The preparation of financial statements in compliance with IFRS requires management to make certain critical accounting estimates. It also requires management to exercise judgment in applying the Credit Union's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 4.

3. Summary of significant accounting policies

Cash resources

Cash resources include cash on hand, deposits with banks, other short-term highly liquid investments which are callable or with original maturities of three months or less; and for the purpose of the statement of cash flows, bank overdrafts that are repayable on demand.

(continued)

3. Summary of significant accounting policies (continued)

Financial instruments

Financial assets and financial liabilities are recognized when the Credit Union becomes a party to the contractual provisions of the financial instrument.

Financial assets are derecognized when contractual rights to the cash flows from the financial asset expire, or when the financial asset and all substantial risks and rewards are transferred.

A financial liability is derecognized when it is extinguished, discharged, cancelled or expires.

Financial assets and financial liabilities are initially measured at fair value plus transactions costs, except for financial assets and financial liabilities carried at fair value through net earnings, which are initially measured at fair value.

Subsequent measurement of financial assets and financial liabilities is as described below.

Financial assets

For the purpose of subsequent measurement, financial assets other than those designated and effective as hedging instruments are classified into the following categories upon initial recognition:

- loans and receivables;
- financial assets at fair value through profit or loss;
- held to maturity investments; and
- available-for-sale financial assets.

The category determines subsequent measurement and whether any resulting income and expense is recognized in net earnings or in other comprehensive income.

At least at each reporting date, all financial assets except for those at fair value through profit or loss are subject to a review for impairment. Financial assets are impaired when there is evidence or events have been identified that affect the value or expected earnings of the financial asset. Different criteria to determine impairment are applied for each category of financial assets, which are described below.

All income and expenses relating to financial assets that are recognized in net earnings are presented within 'financial income' or 'financial expense', except for impairment of trade receivables which is presented within 'other operating and administrative expenses'.

(continued)

3. Summary of significant accounting policies (continued)

Financial instruments (continued)

Loans and receivables

Cash resources and all member loans that are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market have been designated as loans and receivables.

Member loans are initially measured at fair value, net of loan origination fees and inclusive of transaction costs incurred.

Member loans are subsequently measured at amortized cost, using the effective interest rate method, less any impairment.

Member loans are reported at their recoverable amount representing the aggregate amount of principal, less any allowance or provision for credit losses plus accrued interest. Interest for all loans is accounted for on the accrual basis.

If there is objective evidence that an impairment loss on member loans carried at amortized cost has incurred, the amount of the loss is measured as the difference between the loan's carrying amount and the present value of expected cash flows discounted at the loan's original effective interest rate; short-term balances are not discounted.

The Credit Union first assesses whether objective evidence of impairment exists for financial assets that are individually significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, the asset is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognized are not included in a collective assessment of impairment. The expected future cash outflows for a group of financial assets with similar credit risk characteristics are estimated based on historical loss experience.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed. Any subsequent reversal of an impairment loss is recognized in net earnings.

The accounting treatment for loan fees varies depending on the transaction. Significant fees that would result in an adjustment to the overall loan yield are capitalized and amortized using the effective interest method. Mortgage prepayment fees are recognized in other income when received, unless they relate to a minor modification to the terms of the mortgage, in which case the fees are capitalized and amortized over the average remaining term of the original mortgage.

(continued)

3. Summary of significant accounting policies (continued)

Financial instruments (continued)

Bad debts written off
Member loans are written off from time to time as determined by management and approved by the Board of Directors when it is reasonable to expect that the recovery of the debt is unlikely. Bad debts are written off against the allowance for impaired loans, if an allowance for impaired loans had previously been recognized. If no allowance had been recognized, the write offs are recognized as expenses in net earnings.

Held-to-maturity investments
Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturity other than loans and receivables.

Investments are classified as held-to-maturity if the Credit Union has the intention and ability to hold them until maturity. The Credit Union's liquidity term deposits have been classified as held-to maturity investments.

Held-to-maturity investments are measured subsequently at amortized cost using the effective interest method. If there is objective evidence that the investment is impaired, determined by reference to external credit ratings, the financial asset is measured at the present value of estimated future cash flows.

Any changes to the carrying amount of the investment, including impairment losses, are recognized in net earnings.

Available-for-sale financial assets
Available-for-sale financial assets are non-derivative financial assets that are either designated to this category or do not qualify for inclusion in any of the other categories of financial assets. The Credit Union's available-for-sale financial assets include the Credit Union's investments in Central 1 Credit Union ("Central 1"), CUPP Services Ltd., Credential Securities Inc. and Stabilization Central Credit Union.

These investments are measured at cost less any impairment charges, as their fair value cannot currently be estimated reliably. Impairment charges are recognized in net earnings.

Financial liabilities
The Credit Union's financial liabilities include deposits, trade payables, other liabilities and member's shares.

Financial liabilities are measured subsequently at amortized cost using the effective interest method, except for financial liabilities held for trading or designated at fair value through profit or loss, that are carried subsequently at fair value with gains or losses recognized in net earnings.

All interest-related charges are included within the 'deposits' component of financial expense.

(continued)

3. Summary of significant accounting policies (continued)

Financial instruments (continued)

Derivative financial instruments
Derivative financial instruments are accounted for at fair value through profit or loss except for derivatives designated as hedging instruments in cash flow hedge relationships, which requires a specific accounting treatment.

Derivative financial instruments are contracts that are utilized to manage financial risk such as changes in interest rates or other financial indices. The Credit Union uses derivative financial instruments, primarily interest rate swaps, to manage interest rate exposure and applies hedge accounting where applicable.

All derivative financial instruments used for hedge accounting are recognised initially at fair value and reported subsequently at fair value in the statement of financial position.

Hedges
The Credit Union, in accordance with its risk management strategies, enters into various derivative financial instruments to protect itself against the risk of fluctuations in interest rates.

The Credit Union manages interest rate risk through interest rate swaps. These derivatives are carried at fair value and are reported as assets where they have a positive fair value and as liabilities where they have a negative fair value.

Hedge accounting is applied to financial assets and financial liabilities only where all of the following criteria are met:

- At the inception of the hedge there is formal designation and documentation of the hedging relationship and the Credit Union's risk management objective and strategy for undertaking the hedge;
- For cash flow hedges, the hedged item in a forecast transaction is highly probable and presents an exposure to variations in cash flows that could ultimately affect net earnings;
- The effectiveness of the hedge can be reliably measured; and
- The hedge is expected to be highly effective at inception and remains highly effective on each date it is tested. The Credit Union has chosen to test the effectiveness of its hedges on a quarterly basis.

The swap contracts can be designated as fair value hedge instruments or cash flow hedge instruments. The Credit Union has not entered into any fair value hedges at this time.

Cash flow hedges modify exposure to variability in cash flows for variable rate interest bearing instruments or the forecasted assurance of fixed rate liabilities. The Credit Union's cash flow hedges are primarily hedges of floating rate commercial and personal loans.

