

Financial Statements 2010

Independent Auditor's Report

March 16, 2011

To the Members of Cambrian Credit Union Limited

We have audited the accompanying financial statements of Cambrian Credit Union Limited, which comprise the balance sheet as at December 31, 2010 and the statements of net income, comprehensive income and retained earnings, and cash flows for the year then ended, and the related notes including a summary of significant accounting policies.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles, 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.

Auditor's 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 auditor's 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 entity'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 entity'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 in our audit 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 Cambrian Credit Union Limited as at December 31, 2010 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Chartered Accountants
Winnipeg, Canada

Balance Sheet

As at December 31, 2010

(Thousands of Dollars)	2010	2009
ASSETS		
Cash on hand	5,561	5,524
Investments (note 2)	321,812	293,554
Loans outstanding – net of allowance for loss (notes 3 and 4)	1,817,498	1,672,357
Property and equipment (note 5)	16,780	14,051
Other assets (note 6)	2,179	2,314
Future income taxes	553	285
	2,164,383	1,988,085
LIABILITIES		
Savings and deposits (note 7)	2,029,773	1,870,008
Accounts payable and accrued liabilities	6,842	5,534
	2,036,615	1,875,542
MEMBERS' EQUITY		
Shares to be issued (note 8 (b))	390	395
Members' shares (note 9)	9,502	9,519
Retained earnings	117,876	102,629
	127,768	112,543
	2,164,383	1,988,085

See accompanying notes

On behalf of the Board:



Paul Holden, MNRM
Board Chair



Howard Falk, CGA
Audit Committee Chair

Statement of Net Income, Comprehensive Income and Retained Earnings

For the year ended December 31, 2010

(Thousands of Dollars)	2010	2009
Interest income		
Members' loans	77,091	74,287
Investments	4,765	4,095
	81,856	78,382
Interest expense		
Members' deposits	53,263	54,912
Net interest income	28,593	23,470
Other income	17,346	15,846
Net interest and other income	45,939	39,316
Operating expenses		
Salaries and employee benefits	13,574	12,561
Administration	5,315	5,048
Premises	2,969	3,027
Member security (note 11)	1,980	1,109
Organizational (note 11)	1,270	1,100
	25,108	22,845
Income before refunded service fees and income taxes	20,831	16,471
Refunded service fees (note 8(a))	1,802	1,757
Income before income taxes	19,029	14,714
Provision for (recovery of) income taxes (note 13)		
Current	3,781	1,826
Future	(268)	110
	3,513	1,936
Net income and comprehensive income for the year	15,516	12,778
Retained earnings – Beginning of year	102,629	90,122
	118,145	102,900
Dividends – net of \$121 (2009 – \$124) of taxes recoverable (note 8 (b))	(269)	(271)
Retained earnings – End of year	117,876	102,629

See accompanying notes

Statement of Cash Flows

For the year ended December 31, 2010

(Thousands of Dollars)	2010	2009
CASH PROVIDED BY (USED IN)		
Operating activities		
Interest received	82,214	78,749
Interest paid	(54,695)	(54,936)
Payments to suppliers and employees	(23,608)	(21,986)
Other income received	17,346	15,846
Income taxes paid	(2,405)	(2,281)
Cash provided by operating activities	18,852	15,392
Investing activities		
Loans issued	(427,985)	(392,619)
Loans repaid	282,486	267,228
Net loans to members	(145,499)	(125,391)
Increase in investments	(28,258)	(97,595)
Additions to property and equipment	(4,041)	(5,162)
Cash used in investing activities	(177,798)	(228,148)
Financing activities		
Increase in members' savings and deposits	161,197	215,349
Redemption of surplus and common shares	(2,216)	(2,139)
Issuance of common shares – membership	2	3
Cash provided by financing activities	158,983	213,213
Net increase in cash during the year	37	457
Cash on hand – Beginning of year	5,524	5,067
Cash on hand – End of year	5,561	5,524

See accompanying notes

Notes to Financial Statements

December 31, 2010

1. SIGNIFICANT ACCOUNTING POLICIES

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles, which require management to make estimates, and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reported period. Actual results may differ from those estimates.

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

Investments

Contract deposits are classified as held to maturity and are recorded at amortized cost. If the market value of investments becomes lower than cost and this decline in the value is considered to be other than temporary, the investments are written down to market value and recorded in the statement of net income in the period. The Credit Union assesses whether a financial asset is other than temporarily impaired by assessing whether there is a significant or prolonged decline in fair value and objective evidence of impairment exists such as financial difficulty, breach or default of contracts, probability of bankruptcy or other financial reorganization.