(continued)

3. Summary of significant accounting policies (continued)

Financial instruments (continued)

Hedges (continued)
For cash flow hedges that meet the hedging documentation criteria, gains and losses resulting from changes in the fair value of the effective portion of the derivative instrument are recorded in other comprehensive income until the hedged item is recognized in net earnings, at which time such change is recognized as interest income. The ineffective portion is recognized immediately in net earnings as interest income.

If the Credit Union closes out its hedge position early, the cumulative gains and losses recognized in other comprehensive income are reclassified from the cash flow ledger reserve within other comprehensive income to net earnings using the effective interest method. The ineffective portion of gains and losses on derivatives used to manage cash flow interest rate risk are recognized in net earnings within interest expense or interest revenue.

If a forecast transaction is no longer expected to occur or if the hedging instrument becomes ineffective, any related gain or loss recognized in other comprehensive income is transferred immediately to net earnings.

Property, equipment and intangible asset

Property and equipment is initially recorded at cost and subsequently measured at cost less accumulated depreciation and accumulated impairment losses, with the exception of land which is not depreciated. Depreciation is recognized in net earnings and is provided on a straight-line basis over the estimated useful life of the assets as follows:

Building	45 years
Building improvements	20 years
External	15 years
HVAC	15 years
Parking lot	12 years
Furniture and fixtures	10 years
Computer equipment	3 years
Systems software	8 years

Depreciation methods, useful lives and residual values are reviewed annually and adjusted if necessary.

Gains or losses arising on the disposal of property and equipment are determined as the difference between the disposal proceeds and the carrying amount of the assets and are recognized in net earnings within ‘other income’ or ‘operating expenses’.

(continued)

3. Summary of significant accounting policies (continued)

Property, equipment and intangible asset (continued)

Intangible assets include systems software used in administration that qualifies for recognition as an intangible asset. Systems software is initially accounted for using the cost model whereby capitalized costs are amortized on a straight-line basis over its contract term of eight years. Residual values and useful lives are reviewed at each reporting date.

Acquired computer software licences are capitalized on the basis of the costs incurred to acquire and install the specific software. Costs associated with maintaining computer software are expensed as incurred.

Impairment of non-financial assets

Non-financial assets are subject to impairment tests whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. Where the carrying value of an asset exceeds its recoverable amount, which is the higher of value in use and fair value less costs to sell, the asset is written down accordingly.

Where it is not possible to estimate the recoverable amount of an individual asset, the impairment test is carried out on the asset's cash-generating unit, which is the lowest group of assets in which the asset belongs for which there are separately identifiable cash flows.

Impairment charges are included in net earnings, except to the extent they reverse gains previously recognized in other comprehensive income

Income taxes

Tax expense recognized in net earnings comprises the sum of deferred tax and current tax not recognised in other comprehensive income or directly in equity.

Current income tax liabilities comprise those obligations to, or claims from, fiscal authorities relating to the current or prior reporting periods, that are unpaid at the reporting date. Current tax is payable on taxable profit, which differs from net earnings in the financial statements. Calculation of current tax is based on tax rates and tax laws that have been enacted or substantively enacted by the end of the reporting period.

Deferred income taxes are calculated using the liability method on temporary differences between the carrying amounts of assets and liabilities and their tax bases.

(continued)

3. Summary of significant accounting policies (continued)

Income taxes (continued)

Deferred tax assets and liabilities are calculated, without discounting, at tax rates that are expected to apply to their respective period of realisation, provided they are enacted or substantively enacted by the end of the reporting period.

Deferred tax assets are recognised to the extent that it is probable that they will be able to be utilised against future taxable income, based on the Credit Union's forecast of future operating results which is adjusted for significant non-taxable income and expenses and specific limits to the use of any unused tax loss or credit. Deferred tax liabilities are always provided for in full.

Deferred tax assets and liabilities are offset only when the Credit Union has a right and intention to set off current tax assets and liabilities from the same taxation authority.

Changes in deferred tax assets or liabilities are recognised as a component of tax recoveries or expense in net earnings, except where they relate to items that are recognised in other comprehensive income (such as the revaluation of land) or directly in equity, in which case the related deferred tax is also recognised in other comprehensive income or equity, respectively.

Deposits

All member deposits are initially measured at fair value, net of any transaction costs directly attributable to the issuance of the instrument.

Member deposits are subsequently measured at amortized cost, using the effective interest rate method.

Post employment benefits and short-term employee benefits

The Credit Union participates in a multi-employer defined benefit pension plan, however, sufficient information is not available to use defined benefit accounting. Therefore, the Credit Union accounts for the plan as if it were a defined contribution plan, recognizing contributions as an expense in the year to which they relate.

The Credit Union participates in a second defined benefit pension plan sponsored by Central 1. The liability recognized in the statement of financial position for the defined benefit plan is the present value of the defined benefit obligation ("DBO") at the reporting date less the fair value of plan assets. The present value of the defined benefit obligation is determined by discounting the estimated future cash flows using interest rates of government bonds that have terms to maturity approximating to the terms of the related pension liability. The defined benefit obligation is determined using the project unit credit method on an annual basis by an independent actuary. The actuarial valuation of plan obligations is dependent upon a series of assumptions, the key ones being price inflation, earnings growth, mortality and investment returns assumptions. Different assumptions could significantly alter the amount of difference between plan assets and obligations, and the pension cost charged to the statement of comprehensive income.

(continued)

3. Summary of significant accounting policies (continued)

Post employment benefits and short-term employee benefits (continued)

Actuarial gains and losses related to the defined benefit pension plan are recorded directly in equity through other comprehensive income as they arise. Post employment benefit expenses are included in 'salaries and benefits'.

Short-term employee benefits
Short-term employee benefits, including holiday entitlement, are current liabilities included in 'payables and other liabilities', measured at the undiscounted amount that the Credit Union expects to pay as a result of the unused entitlement.

Provisions

Provisions are recognized when present obligations as a result of a past event will probably lead to an outflow of economic resources from the Credit Union and amounts can be estimated reliably. Timing or amount of the outflow may still be uncertain. A present obligation arises from the presence of a legal or constructive commitment that has resulted from past events, for example, legal disputes or onerous contracts. Restructuring provisions are recognized only if a detailed formal plan for the restructuring has been developed and implemented, or management has at least announced the plan's main features to those affected by it. Provisions are not recognized for future operating losses.

Provisions are measured at the estimated expenditure required to settle the present obligation, based on the most reliable evidence available at the reporting date, including the risks and uncertainties associated with the present obligation. Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. Provisions are discounted to their present values, where the time value of money is material.

Any reimbursement that the Credit Union can be virtually certain to collect from a third party with respect to the obligation is recognized as a separate asset. However, this asset may not exceed the amount of the related provision.

All provisions are reviewed at each reporting date and adjusted to reflect the current best estimate.