Shares of Credit Union Central of Manitoba ("Central") are classified as available for sale and are not actively traded in a quoted market and are accordingly, recorded at cost.

Loans outstanding

Loans outstanding are initially recognized at fair value and are subsequently recorded at amortized cost using the effective interest method of amortization. Loans are stated net of an allowance established to recognize estimated probable losses. A loan is considered non-performing when management has determined that there has been a deterioration in credit quality of the loan and/or the loan is greater than 90 days past due. A loan is considered impaired when the deterioration of credit quality is such that the Credit Union no longer has reasonable assurance of timely collection of the full amount of principal and interest. When a loan is considered impaired, the carrying amount of the loan is reduced to its estimated realizable value. Estimated realizable amounts are determined by estimating the fair value of security underlying the loans and deducting costs of realization. In addition to a specific allowance against identified impaired loans, the Credit Union maintains a non-specific allowance to cover impairment which is inherent in the loan portfolio and is estimated based upon historical loss experience and prevailing economic conditions. Accounts written off reduce the allowance.

Interest revenue on loans is recognized using the effective interest method. Interest is accrued on non-performing loans until such time as it becomes apparent that loan is impaired.

Property held for resale is valued at the lower of cost and estimated net realizable value. At December 31, 2010 there was no property held for sale.

Property and equipment

Property and equipment are recorded at cost. These assets are depreciated on a straight-line basis to the statement of net income at the rates set out below:

Buildings	2.5%
Computer system	10% – 33%
Furniture and fixtures	20%
Security equipment	10%
Leasehold improvements	3.3% – 10%

Income taxes

Income taxes are provided for using the liability method. Under this method, temporary differences are recorded using tax rates anticipated to be in effect when the corresponding taxes will be paid or refunded. Temporary differences are differences between the financial reporting and the income tax bases of the Credit Union's allowance for loss on loans outstanding, and property and equipment.

Translation of foreign currencies

Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the rates prevailing on the balance sheet date. Foreign exchange gains and losses are recorded in Other income.

2. INVESTMENTS

(Thousands of Dollars)	2010	2009
Credit Union Central of Manitoba		
Shares	16,346	16,347
Current account		
Canadian – 1.00%	290,124	266,692
U.S. – 0.15%	15,068	10,241
	321,538	293,280
Credential Securities Inc. debenture, non-interest bearing, repayable in 2020	250	250
Concentra Financial Services Association - shares	24	24
	321,812	293,554

3. LOANS OUTSTANDING

(Thousands of Dollars)	2010	2009
Consumer		
Loans	151,924	137,581
Mortgages	992,750	909,232
Lines of credit	135,238	126,948
Commercial		
Loans	21,132	24,780
Mortgages	489,537	441,606
Lines of credit	29,896	35,067
Accrued interest receivable	2,565	2,923
	1,823,042	1,678,137
Less: Allowance for loss (note 4)	(5,544)	(5,780)
	1,817,498	1,672,357

4. ALLOWANCE FOR LOSS

As at December 31, 2010, the Credit Union has recorded allowances for loss totalling \$5,544,000 (2009 - \$5,780,000), consisting of \$1,848,000 (2009 - \$1,865,000) for specific loans considered impaired and/or non-performing and \$3,696,000 (2009 - \$3,915,000) as a non-specific allowance.

The following schedule provides the total amount of allowance recorded for each major loan category:

(Thousands of Dollars)	2010			2009		
	Gross loan balances	Total allowance	Net loan balances	Gross loan balances	Total allowance	Net loan balances
Non-performing						
Consumer						
Loans	737	354	383	810	350	460
Mortgages	4,082	130	3,952	3,682	36	3,646
Lines of credit	119	111	8	320	120	200
Commercial						
Loans	14	7	7	1,008	51	957
Lines of credit	1,246	1,246	-	2,665	1,308	1,357
	6,198	1,848	4,350	8,485	1,865	6,620
Performing	1,816,844	3,696	1,813,148	1,669,652	3,915	1,665,737
	1,823,042	5,544	1,817,498	1,678,137	5,780	1,672,357

The total allowance for loss consists of:

(Thousands of Dollars)			2010	2009
	Specific allowance	Non-specific allowance	Total	Total
Consumer				
Loans	354	308	662	672
Mortgages	130	2,015	2,145	2,161
Lines of credit	111	275	386	417
Commercial				
Loans	7	43	50	109
Mortgages	–	994	994	1,030
Lines of credit	1,246	61	1,307	1,391
	1,848	3,696	5,544	5,780

The change in the allowance for loss is as follows:

As at December 31, 2010:

(Thousands of Dollars)	Balance – beginning of year	Loans written off in the year	Provision made in the year	Balance – end of year
Consumer				
Loans	350	(99)	103	354
Mortgages	36	–	94	130
Lines of credit	120	(93)	84	111
Commercial				
Loans	51	(44)	–	7
Lines of credit	1,308	–	(62)	1,246
Total specific allowance	1,865	(236)	219	1,848
Non-specific allowance	3,915	–	(219)	3,696
Total allowance	5,780	(236)	–	5,544

As at December 31, 2009:

(Thousands of Dollars)	Balance – beginning of year	Loans written off in the year	Provision made in the year	Balance – end of year
Consumer				
Loans	146	(159)	363	350
Mortgages	30	–	6	36
Lines of credit	79	(58)	99	120
Commercial				
Loans	33	(10)	28	51
Mortgages	–	(7)	7	–
Lines of credit	1,348	–	(40)	1,308
Total specific allowance	1,636	(234)	463	1,865
Non-specific allowance	4,378	–	(463)	3,915
Total allowance for loss	6,014	(234)	–	5,780

The fair value of the collateral held by the Credit Union as security for impaired and/or non-performing loans as at December 31, 2010 was \$4,350,000 (2009 - \$6,620,000). The Credit Union has estimated the fair value of collateral based on an updated assessment of the security appraisal undertaken at the original funding assessment and management's knowledge of the market value of security.

Loans past due but not impaired or non-performing

A loan is considered past due when a counterparty has not made a payment by the contractual due date. The following table presents the carrying value of loans that are past due but not classified as impaired or non-performing because they are either (i) less than 90 days past due, or (ii) fully secured and collection efforts are reasonably expected to result in repayment.

(Thousands of Dollars)	1 – 30 days	31 – 60 days	61 – 89 days	90 days and greater	Total
Consumer					
Loans	5,361	151	120	9	5,641
Mortgages	23,042	367	488	7	23,904
Lines of credit	–	27	5	13	45
Commercial					
Loans	686	–	–	–	686
Mortgages	9,710	–	–	–	9,710
	38,799	545	613	29	39,986

The principal collateral the Credit Union holds as security for loans include (i) insurance, and mortgages over residential lots and properties, (ii) recourse to business assets such as real estate, equipment, inventory and accounts receivable, (iii) recourse to the commercial real estate properties being financed, and (iv) recourse to liquid assets, guarantees and securities. Valuations of collateral are updated periodically depending on the nature of the collateral. The Credit Union has policies in place to monitor the existence of undesirable concentration in the collateral supporting its credit exposure.

The Credit Union has a policy and procedures in place to control the risk that past due loans will be rewritten or extended without the approval of senior management or the Board of Directors (the "Board") of the Credit Union. Loans that are greater than 30 days past due cannot be rewritten without the approval of senior management of the Credit Union. During the year ended December 31, 2010, there was \$23,000 (2009 - \$199,000) in loans greater than 30 days past due that were rewritten on the approval of senior management for the purpose of improving the Credit Union's security position.

During the year ended December 31, 2010, the Credit Union did not acquire any assets in respect of delinquent loans.

5. PROPERTY AND EQUIPMENT

(Thousands of Dollars)	2010		2009	
	Cost	Accumulated depreciation	Cost	Accumulated depreciation
Land	5,091	–	5,091	–
Buildings	7,847	1,478	4,973	1,353
Computer system	11,115	8,603	10,173	7,756
Furniture and fixtures	3,254	2,969	3,232	2,867
Security equipment	838	587	695	566
Leasehold improvements	3,762	1,490	3,762	1,333
	31,907	15,127	27,926	13,875
Net book value		16,780		14,051

Assets acquired but not yet in use totalled \$6,892,000 (2009 - \$4,380,000) as at December 31, 2010. Depreciation expense of \$1,312,000 (2009 - \$1,380,000) is included in administration and premises expenses in the statement of net income, comprehensive income and retained earnings.