Members' shares

Membership shares are classified as liabilities or as members' equity according to their terms. Where shares are redeemable at the option of the member, either on demand or on withdrawal from membership, the shares are classified as liabilities.

(continued)

3. Summary of significant accounting policies (continued)

Distributions to Members

Patronage distributions on shares classified as liabilities are recognized in net earnings when declared and approved by the Board of Directors.

Revenue recognition

Revenue from the provision of services to members is recognized when earned, specifically when amounts are fixed or can be determined and the ability to collect is reasonably assured.

Foreign currency translation

Foreign currency transactions are translated into the functional currency of the Credit Union using the exchange rates prevailing at the dates of the transactions (spot exchange rate). Foreign exchange gains and losses resulting from the settlement of such transactions and from re-measurement of monetary items at year-end exchange rates are recognized in net earnings.

Standards and interpretations not yet effective

Certain new standards, amendments and interpretations have been published that are mandatory for the Credit Union's accounting periods beginning on or after January 1, 2013 or later periods that the Credit Union has decided not to early adopt. The standards, amendments and interpretations that will be relevant to the Credit Union are:

IFRS 9 Financial Instruments
IFRS 9 is part of phase I of the IASB's wider project to replace IAS 39 *Financial Instruments: Recognition and Measurement*. IFRS 9 deals with classification and measurement of financial assets. The requirements of this standard represent a significant change from the existing requirements in IAS in respect of financial assets. All financial assets that are currently in the scope of IAS 39 will be classified as either amortized cost or fair value. The available for sale, held-to-maturity, and loans and receivables categories will no longer exist. Classification of financial assets is based on an entity's business model for managing the financial assets and their contractual cash flow characteristics. Reclassifications between the two categories are prohibited unless there is a change in the entity's business model.

The standard is effective for annual periods beginning on or after January 1, 2015 with earlier adoption permitted.

(continued)

3. Summary of significant accounting policies (continued)

Standards and interpretations not yet effective (continued)

IFRS 13 Fair Value Measurement
IFRS 13 defines fair value, provides guidance on the measurement of fair value, and requires disclosures about fair value measurements. IFRS 13 does not determine when an asset, a liability or an entity's own equity instrument is measured at fair value. Rather, the measurement and disclosure requirements of IFRS 13 apply when another IFRS requires or permits the item to be measured at fair value (with limited exceptions). The standard is effective for annual periods beginning on or after January 1, 2013 and is required to be applied prospectively.

IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements, IFRS 12 Disclosure of Interests in Other Entities
In May 2011, this IASB introduced IFRS 10 *Consolidated Financial Statements*, which replaces IAS 27 *Consolidated and Separate Financial Statements*, and SIC 12 *Consolidation – Special Purpose Entities*. The new standard defines the principle of control and establishes control as the basis for determining which entities are consolidated in the consolidated financial statements.

Under IFRS 11, which replaces IAS 31 *Interests in Joint Ventures*, the structure of the joint arrangement, although still an important consideration, is no longer the main factor in determining the type of joint arrangement and therefore the subsequent accounting. The new standard eliminates the option to proportionately consolidate interests in certain types of joint ventures.

IFRS 12 brings together into a single standard all the disclosure requirements about an entity's interest in subsidiaries, joint arrangements, associates and unconsolidated structured entities. IFRS 12 requires an entity to disclose information that enables users of financial statements to evaluate the judgments and assumptions made in determining how to classify involvement with another entity; the nature of, and risks associated with, its interests in other entities; and the effects of those interests on its financial position, financial performance and cash flows.

These standards are effective for annual periods beginning on or after January 1, 2013. Early adoption is only permitted if IFRS 10, IFRS 11 and IFRS 12 are applied at the same time.

Certain new standards, amendments and interpretations have been published that are mandatory for the Credit Union's accounting periods beginning on or after January 1, 2013 or later periods that the Credit Union has decided to early adopt.

IFRS 19 Employee Benefits
The Credit Union has early adopted the amendments to IAS 19. The amended standard results in immediate recognition of all estimated changes in the cost of providing defined benefits and all changes in the value of plan assets. The various methods which allowed deferral of some gains or losses under the previous standard have been eliminated. The new standard also results in a new presentation approach that distinguishes the different types of gains and losses arising from defined benefit plans and requires all gains and losses to be presented in net earnings apart from 're-measurements' that are presented in other comprehensive income.

4. Significant management judgments in applying accounting policies and estimation uncertainty

When preparing the financial statements, management undertakes a number of judgments, estimates and assumptions about the recognition and measurement of assets, liabilities, income and expenses.

The effect of a change in an accounting estimate is recognized prospectively by including it in net earnings in the period of the change, if the change affects that period only; or in the period of the change and future periods, if the change affects both. Information about the significant judgments, estimates and assumptions that have the most significant effect on the recognition and measurement of assets, liabilities, income and expenses are discussed below.

Useful lives of depreciable assets

Management reviews the useful lives of depreciable assets at each reporting date. At December 31, 2012, management assesses that the useful lives represent the expected utility of the assets to the Credit Union. The carrying amounts are analyzed in Notes 3 and 10. Actual results, however, may vary due to technical obsolescence, particularly for computer equipment and system software.

Fair value of financial instruments

Management uses valuation techniques in measuring the fair value of financial instruments, where active market quotes are not available. Details of the assumptions used are given in the notes regarding financial assets and liabilities.

In applying the valuation techniques management makes maximum use of market inputs, and uses estimates and assumptions that are, as far as possible, consistent with observable data that market participants would use in pricing the instrument. Where applicable data is not observable, management uses its best estimate about the assumptions that market participants would make.

These estimates may vary from the actual prices that would be achieved in an arm's length transaction at the reporting date.

Member loan loss provision, defined benefit liability and income taxes

Please see Notes 3, 9, 13 and 14 for information regarding member loan loss provision, defined benefit liability and income taxes.

5. Cash resources

The Credit Union's cash and current accounts are held with Central 1. The average yield on the accounts at December 31, 2012 is 2.26% (2011 – 2.30%).

		2012		2011
Cash and current accounts	$	**5,495,895**	$	6,895,074
Term deposits and accrued interest				
Callable or maturing in - three months or less		**2,588,383**		6,178,611
- more than three months		**21,815,263**		29,497,619
	$	**29,899,541**	$	42,571,304

6. Investments

		2012		2011
Term deposits	$	**14,790,191**	$	16,250,515
Shares				
Central 1 Credit Union		**753,579**		791,110
CUPP Services Ltd.		**79,289**		75,004
Credential Securities Inc.		**10,000**		10,000
Stabilization Central Credit Union		**252**		252
	$	**15,633,311**	$	17,126,881

Term deposits can be withdrawn only if there is a sufficient reduction in the Credit Union's total assets or upon withdrawal of membership from Central 1. The liquidity reserves are due within one year. At maturity, these deposits are reinvested at market rates for various terms.