6. OTHER ASSETS

(Thousands of Dollars)	2010	2009
Accounts receivable	1,804	1,901
Prepaid expenses	375	413
	2,179	2,314

7. SAVINGS AND DEPOSITS

(Thousands of Dollars)	2010	2009
Chequing accounts	150,645	137,810
Savings accounts	683,204	619,435
Guaranteed Investment Certificates	657,401	619,216
Registered retirement savings and income funds	515,087	468,684
Unclaimed accounts	112	107
Accrued interest	23,324	24,756
	2,029,773	1,870,008

8. REFUNDED SERVICE FEES AND SHARE DIVIDEND

a) Refunded service fees

For 2010, refunded service fees of \$1,802,000 (2009 - \$1,757,000) were paid under the refunded service fees program on qualifying service fees in the year to members having a minimum threshold of business in the Credit Union. The refunded service fees will result in income tax recoveries in the current year of \$541,000 (2009 - \$553,000).

b) Share dividend

In respect to 2010, the Board has declared a 4.50% (2009 - 4.50%) dividend on existing common and surplus shares. The entire amount of the dividend of \$390,000 (2009 - \$395,000) will be used in 2010 to purchase surplus shares under the Credit Union's member equity plan. The share dividend will result in income tax recoveries in the current year of \$121,000 (2009 - \$124,000).

9. MEMBERS' SHARES

Each member of the Credit Union has one vote, regardless of the number of shares a member holds. Each member must purchase and hold one or more common shares. At December 31, 2010, the number of members was 54,798 (2009 - 54,442).

Authorized share capital

a) Common shares

Authorized common share capital consists of an unlimited number of common shares with an issue price of \$5 and an unlimited number of common shares issued under the refunded service program with an issue price of \$0.01.

b) Surplus shares

Authorized surplus shares consist of an unlimited number of surplus shares, with an issue price of \$1.

Issued share capital

(Thousands of Dollars)	2010	2009
Surplus share capital		
Beginning of year	8,299	8,159
Issued during the year (previous year's share dividends) (note 8 (b))	395	500
Redemption of surplus shares	(389)	(360)
End of year	8,305	8,299
Common share capital		
Beginning of year	1,220	1,239
Issued on application for membership	2	3
Issued based on Refunded Service Fee Program (note 8 (a))	1,802	1,757
Redemption of common shares	(1,827)	(1,779)
End of year	1,197	1,220
Total share capital	9,502	9,519

The Board approved a special redemption of surplus shares in the amount of \$170,000 (2009 - \$141,000) which, together with regular redemptions of \$219,000 (2009 - \$219,000) comprised surplus shares redeemed during the year of \$389,000 (2009 - \$360,000).

The common share redemption of \$1,827,000 (2009 - \$1,779,000) consists of redemption of \$1,802,000 (2009 - \$1,757,000) of common shares under the refunded service fee program and \$25,000 (2009 - \$22,000) of regular redemptions.

Redemptions of share capital amounted to \$2,216,000 (2009 - \$2,139,000).

10. CAPITAL DISCLOSURES

The Credit Union operates pursuant to the Credit Unions and Caisses Populaires Act (Manitoba) (the “Act”). Regulations to the Act establish the following requirements with respect to capital and liquidity reserves:

Capital requirements

The Credit Union shall maintain a level of capital, which is comprised of members’ equity that meets or exceeds the following requirements:

- a) its capital shall not be less than 5% of the book value of its assets;
- b) its retained earnings shall not be less than 3% of the book value of its assets; and
- c) a tiered level of capital shall not be less than 8% of the risk weighted value of its assets.

The Credit Union is in compliance with the capital requirements at December 31, 2010.

Liquidity reserve

The Credit Union shall maintain in cash on hand and investments in Central not less than 8% of its total members’ savings and deposits.

The Credit Union is in compliance with the liquidity reserve requirements at December 31, 2010.

Capital and liquidity reserves are managed in accordance with policies established by the Board and in relation to the capital requirements above. Management regards a strong capital base as an integral part of the Credit Union’s strategy. All of the capital requirements are monitored throughout the year, and modifications to the capital management strategies are made as appropriate. The Credit Union makes periodic dividend payments on eligible member shares, within the context of its overall capital management plan.

11. TRANSACTIONS WITH RELATED PARTIES, THE DEPOSIT GUARANTEE CORPORATION OF MANITOBA AND CENTRAL

Directors, management and employees

All transactions with the Credit Union's directors, management and employees were in accordance with the statutes, by-laws and policies of the Credit Union. Outstanding loans to directors and employees as at December 31, 2010 were 0.9% (2009 - 0.8%) in aggregate of the assets of the Credit Union.

The Deposit Guarantee Corporation of Manitoba

The Deposit Guarantee Corporation of Manitoba ("Deposit Guarantee Corporation") was incorporated for the purpose of protecting the members of credit unions from financial loss in respect of their deposits with credit unions and to establish sound procedures and controls for credit unions. The Deposit Guarantee Corporation provides a safeguard of all savings and deposits of members of Manitoba credit unions.

Transactions with the Deposit Guarantee Corporation included assessments of \$1,810,000 (2009 - \$956,000) and are recorded as member security expense.

Central

The Credit Union is a member of Central, which acts as a depository for surplus funds, and makes loans to credit unions. Central also acts as a trade association for credit unions.

The Credit Union has in place a line of credit with Central in the amount of 10% of member deposits. It was not utilized at December 31, 2010. The line of credit with Central is payable on demand with interest payable on a variable rate basis which at year-end was 3.00% (2009 - 2.77%). As collateral for the line of credit, the Credit Union has pledged its loans outstanding. Interest paid on borrowings from Central during the year amounted to nil (2009 - nil).

Other transactions with Central included income earned on investments referred to in note 2 in the amount of \$4,763,000 (2009 - \$4,095,000) and fees assessed by Central which include annual affiliation dues in the amount of \$836,000 (2009 - \$785,000), recorded as organizational expenses.

12. OBLIGATIONS UNDER OPERATING LEASES

Under the terms of premises leases, the Credit Union is committed to future aggregate lease payments as follows:

(Thousands of Dollars)	
2011	815
2012	612
2013	591
2014	576
2015	433
Thereafter	6,141
	9,168

13. INCOME TAX RATE

At current levels of income, the Credit Union is subject to a tax rate of approximately 18% (2009 - 13%).

14. RISK MANAGEMENT

The Credit Union's risk management policies are designed to identify and analyse risks, to set appropriate risk limits and controls, and to monitor the risks and adherence to limits by means of reliable and up-to-date information systems. The Credit Union follows an enterprise risk management framework which involves identifying particular events or circumstances relevant to its objectives, assessing them in terms of probability and magnitude, determining a response strategy and monitoring progress. The Credit Union regularly reviews its risk management policies and systems to take account of changes in markets and products.

Risk management is carried out by management who reports to the Board. The Board provides written principles for risk tolerance and overall risk management. Management reports to the Board on the Credit Union's compliance with the risk management policies. In addition, the Credit Union maintains a Risk Management department, which is responsible for the review of risk management and the Credit Union's control environment.

Financial instruments comprise the majority of the Credit Union's assets and liabilities. The Credit Union accepts deposits from members at both fixed and floating rates for various periods and seeks to earn an interest rate margin by investing these funds in high quality financial instruments - principally loans and mortgages. The primary types of financial risk which arise from this activity are interest rate risk, credit risk, liquidity risk, foreign exchange risk and price risk.

The following table describes the significant financial instrument activity undertaken by the Credit Union, the risks associated with such activities and the types of method used in managing those risks.

ACTIVITY	RISKS	METHOD IN MANAGING RISKS
Savings and deposits	Sensitivity to changes in interest rates	Asset-liability matching and periodic use of derivatives
Investments	Sensitivity to changes in interest rates and credit risk	Monitoring of investment restrictions and counterparty risk
Loans to members	Sensitivity to changes in interest rates and credit risk	Asset-liability matching and periodic use of derivatives, and monitoring of counterparty risk

Interest rate risk

Cash flow interest rate risk is the risk that the future cash flows of the Credit Union's financial instruments will fluctuate due to changes in market interest rates. Fair value interest rate risk is the risk that the value of a financial instrument will fluctuate because of changes in prevailing market interest rates. Net interest income reported in the statement of net income, comprehensive income and retained earnings may increase or decrease in response to changes in market interest rates. Accordingly, the Credit Union sets limits on the level of mismatch of interest rate re-pricing that may be undertaken, which is monitored by the Credit Union's management and reported to the Board, which is responsible for managing interest rate risk.

In managing interest rate risk, the Credit Union relies primarily upon use of asset-liability and interest rate sensitivity models. Periodically, the Credit Union may enter into interest rate swaps to adjust the exposure to interest rate risk by modifying the re-pricing of the Credit Union's financial instruments. The Credit Union has not entered into any interest rate swaps in the current or prior year.