Non-callable term deposits are due between three months and one year. The carrying amounts for deposits approximate their fair value due to having similar characteristics as cash resources.

The shares in Central 1 are required as a condition of membership and are redeemable upon withdrawal of membership or at the discretion of the Board of Directors of Central 1. In addition, the member Credit Unions are subject to additional capital calls at the discretion of the Board of Directors of Central 1.

(continued)

6. Investments (continued)

Central 1 shares are subject to an annual rebalancing mechanism and are issued and redeemable at par value. There is no separately quoted market value for these shares however, fair value is determined to be equivalent to the par value due to the fact transactions occur at par value on a regular and recurring basis.

Dividends on these shares are at the discretion of the Board of Directors of Central 1.

7. Derivative financial instruments

As at December 31, 2012, the Credit Union had entered into interest rate swap contracts for a total of $20 million of notional principal whereby it has agreed to pay at floating interest rates based on Banker's Acceptance rates and receive at fixed interest rates. These swap contracts have fixed interest rates ranging from 2.73% to 2.77% and mature from July 8, 2014 to September 8, 2014. The agreements are secured by a general security agreement covering all assets of the Credit Union.

8. Loans

	2012	2011
Personal loans		
Residential mortgages	**$ 86,674,854**	$ 82,231,864
Other	**20,563,710**	19,054,896
Commercial loans		
Mortgages	**42,767,244**	38,082,834
Other	**3,468,355**	3,669,443
Purchased mortgages	**14,681,021**	6,753,355
Accrued interest	**503,735**	349,590
Deferred loan fees	**(105,950)**	(56,539)
	168,552,969	150,085,443
Allowance for impaired loans (Note 9)	**(178,565)**	(96,565)
	$ 168,374,404	$ 149,988,878

Terms and conditions

Member loans can have either a variable or fixed rate of interest with a maturity date of up to five years.

(continued)

8. Loans (continued)

Terms and conditions (continued)

Variable rate loans are based on a "prime rate" formula, ranging from prime minus 0.5% to prime plus 12%. The Credit Union's prime rate at December 31, 2012 was 3%.

The interest rate offered on fixed rate loans advanced at December 31, 2012 range from 2.79% to 15%.

Residential mortgages are loans and lines of credit secured by residential property and are generally repayable monthly with either blended payments of principal and interest or interest only.

Other personal loans consist of term loans and lines of credit that are non-real estate secured and have various repayment terms. Some of these loans are secured by wage assignments and personal property or investments, and others are secured by wage assignments only.

Commercial loans consist of term loans, operating lines of credit and mortgages to individuals, partnerships and corporations, and have various repayment terms. They are secured by various types of collateral, including mortgages on real property, general security agreements, charges on specific equipment, investments, and personal guarantees.

Average yields to maturity

Loans bear interest at both variable and fixed rates with the following average yields at:

	2012		2011	
	Principal	**Yield**	Principal	Yield
Variable rate	**$ 34,368,450**	**4.23%**	$ 35,078,871	4.29%
Fixed rate due less than one year	**38,203,116**	**4.87%**	36,576,700	5.19%
Fixed rate due between one and five years	**95,583,618**	**4.15%**	78,136,821	4.94%
	$ 168,155,184		$ 149,792,392	

(continued)

8. **Loans** (continued)

Credit quality of loans

It is not practical to value all collateral as at the balance sheet date due to the variety of assets and conditions. A breakdown of the security held on a portfolio basis is as follows:

	2012	2011
Unsecured loans	**$ 1,828,205**	$ 1,845,806
Loans secured by cash, member deposits	**742,963**	1,047,851
Loans secured by other property	**108,680,401**	100,173,415
Residential mortgages insured by government	**37,289,051**	27,570,347
Other	**19,614,564**	19,154,973
	$ 168,155,184	$ 149,792,392

Fair value

The fair value of member loans at December 31, 2012 was $169,519,181 (2011 - $151,865,878).

The estimated fair value of the variable rate loans is assumed to be equal to book value as the interest rates on these loans re-price to market on a periodic basis. The estimated fair value of fixed rate loans is determined by discounting the expected future cash flows at current market rates for products with similar terms and credit risks.

9. Allowance for impaired loans

Total allowance for impaired loan provision:

	2012	2011
Collective provision	**$ 65,018**	$ 58,018
Individual specific provision	**113,547**	38,547
Total provision	**$ 178,565**	$ 96,565

(continued)

9. Allowance for impaired loans (continued)

Change in individual specific provision and collective provision for impairment:

	Beginning balance	Provision (recoveries)	Write-offs	**2012 Ending balance**	2011 Ending balance
Commercial loans	$ 67,420	$ 30,238	$ (38,945)	**$ 58,713**	$ 67,420
Personal loans	29,145	109,780	(19,073)	**119,852**	29,145
Total provision	$ 96,565	$ 140,018	$ (58,018)	**$ 178,565**	$ 96,565
Percentage of total loans, accrued interest and deferred loan fees				**0.11%**	0.06%

In addition to the adjustments to the above noted provisions, during the year $35,470 was directly written off to bad debts expense (2011 - $30,389).

Impaired loans and related allowances	Loan balances	Specific allowance	**2012 Carrying amount**	2011 Carrying amount
Commercial loans	$ 112,427	$ 6,425	**$ 106,002**	$ 96,557
Personal loans	462,696	107,122	**355,574**	21,853
	$ 575,123	$ 113,547	**$ 461,576**	$ 118,410

Key assumptions in determining the allowance for impaired loans collective provision

A collective provision is established to cover estimated loan losses which have not yet been specifically identified as impaired. In determining the allowance for impaired loans, management considers factors such as the composition and credit quality of the portfolio, current economic conditions and trends and historical loss experience.

(continued)

9. Allowance for impaired loans (continued)

Key assumptions in determining the allowance for impaired loans collective provision (continued)

For purposes of the collective provision, loans are classified into separate groups with similar risk characteristics, based on the type of product and type of security. The information below, which details the total non-impaired loan balances by classification as at year end, was used in the calculation of the collective provision.