Sensitivity analysis is used to assess the change in value of the Credit Union's financial instruments against a range of incremental basis point changes in interest rates over a twelve month period. Sensitivity analysis is calculated on a periodic basis and is reported to the Board. Based on current portfolio of loans and deposits as at December 31, 2010, the Credit Union estimates that an immediate and sustained 100 basis point increase in interest rates would decrease net interest income by \$418,000 over the next twelve months while an immediate and sustained 100 basis point decrease in interest rates would increase net interest income by \$200,000 over the next twelve months.

Other types of interest rate risk may involve basis risk (the risk of loss arising from changes in the relationship of interest rates which may not have identical characteristics, for example the difference between prime rate and variable rate loans and variable rate deposits) and prepayment risk (the risk of loss of interest income arising from the early repayment of fixed rate mortgages and loans). These risks are also monitored on a regular basis and are reported to the Board.

The following schedule shows the Credit Union's sensitivity to interest rate changes as at December 31, 2010:

(Thousands of Dollars)					
Expected re-pricing or maturity dates	Assets	Interest rate %	Liabilities and equity	Interest rate %	Asset liability gap
Variable to 6 months	900,226	2.88	963,572	1.93	(63,346)
6 months to 1 year	89,441	4.86	212,590	3.69	(123,149)
1 to 2 years	201,189	5.19	283,382	4.22	(82,193)
2 to 3 years	215,641	5.05	203,693	4.41	11,948
3 to 4 years	322,480	4.57	89,690	3.69	232,790
4 to 5 years	403,651	4.26	106,612	3.54	297,039
Over 5 years	9,387	4.16	144	3.45	9,243
	2,142,015		1,859,683		282,332
Non-interest rate sensitive	22,368	0.00	304,700	0.03	(282,332)
Total	2,164,383		2,164,383		–

The Credit Union's major source of income is its financial margin, which is the difference between income earned on investments and loans to members and interest paid to members on their deposits. The objective of asset liability management is to match interest-sensitive assets with interest-sensitive liabilities, thus controlling wide fluctuations of income during periods of changing interest rates. Certain items on the balance sheet, such as non-interest bearing member deposits and equity do not provide interest rate exposure to the Credit Union. These items are reported as non-interest rate sensitive on the schedule. The Credit Union may enter into interest rate swap contracts when its portfolio is mismatched.

Credit risk

Credit risk is the risk that a Credit Union member or counterparty will be unable to pay amounts in full when due. Impairment provisions are provided for losses that have been incurred at the balance sheet date. Significant changes in the economy of Manitoba or deteriorations in lending sectors which represent a concentration within the Credit Union's loan portfolio may result in losses that are different from those provided for at the balance sheet date. Credit risk management is an integral part of the Credit Union's activities. Management carefully monitors and manages the Credit Union's exposure to credit risk by a combination of methods. Credit risk arises principally from lending activities that result in member loans and advances, and investing activities that result in investments in cash resources. There is also credit risk in unfunded loan commitments. The overall management of credit risk is reported to Board.

Concentration of loans is managed by the implementation of sectoral and member specific limits as well as the periodic use of syndications with other financial institutions to limit the potential exposure to any one member.

The Board is responsible for approving and monitoring the Credit Union's tolerance for credit exposures which it does through review and approval of the Credit Union's lending policies and through setting limits on credit exposures to individual members and across sectors. The Credit Union maintains levels of borrowing approval limits and prior to advancing funds to a member, an assessment of the credit quality of the member is made. The Credit Union emphasises responsible lending in its relationships with members and to establish that loans are within the member's ability to repay, rather than relying exclusively on collateral.

The classes of financial instruments to which the Credit Union is most exposed are loans to members and investments.

At December 31, 2010, the maximum credit risk exposure of the Credit Union, without taking account of any collateral or other credit enhancements was as follows:

(Thousands of Dollars)			
Credit risk exposure	Outstanding	Undrawn commitments	Total exposure
Investments	321,812	–	321,812
Consumer			
Loans	151,924	–	151,924
Mortgages	992,750	20,853	1,013,603
Lines of credit	135,238	184,703	319,941
Commercial			
Loans	21,132	200	21,332
Mortgages	489,537	46,797	536,334
Lines of credit	29,896	69,072	98,968
Letters of credit	–	2,788	2,788
Total exposure	2,142,289	324,413	2,466,702

Investments

Credit risk arises from the investments in cash resources held by the Credit Union to meet regulatory and internal liquidity requirements and for general business purposes. This aspect of credit risk is principally managed by management who reports to the Board. The managed assets consist of cash resources held with Central. All of the Credit Union's liquidity investments are held with Central. Central invests on behalf of the Credit Union as per the investment policies approved by the Investment Committee of the Board of Directors of Central. The investment policy requires that all investments are highly-rated and that all of the assets are readily convertible to cash.

Personal loans and residential mortgages

Loans to members consist of personal loans and lines of credit which are secured by various types of collateral as required in the loans policy approved by the Board. Unsecured personal loans are only granted on the basis of a properly qualified and documented covenant value.

Residential mortgages to members, consist of \$351,158,000 (2009 - \$322,989,000) in mortgages with an advance ratio of 80% to 95% of the appraised value which are fully insured by either the Canadian Mortgage Housing Corporation or Genworth Capital, \$639,346,000 (2009 - \$583,791,000) in conventional residential mortgages with an original maximum advance ratio to 80% of the appraised value and \$2,246,000 (2009 - \$2,453,000) in residential mortgages with an original advance ratio to 85% of the appraised value.

Commercial loans and lines of credit

The Credit Union often takes security as collateral in common with other lending institutions. The Credit Union maintains guidelines on the acceptability of specific types of collateral. Collateral may include mortgages over commercial properties and charges over business assets such as premises, inventory and accounts receivable. Where significant impairment indicators are identified, the Credit Union will take additional measures to manage the risk of default, which may include seeking additional collateral.

The Credit Union has established guidelines to ensure that the Credit Union's commercial lending is well diversified by industry type, as follows:

(Thousands of Dollars)	2010	2009
Commercial rental	222,302	226,757
Residential rental	145,860	111,203
Health care	43,756	40,617
Accommodation and food services	18,989	25,986
Retail	15,917	17,856
Construction	7,543	10,456
Entertainment and recreation	10,496	8,970
Other	75,702	59,608
	540,565	501,453

The credit quality of the commercial loan portfolio for those loans which are neither past due or impaired can be assessed by reference to the Credit Union's internal rating system. The Credit Union assesses the probability of a default using internal rating tools and taking into account statistical analysis as well as the experience and judgement of the Credit department. Commercial loans to members are divided into eight segments and are regularly reviewed and updated as appropriate. Loans in the lower segments are not considered to be impaired taking into account the repayment status of the loans and the estimated fair value of the collateral.

(Thousands of Dollars)	2010	2009
Rating 1 – Excellent risk	5,109	3,236
Rating 2 – Very good risk	168,913	106,853
Rating 3 – Good risk	222,361	253,831
Rating 4 – Acceptable risk	118,730	122,512
Rating 5 – Caution risk	24,192	11,348
Rating 6 – At risk	–	–
Rating 7 – Impaired with no loan loss allowance	–	–
Rating 8 – Impaired with loan loss allowance	1,260	3,673
	540,565	501,453

Liquidity risk

Liquidity risk is the risk that the Credit Union will encounter difficulty in raising funds to meet its obligations to members and other liabilities. As disclosed in note 10, the Credit Union is required to maintain in cash on hand and investments in Central not less than 8% of its total members' savings and deposits. The Credit Union's own risk management policies require it to maintain sufficient liquid resources to cover cash flow imbalances, to retain member confidence in the Credit Union and to enable the Credit Union to meet all financial obligations. This is achieved through maintaining a prudent level of liquid assets, through management control of the growth of the loan portfolio, and asset-liability maturity management. Management monitors forecasts of the Credit Union's liquidity requirements on the basis of expected cash flows as part of its liquidity management. The Credit Union also maintains a borrowing facility with CUCM in the amount of 10% of member deposits as part of its liquidity management strategy.

The contractual maturity of recognized financial assets and liabilities is as follows:

(Thousands of Dollars)	Payable on a fixed date					Total
	On demand	Less than 1 year	1 to 2 years	2 to 5 years	More than 5 years	
Cash on hand	5,561	–	–	–	–	5,561
Investments	305,192	–	–	–	16,620	321,812
Loans outstanding	488,097	177,055	201,188	941,770	9,388	1,817,498
Accounts receivable	–	1,804	–	–	–	1,804
Total financial assets	798,850	178,859	201,188	941,770	26,008	2,146,675
Savings and deposits	900,866	445,383	283,382	399,998	144	2,029,773
Accounts payable and accrued liabilities	–	6,842	–	–	–	6,842
Total financial liabilities	900,866	452,225	283,382	399,998	144	2,036,615

Foreign exchange risk

Foreign exchange risk is not considered significant at this time as the Credit Union does not engage in any active trading of foreign currency positions or hold significant foreign currency denominated financed investments for an extended period.