	2012			
	Residential Mortgage	**Personal**	**Commercial**	**Total**
Balance at December 31, 2012	**$ 85,876,847**	**$ 3,644,500**	**$ 43,670,295**	**$ 133,191,642**

	2011			
	Residential Mortgage	Personal	Commercial	Total
Balance at December 31, 2011	$ 81,918,125	$ 3,488,113	$ 39,116,866	$ 124,523,104

10. Property, equipment and intangible asset

	Property and equipment								Intangible asset	
	Land	Buildings	Building Improvements	External	HVAC	Parking lot	Furniture and fixtures	Computer equipment	System software	Total
Cost										
Balance, December 31, 2011	$ 239,792	$ 1,718,857	$ 278,401	$ 234,319	$ 105,515	$ 37,637	$ 954,281	$ 978,437	$ 805,385	$ 5,352,624
Additions	-	-	38,755	-	-	-	27,584	122,429	-	188,768
Disposals	-	-	-	-	-	-	(6,269)	(70,914)	-	(77,183)
Balance, December 31, 2012	**$ 239,792**	**$ 1,718,857**	**$ 317,156**	**$ 234,319**	**$ 105,515**	**$ 37,637**	**$ 975,596**	**$ 1,029,952**	**$ 805,385**	**$ 5,464,209**
Accumulated depreciation										
Balance, December 31, 2011	$ -	$ 842,665	$ 88,208	$ 50,699	$ 37,809	$ 28,792	$ 509,747	$ 815,202	$ 304,004	$ 2,677,126
Depreciation	-	38,197	13,920	15,621	7,035	2,211	88,477	102,696	100,518	368,675
Disposals	-	-	-	-	-	-	(4,179)	(70,914)	-	(75,093)
pBalance, December 31, 2012	**$ -**	**$ 880,862**	**$ 102,128**	**$ 66,320**	**$ 44,844**	**$ 31,003**	**$ 594,045**	**$ 846,984**	**$ 404,522**	**$ 2,970,708**
Net book value										
December 31, 2011	$ 239,792	$ 876,192	$ 190,193	$ 183,620	$ 67,706	$ 8,845	$ 444,534	$ 163,235	$ 501,381	$ 2,675,498
December 31, 2012	**$ 239,792**	**$ 837,995**	**$ 215,028**	**$ 167,999**	**$ 60,671**	**$ 6,634**	**$ 381,551**	**$ 182,968**	**$ 400,863**	**$ 2,493,501**

11. Deposits

	2012	2011
Term	$ **75,540,625**	$ 80,979,191
Demand	**75,693,407**	67,934,880
Registered savings plans	**41,878,575**	41,706,333
Tax free savings accounts	**8,281,982**	6,320,459
Accrued interest and dividends	**1,040,729**	1,348,008
Membership equity shares (Note 15)	**293,808**	293,494
	$ **202,729,126**	$ 198,582,365

Terms and conditions

Term deposits bear fixed rates of interest for terms of up to five years. Interest can be paid annually, semi-annually, monthly or upon maturity. The historical interest rates offered on term deposits issued at December 31, 2012 range from 0.25% to 5.00%.

Demand deposits are due on demand and bear interest at an interest rate up to 1.5% at December 31, 2012. Interest, where applicable, is calculated daily and paid on the accounts monthly.

The registered savings plan accounts can be fixed or variable rate. The fixed rate accounts have terms and rates similar to the term deposit accounts described above. The variable rate accounts issued at December 31, 2012 bear interest at rates up to 0.80%. Members may make withdrawals from their registered savings plan accounts according to their needs or to satisfy statutory requirements.

Included in demand deposits is an amount of $2,674,281 denominated in United States dollars.

Average yields to maturity

Members' deposits bear interest at both variable and fixed rates with the following average yields at:

	2012		2011	
	Principal	**Yield**	Principal	Yield
Non-interest sensitive	$ **66,629,134**	**0.00%**	$ 59,959,558	0.00%
Variable rate	**14,180,127**	**1.25%**	11,394,454	1.25%
Fixed rate due less than one year	**85,615,735**	**1.54%**	79,786,269	1.65%
Fixed rate due between one and five years	**34,969,593**	**2.08%**	45,800,582	2.72%
	$ **201,394,589**		$ 196,940,863	

(continued)

11. **Deposits** (continued)

Fair value

The fair value of member deposits at December 31, 2012 was $202,678,030 (2011 - $198,869,365).

The estimated fair value of the variable rate deposits is assumed to be equal to book value as the interest rates on these deposits re-price to market on a periodic basis. The estimated fair value of fixed rate deposits is determined by discounting the expected future cash flows at current market rates for products with similar terms and credit risks.

12. Payables and other liabilities

Payables and other liabilities recognized in the statement of financial position can be analyzed as follows:

		2012		2011
Trade payables	$	**514,463**	$	517,187
Accrued payroll liabilities		**915,575**		735,301
Patronage and dividends		**670,705**		847,879
Total payables and other liabilities	$	**2,100,743**	$	2,100,367

All amounts are short-term except for the defined benefit obligations of $601,400 (2011 – $537,800) associated with the pension plans as described in Note 13.

13. Pension plan

The Credit Union makes contributions to BC Credit Union Employees' Pension Plan 1.75% Division, which is a multi-Credit Union plan, on behalf of members of its staff. Central 1 Credit Union's Employee Benefits and Retirement Services administers the plan including the payment of the pension benefits on behalf of employers and employees in accordance with the BC Credit Union Employees' Pension Plan 1.75% Division Rules. The pension is based on years of service, contributions and average earnings at retirement. The plan is accounted for as a defined contribution plan as insufficient information is available to account for the plan as a defined benefit plan. The Credit Union is only one of a number of employers that participates in the plan and the financial information provided to the Credit Union on the basis of the contractual agreements, is usually insufficient to reliably measure the Credit Union's proportionate share in the plan assets and liabilities on defined benefit accounting requirements.

(continued)

13. Pension plan (continued)

Employer contributions to the plan for 2012 were $181,313 (2011 - $169,257). The contributions were made for current service and these have been recognized in net earnings.

As at December 31, 2009 (date of the most recent valuation), the plan actuary reported a total deficit of $34,145,000 which is the responsibility of all Credit Unions participating in the plan. The next actuary report will be as at December 31, 2012 with results expected to be available in mid-2013. Approval has been given by the regulatory body governing the participating Credit Unions to fund any deficit calculated as at December 31, 2012 over a ten year period.

Pensions and other employee obligations

The liabilities recognized for pensions and other employee remuneration consist of the following amounts:

		2012		2011
Non-current:				
Defined benefit plans	**$**	**601,400**	$	537,800
Current:				
Other short term employee obligations	**$**	**314,175**	$	197,501

The current portion of these liabilities represents the Credit Union's obligations to its current and former employees that are expected to be settled during 2013. Other short-term employee obligations arise mainly from accrued holiday entitlement at the reporting date and various pension payments. As none of the employees are eligible for early settlement of pension arrangements, the remaining part of pension obligations for defined benefit plans is considered non-current.

The Credit Union has set up non-pension retiree benefits plans that are available to certain senior workers. According to the plan, a certain percentage of current salary is converted into a pension component each year. Pensions under this scheme are paid out once a beneficiary retires.

The reconciliation of the Credit Union's defined benefit obligations (DBO) and plan assets to the amounts presented on the statement of financial position for each of the reporting periods are presented below:

The details of the Credit Union's DBO are as follows:

		2012		2011
Defined benefit obligation 1 January	**$**	**537,800**	$	536,600
Current service cost		**13,000**		13,000
Interest cost		**26,600**		26,600
Benefits paid		**(38,400)**		(38,400)
Actuarial losses		**62,400**		-
Defined benefit obligation 31 December	**$**	**601,400**	$	537,800
Unfunded	**$**	**601,400**	$	537,800

(continued)

13. Pension plan (continued)

Pensions and other employee obligations (continued)

The DBO was determined using the following actuarial assumptions:

	2012	2011
Discount rate	**4.25%**	5.00%
Expected rate of return on plan assets	**Not applicable**	Not applicable
Expected rate of salary increases	**3%**	3%
Medical cost trend rates	**3%-5%**	3%-5%
Inflationary increases	**2.5%**	2.5%

These assumptions were developed by management with the assistance of independent actuaries. Discount factors are determined close to each year-end by reference to high quality corporate bonds that are denominated in the currency in which the benefits will be paid and that have terms to maturity approximating to the terms of the related pension obligation. Other assumptions are based on management's historical experience.

The estimate of the DBO is particularly sensitive to medical cost trends as well as the discount rates used. If the rates assumed in the actuarial valuation had varied by +/- 1 percent, this would have altered the Credit Union's defined benefit obligation as follows:

	+1%	-1%
Medical/dental trend rates	56,200	(48,000)
Discount rates	(55,600)	66,200

Statement of comprehensive income

The charge to the statement of comprehensive income comprises:

	2012	2011
Employee benefits expense:		
Current service cost	**$ 13,000**	$ 13,000
Interest costs	**26,600**	26,600
Total expenses recognized in net earnings	**$ 39,600**	$ 39,600

All expenses summarized above were included within employee benefits expense.

Amounts recognized in other comprehensive income:

	2012	2011
Unrealized actuarial losses	**$ 62,400**	$ -

(continued)

13. Pension plan (continued)

Statement of comprehensive income (continued)

Expected returns on plan assets are based on a weighted average of expected returns of the various assets in the plan, and include an analysis of historical returns and predictions about future returns. Expected returns on plan assets are estimated by independent pension scheme appraisals undertaken by external valuers in close co-ordination with each fund's treasury board.

Other defined benefit plan information

Based on historical data, the Credit Union expects contributions of approximately $40,400 to be paid for 2013.

14. Income taxes

The significant components of tax expense included in net earnings are composed of:

		2012		2011
Current tax expense				
Based on current year taxable income	**$**	**222,721**	$	274,230
Deferred tax expense				
Origination and reversal of temporary differences		**(40,060)**		91,803
Increase in tax rate		**(2,076)**		5,344
Income taxes	**$**	**180,585**	$	371,377

The significant components of the tax effect of the amounts recognized in other comprehensive income are composed of:

		2012		2011
Current tax				
Change in unrealized gain on derivative instruments	**$**	**(35,039)**	$	162,090
Reclassification of realized gains on derivative instruments		**(27,299)**		(15,150)
Total tax effect of amounts recorded in other comprehensive income	**$**	**(62,338)**	$	146,940

(continued)

14. Income taxes (continued)

Reasons for the difference between tax expense for the year and the expected income taxes based on the statutory tax rate of 38% (2011 – 38%) are as follows:

	2012	2011
Earnings before income taxes	**$ 948,799**	$ 1,124,949
Expected taxes based on the statutory rate of 38%	**$ 360,544**	$ 427,481
Depreciation in excess of capital cost allowance	**40,441**	24,303
Inclusion for loan allowance transitional adjustment	**-**	203,465
Taxable other comprehensive income	**(112,791)**	239,246
Deductible portion of loan allowance	**5,562**	(154,718)
Other	**9,217**	(31,010)
Tax rate reductions	**(122,383)**	(245,423)
Differences on preferential tax rate income	**(20,207)**	(42,174)
Total income tax expense	**160,383**	421,170
Included in other comprehensive income	**62,338**	(146,940)
Current tax expense	**$ 222,721**	$ 274,230

(continued)

14. Income taxes (continued)

The movement in 2012 deferred tax liabilities and assets are:

	Opening balance at January 1, 2012	Recognized in net earnings	**Closing Balance December 31, 2012**
Deferred tax liabilities			
Property, equipment and intangible asset	$ 129,336	$ (6,973)	**$ 122,363**
Deferred tax assets			
Allowance for loan losses	11,154	4,167	**15,321**
Employee future benefits	96,804	30,996	**127,800**
Deferred tax asset	107,958	35,163	**143,121**
Net deferred tax (asset) liability	$ 21,378	$ (42,136)	**$ (20,758)**

	2012	2011
Deferred tax liabilities		
Deferred tax liabilities to be settled within 12 months	**$ -**	$ -
Deferred tax liabilities to be settled after more than 12 months	**122,363**	129,336
Deferred tax assets		
Deferred tax assets to be recovered within 12 months	**20,000**	-
Deferred tax assets to be recovered after more than 12 months	**123,121**	107,958
	143,121	107,958
Net deferred tax (asset) liability	**$ (20,758)**	$ 21,378

15. Members' shares

The Credit Union may issue two classes of shares designated as membership equity of $1 par value.

Membership equity shares
Membership equity shares are a requirement for membership in the Credit Union and are redeemable on withdrawal from membership. Membership shares are non-transferable, voting and have a par value of $1.

Patronage shares
Patronage shares are issued as part of patronage rebates

Membership shares issued and outstanding are included in deposit balances (see Note 12).

Equity shares are not guaranteed by the Credit Union Deposit Insurance Corporation of British Columbia.

During the year, the Credit Union declared patronage distributions of $618,230 (2011 - $809,000) and dividends on membership shares of $11,322 (2011 - $15,000). Total distributions to members are included in operating expenses (Note 17).

16. Other income

	2012	2011
Account service fees	**$ 570,948**	$ 599,263
Foreign exchange	**151,231**	178,113
Insurance commissions and fees	**118,969**	134,016
Loan administration fees	**73,043**	73,631
(Loss) gain on disposal of property, equipment and intangible asset	**(295)**	1,950
Mutual fund fees	**95,547**	103,478
Other	**98,692**	76,177
Safety deposit rentals	**36,563**	37,324
	$ 1,144,698	$ 1,203,952

17. Operating expenses

		2012		2011
Advertising and member relations	**$**	**51,839**	$	56,401
Depreciation		**368,675**		347,517
Community involvement		**90,978**		50,902
Data processing		**554,741**		507,107
Distributions to members		**629,552**		824,000
Dues and assessments		**199,859**		193,744
Human resource development		**43,170**		63,911
Occupancy		**508,317**		544,377
Other		**378,376**		357,153
Phoenix Foundation donation		**100,000**		100,000
Professional fees		**305,786**		367,087
Salaries and benefits		**2,965,290**		2,916,521
Service charges		**132,170**		137,579
	$	**6,328,753**	$	6,466,299

18. Related party transactions

The Credit Union's related parties include key management, as those persons having authority and responsibility for planning, directing and controlling the activities of the Credit Union, including directors and management, post-employment benefit plans for the Credit Union's employees and others as described below. Unless otherwise stated, none of the transactions incorporate special terms and conditions and no guarantees were given or received. Outstanding balances are usually settled in cash.