Price risk

Price risk arises from changes in market risks, other than interest rate, credit, liquidity or foreign exchange risk, causing fluctuations in the fair value or future cash flows of a financial instrument. Price risk is not considered significant at this time.

15. FAIR VALUE OF FINANCIAL INSTRUMENTS

Differences between book value and fair value of the investments, loans outstanding, savings and deposits, and other financial assets and liabilities are caused by differences between the interest rate obtained at the time of the original investment, loan or deposit and the current rate for the same product. Loans and deposits that are priced with variable rates have a fair value equal to book value, as they are priced at current interest rates.

While fair value amounts are designed to represent estimates of the amounts at which assets and liabilities could be exchanged in a current transaction between arm's length willing parties, the Credit Union normally holds all of its fixed term investments, loans and deposits to their maturity date. Consequently, the fair values presented are estimates derived by taking into account changes in the market interest rates and may not be indicative of the net realizable value. Furthermore, as many of the Credit Union's financial instruments lack an available trading market, the fair value of loans and member deposits with fixed rates are estimated using discounted cash flow models with discount rates based on current market interest rates for similar types of instruments. The inputs to the valuation model for fixed rate loans include scheduled loan amortization rates and estimated rates of repayment with the future cash flows discounted using current market rates for equivalent groups of mortgages or loans. The future cash flows on fixed rate deposits and fixed rate borrowings are discounted to their estimated present value using a discount rate based on current market rates for equivalent groups of fixed rate deposits.

The most significant assumption relates to the discount rates utilized. If the forward yield curve of such instruments would increase by 100 basis points then the fair value of loans outstanding and investments would decrease by approximately \$35,963,000 and the fair value of savings and deposits would increase by approximately \$16,780,000. A corresponding decrease of 100 basis points would result in the fair value of loans outstanding and investments increasing by approximately \$37,426,000 and the fair value of savings and deposits decreasing by approximately \$16,411,000.

The fair values disclosed exclude the values of assets and liabilities that are not considered financial instruments such as land, buildings and equipment.

Financial assets and liabilities are recognized on the balance sheet at fair value, cost or amortized cost according to the categories determined by the accounting framework for financial instruments. The carrying values and fair values for each category of financial asset and liability are presented in the following table:

As at December 31, 2010:

(Thousands of Dollars)	Held for trading	Financial assets and financial liabilities at cost or amortized cost	Estimated fair value	Fair value greater (less) than book value
Assets				
Cash on hand	5,561	–	5,561	–
Investments	–	321,812	321,812	–
Loans outstanding	–	1,817,498	1,843,474	25,976
Accounts receivable	1,804	–	1,804	–
Total financial assets	7,365	2,139,310	2,172,651	25,976
Liabilities				
Savings and deposits	–	2,029,773	2,009,410	(20,363)
Accounts payable and accrued liabilities	–	6,842	6,842	–
Total financial liabilities	–	2,036,615	2,016,252	(20,363)

As at December 31, 2009:

(Thousands of Dollars)	Held for trading	Financial assets and financial liabilities at cost or amortized cost	Estimated fair value	Fair value greater (less) than book value
Assets				
Cash on hand	5,524	–	5,524	–
Investments	–	293,554	293,554	–
Loans outstanding	–	1,672,357	1,701,528	29,171
Accounts receivable	1,901	–	1,901	–
Total financial assets	7,425	1,965,911	2,002,507	29,171
Liabilities				
Savings and deposits	–	1,870,008	1,807,213	(62,795)
Accounts payable and accrued liabilities	–	5,534	5,534	–
Total financial liabilities	–	1,875,542	1,812,747	(62,795)

16. PENSION PLAN

The Credit Union has a defined contribution pension plan for qualifying employees. The contributions are held in trust by the Co-operative Superannuation Society Limited and are not recorded in these financial statements. The Credit Union matches employee contributions at a rate of 6% of the employee salary. The expense and payments for the year ended December 31, 2010 were \$628,000 (2009 - \$583,000) and are recorded as salaries and employee benefits. As a defined contribution pension plan, the Credit Union has no further liability or obligation for future contributions to fund benefits to plan members.

17. COMPARATIVE FIGURES

Certain of the prior year's figures have been reclassified to conform to the current year's presentation of the financial statements.