The Credit Union entered into the following transactions with key management personnel, which are defined by IAS 24 *Related Party Disclosures.*

		2012		2011
Compensation to key management personnel				
Salaries and other short-term employee benefits	**$**	**1,096,938**	$	1,098,561
Total pension and other post-employment benefits		**83,775**		72,764
	$	**1,180,713**	$	1,171,325

		2012		2011
Loans and lines of credit to key management personnel				
Aggregate value of loans and lines of credit advanced	**$**	**5,730,971**	$	3,038,206
Aggregate value of un-advanced loans and lines of credit	**$**	**554,976**	$	708,841

(continued)

18. Related party transactions (continued)

The Credit Union's policy for lending to key management personnel is that all such loans and leases were granted in accordance with normal lending terms.

		2012		2011
Deposits from key management personnel				
Aggregate value of term and savings deposits	**$**	**3,556,934**	$	3,647,225

The Credit Union's policy for receiving deposits from key management personnel is that all transactions are approved and deposits accepted in accordance with the same conditions which apply to Members for each type of deposit.

19. Financial instrument classification and fair values

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities using the last bid price;
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The level in the fair value hierarchy within which the financial asset or financial liability is categorized is determined on the basis of the lowest level of input that is significant to the fair value measurement. Financial assets and financial liabilities are classified in their entirety into only one of three levels.

The only financial instruments carried at fair value were Level 2 derivative financial instruments.

There were no transfers between Level 1 and 2 for the years ended December 31, 2012 and 2011.

20. Financial instrument risk management

General objectives, policies, and processes

The Board of Directors has overall responsibility for the determination of the Credit Union's risk management objectives and policies and, whilst retaining ultimate responsibility for them, it has delegated the authority for designing and operating processes that ensure effective implementation of the objectives and policies to the Credit Union's finance function. The Board of Directors receives quarterly reports from the Credit Union's Controller through which it reviews the effectiveness of the processes put in place and the appropriateness of the objectives and policies it sets.

Credit risk is the risk of loss resulting from the failure of a borrower or counter party to honour its financial or contractual obligation to the Credit Union. Credit risk primarily arises from loans receivable. Management and the Board of Directors reviews and updates the credit risk policy annually. The maximum exposure of the Credit Union to credit risk before taking into account any collateral held is the carrying amount of the loans as disclosed on the statement of financial position.

Concentration of credit risk exists if a number of borrowers are engaged in similar economic activities or are located in the same geographic region, and indicate the relative sensitivity of the Credit Union’s performance to developments affecting a particular segment of borrowers or geographic region. Geographic risk exists for the Credit Union due to its primary service area being the Boundary Area of British Columbia.

Credit risk rating systems are designed to assess and quantify the risk inherent in credit activities in an accurate and consistent manner. To assess credit risk, the Credit Union takes into consideration the member's character, ability to pay, and value of collateral available to secure the loan.

The Credit Union's credit risk management principles are guided by its overall risk management principles. The Board of Directors ensures that management has a framework, and policies, processes and procedures in place to manage credit risks and that the overall credit risk policies are complied with at the business and transaction level.

(continued)

20. Financial instrument risk management (continued)

General objectives, policies, and processes (continued)

The Credit Union's credit risk policies set out the minimum requirements for management of credit risk in a variety of transactional and portfolio management contexts. Its credit risk policies comprise the following:

- General loan policy statements including approval of lending policies, eligibility for loans, exceptions to policy, policy violations, liquidity, and loan administration;
- Loan lending limits including Board of Director limits, schedule of assigned limits and exemptions from aggregate indebtedness;
- Loan collateral security classifications which set loan classifications, advance ratios and amortization periods;
- Procedures outlining loan overdrafts, release or substitution of collateral, temporary suspension of payments and loan renegotiations;
- Loan delinquency controls regarding procedures followed for loans in arrears; and
- Audit procedures and processes for the Credit Union's lending activities.

Credit risk

With respect to credit risk, the Board of Directors receives monthly reports summarizing new loans in total (by category), delinquent loans and overdraft utilization. The Board of Directors also receives an analysis of bad debts and provision for credit losses quarterly.

For the current year, there have been no financial assets that would otherwise be past due or impaired whose terms have been renegotiated.

There have been no significant changes from the previous year in the exposure to risk or policies, procedures and methods used to measure the risk.

Liquidity risk

Liquidity risk is the risk that the Credit Union cannot meet a demand for cash or fund its obligations as they come due. The Credit Union’s management oversees the Credit Union’s liquidity risk to ensure the Credit Union has access to enough readily available funds to cover its financial obligations as they come due. The Credit Union’s business requires such liquidity for operating and regulatory purposes.

(continued)

20. Financial instrument risk management (continued)

Liquidity risk (continued)

The assessment of the Credit Union's liquidity position reflects management's estimates, assumptions and judgments pertaining to current and prospective firm specific and market conditions and the related behaviour of its members and counterparties.

Provincial legislation requires the Credit Union to maintain a prudent amount of liquid assets in order to meet member withdrawals. The Credit Union has set a minimum liquidity ratio of 8% of deposits and borrowings.

The Credit Union manages liquidity risk by:

- Continuously monitoring actual daily cash flows and longer term forecasted cash flows;
- Maintaining adequate reserves, liquidity support facilities and reserve borrowing facilities;
- Monitoring the maturity profiles of financial assets and liabilities; and
- Monitoring the liquidity ratios monthly.

The Board of Directors receives monthly liquidity reports as well as information regarding cash balances in order for it to monitor the Credit Union's liquidity framework. The Credit Union was in compliance with the liquidity requirements throughout the fiscal year.

As at December 31, 2012, the position of the Credit Union is as follows:

	Maximum exposure
Qualifying liquid assets on hand	
Cash	$ 3,713,180
Liquidity reserve deposit	17,181,225
Discount deposits and term deposits	21,500,000
Total liquidity requirement at 8%	(16,218,330)
Excess liquidity requirement	$ 26,176,075

The maturities of liabilities are shown below under market risk. The Credit Union has no material commitments for capital expenditures and there is no need for such expenditures in the normal course of business.

There have been no significant changes from the previous year in the exposure to risk or policies, procedures and methods used to measure the risk.

(continued)

20. Financial instrument risk management (continued)

Market risk

Market risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices. For purposes of this disclosure, the Credit Union segregates market risk into two categories: fair value risk and interest rate risk. The Credit Union is not significantly exposed to currency risk or other price risk.

Fair value risk

Fair value risk is the potential for loss from an adverse movement in the value of a financial instrument. The Credit Union incurs fair value risk on its loans, term deposits and investments held. The Credit Union does not hedge its fair value risk.

Interest rate risk

Interest rate risk relates to the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Credit Union incurs interest rate risk on its loans and other interest bearing financial instruments. At December 31, 2012, the Credit Union had interest rate swap contracts in the total notional principal amount of $20 million. The contracts mature from July 8, 2014 to September 8, 2014. Interest rate swaps involve the exchange of interest flows between two parties on a specified notional principal amount for a pre-determined period at agreed upon fixed and floating rates. Principal amounts are not exchanged and are not indicative of a credit exposure. The Credit Union's goal is to manage the interest rate risk of the statement of financial position to a target level. The Credit Union continually monitors the effectiveness of its interest rate mitigation activities.

The Credit Union's position is measured monthly. Measurement of risk is based on rates charged to clients as well as funds transfer pricing rates.

The Credit Union is exposed to interest rate risk as a consequence of the mismatch, or gap between the assets, liabilities and off balance sheet instruments scheduled to re-price on particular dates. The following table details the Credit Union’s exposure to interest rate risk.

Maturity dates substantially coincide with interest adjustment dates. Amounts with floating interest rates, or due on demand, are classified as maturing within three months, regardless of maturity. Amounts that are not interest sensitive are grouped together, regardless of maturity.

The table below does not incorporate management’s expectation of future events where re-pricing or maturity dates of certain loans and deposits differ significantly from the contractual date.

(continued)

20. Financial instrument risk management (continued)

Market risk (continued)

Interest rate risk (continued)

		Interest sensitive balances in $000's				
	Average Rates	Within 3 months	4 months to 1 year	Beyond 1 year	Not interest sensitive	Total
Assets						
Cash resources	2.26%	$ 7,065	$ 3,000	$ 18,500	$ 1,335	$ 29,900
Loans	4.31%	25,797	27,392	114,966	219	168,374
Other	1.97%	-	2,340	12,279	4,624	19,243
		32,862	32,732	145,745	6,178	217,517
Liabilities						
Deposits	1.13%	21,583	64,196	48,987	67,963	202,729
Other	0.00%	-	-	-	2,101	2,101
		21,583	64,196	48,987	70,064	204,830
Balance sheet mismatch		11,279	(31,464)	96,758	(63,886)	12,687
Derivatives		(20,000)	-	20,000	-	-
Interest sensitivity position 2012		**$ (8,721)**	**$ (31,464)**	**$ 116,758**	**$ (63,886)**	**$ 12,687**
Interest sensitivity position 2011		$ 15,298	$ (22,619)	$ 75,386	$ (55,849)	$ 12,216

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Interest sensitive assets and liabilities cannot normally be perfectly matched by amount and term to maturity. The credit union utilizes interest rate swaps to assist in managing this rate gap. One of the roles of a credit union is to intermediate between the expectations of borrowers and depositors.

An analysis of the Credit Union's risk due to changes in interest rates determined that an increase in interest rates of 1% could result in a decrease to net earnings of $104,872 while a decrease in interest rates of 1% could result in an increase to net earnings of $35,832.

There have been no significant changes from the previous year in the exposure to risk or policies, procedures and methods used to measure the risk.

(continued)

20. Financial instrument risk management (continued)

Currency risk

Currency risk relates to the Credit Union operating in different currencies and converting non Canadian earnings at different points in time at different foreign exchange levels when adverse changes in foreign currency exchange rates occur.

The Credit Union's foreign exchange risk is related to United States dollar deposits. The Credit Union controls its exposure to changes in the United States currency exchange rates by limiting the un-hedged holdings in foreign currency to 0.5% of total assets in accordance with its investment policy. Foreign currency changes are continually monitored by the investment committee for effectiveness of its foreign exchange mitigation activities and holdings are adjusted when offside of the investment policy.

The Credit Union's position is measured monthly. Measurement of risk is based on rates charged to clients as well as currency purchase costs.

For the year-ended December 31, 2012, the Credit Union's exposure to foreign exchange risk is within policy.

There have been no significant changes from the previous year in the exposure to risk or policies, procedures and methods used to measure the risk.

21. Capital requirements and management

The Credit Union requires capital to fund existing and future operations and to meet regulatory capital requirements.

In the management of capital, the Credit Union includes retained earnings, accumulated other comprehensive income, and equity shares totalling $13.0 million (2011 - $12.5 million).

The Credit Union is required under provincial legislation to maintain a minimum capital base equal to 8% of the total risk-weighted value of assets, each asset being assigned a risk factor based on the probability that a loss may be incurred on ultimate realization of that asset.

The Credit Union's current capital base is equal to 18.0% (2011 – 17.5%) of the total value of risk-weighted assets.

The Credit Union employs a Capital Management Plan and a Capital Appreciation Plan that are reviewed by management and the Board of Directors. The Capital Appreciation Plan forecasts the Credit Union's capital position over a five year period.

(continued)

21. Capital requirements and management (continued)

The Capital Management Plan dictates management's approach to growth, loan mix, credit quality, fixed assets, profitability objectives, dividend/patronage rebate policy and has a significant influence on member service objectives. It also establishes the criteria to maintain a cushion beyond the minimum statutory capital requirements. Management and the Board of Directors ensure the Credit Union's Investment and Lending Policy and credit risk profile reflect loan portfolio composition and levels of risk that are consistent with the Credit Union's Capital Management Plan objectives. There has been no change in the overall capital requirements strategy employed during the year ended December 31, 2012.

Management will continue to develop business plans targeting a capital adequacy ratio which exceeds the minimum ratio established by legislation or regulations. Capital adequacy ratio is driven by the risk weighting of the Credit Union's assets. Accordingly, capital adequacy objectives must take into account factors such as loan mix, investment quality and the level of fixed assets. Decisions relating to strategic objectives that impact the risk weighting of the Credit Union's assets are analyzed by management to determine their effect on the Credit Union’s capital adequacy ratio.

22. Commitments

Member loans

The Credit Union has the following commitments to its members at the year-end date on unused lines of credit and letters of credit:

Unused lines of credit	$ 25,743,385
Letters of credit	$ 276,000

In the normal course of business, the Credit Union enters into various off balance sheet commitments such as letters of credit. Letters of credit are not reflected on the balance sheet.

Data processing services

The Credit Union is committed to acquiring online data processing services until November 30, 2016 at an approximate cost of $300,000 per year. Data processing charges are based on the level of equipment and services utilized and on the number of Credit Union members.

(continued)

22. Commitments (continued)

Off balance sheet

Funds under administration

Off balance sheet funds under administration by the Credit Union are comprised of a loan that has been syndicated and administered in its capacity as an agent. Off balance sheet funds are not included in the statement of financial position and have a value at year end as follows:

	2012	2011
Syndicated loans	**$ 457,859**	$ 476,512

23. Post-reporting date events

No adjustment events have occurred between the reporting date and the date of authorization.

During the year, the Credit Union joined two other Credit Unions in forming a separate Wealth Management Company (0948859 B.C. Ltd.). Subsequent to year end, the Credit Union transferred its wealth management business to 0948859 B.C. Ltd. in exchange for one-third ownership. As at December 31, 2012, the fair market value of the Credit Union's wealth management business was not determinable.